

Edgar Filing: HERCULES INC - Form 10-K/A

HERCULES INC  
Form 10-K/A  
December 13, 2002

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D. C. 20549

FORM 10-K/A

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

For the fiscal year ended December 31, 2001

Commission file number 1-496

-----  
HERCULES INCORPORATED

A DELAWARE CORPORATION  
I.R.S. EMPLOYER IDENTIFICATION NO. 51-0023450  
HERCULES PLAZA  
1313 NORTH MARKET STREET  
WILMINGTON, DELAWARE 19894-0001  
TELEPHONE: 302-594-5000

Securities registered pursuant to Section 12(b) of the Act (Each class is registered on the New York Stock Exchange, Inc.)

Title of each class  
-----

Common Stock (\$25/48 Stated Value)  
8% Convertible Subordinated Debentures due August 15, 2010  
9.42% Trust Originated Preferred Securities (\$25 liquidation amount),  
issued by Hercules Trust I and guaranteed by Hercules Incorporated  
Preferred Share Purchase Rights

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements in Part III of this Form 10-K/A or any amendment to this Form 10-K/A.  
X

As of March 15, 2002, registrant had 109,157,515 shares of common stock, \$25/48 stated value ("Common Stock") outstanding, which is registrant's only class of common stock.

The aggregate market value of registrant's Common Stock held by non-affiliates based on the closing price on March 15, 2002 was approximately \$1.3 billion.

DOCUMENTS INCORPORATED BY REFERENCE  
(SPECIFIC PAGES INCORPORATED ARE IDENTIFIED UNDER THE APPLICABLE ITEM HEREIN.)

# Edgar Filing: HERCULES INC - Form 10-K/A

## EXPLANATORY NOTE

This amendment to Hercules Incorporated's Annual Report on Form 10-K for the year ended December 31, 2001 filed with the Securities and Exchange Commission on March 29, 2002 is being filed to amend Part II, Item 8, Financial Statements and Supplementary Data, to add the recently completed audited financial statements of certain subsidiaries and to add Exhibits 23.1 to 23.18, Consents of PricewaterhouseCoopers LLP.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA:

### INDEX TO REQUIRED SUPPLEMENTARY DATA HERCULES INCORPORATED

#### SUBSIDIARY FINANCIAL STATEMENTS

Aqualon Company.....	1
BetzDearborn Inc. ....	15
BetzDearborn Canada, Inc. ....	35
BetzDearborn Europe, Inc. ....	56
BetzDearborn International, Inc. ....	76
BL Technologies, Inc. ....	97
FiberVisions A/S.....	106
FiberVisions Incorporated.....	122
FiberVisions L.L.C. ....	138
FiberVisions Products, Inc. ....	156
Hercules Canada, Inc. ....	170
Hercules Chemicals (Taiwan) Co., Limited.....	180
Hercules Credit, Inc. ....	205
Hercules GB Holdings Limited.....	220
Hercules International Limited.....	237
Hercules Investments Sarl.....	259
WSP, Inc.....	279

#### REPORT OF INDEPENDENT ACCOUNTANTS

TO THE SHAREHOLDERS AND THE BOARD OF DIRECTORS OF  
HERCULES INCORPORATED  
WILMINGTON, DELAWARE

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income and of cash flows present fairly, in all material respects, the financial position of Aqualon Company, a subsidiary of Hercules Incorporated, and its subsidiaries at December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting

## Edgar Filing: HERCULES INC - Form 10-K/A

principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP  
Philadelphia, Pennsylvania  
November 4, 2002

1

### AQUALON COMPANY CONSOLIDATED STATEMENTS OF INCOME

	(Dollars in thousands)		
	Year Ended December 31,		
	2001	2000	1999
	----	----	----
Sales to third parties	\$ 255,285	\$ 274,775	\$ 295,000
Sales to Hercules Group	49,359	63,033	62,000
	-----	-----	-----
	304,644	337,808	358,000
Cost of sales third parties	204,127	227,272	250,000
Selling, general, and administrative expenses	48,119	48,069	53,000
Research and development	12,708	11,780	12,000
Goodwill and intangible asset amortization	1,014	1,014	1,000
Other operating (income) expense, net (Note 11)	(2,129)	22,259	3,000
	-----	-----	-----
Profit from operations	40,805	27,414	37,000
Interest and debt expense	56	415	
Other (income) expense, net	(1,091)	(1,199)	
	-----	-----	-----
Net income	\$ 41,840	\$ 28,198	\$ 36,000
	=====	=====	=====

The accompanying accounting policies and notes are an integral part of the consolidated financial statements.

2

### AQUALON COMPANY CONSOLIDATED BALANCE SHEETS

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousands)	
	December 31,	
	2001	2000
	----	----
ASSETS		
Current assets		
Cash and cash equivalents	\$ 5,534	\$ 2,494
Accounts receivable, net (Note 3)	30,924	35,743
Notes receivable (Note 4)	--	3,600
Inventories (Note 5)	39,340	45,409
Other current assets	4,205	4,691
	-----	-----
Total current assets	80,003	91,937
	-----	-----
Property, plant, and equipment, net (Note 7)	94,338	91,742
Notes receivable (Note 4)	3,000	3,000
Goodwill, net (Note 8)	27,536	28,550
Deferred charges and other assets	3,141	5,256
	-----	-----
Total assets	\$208,018	\$220,485
	=====	=====
LIABILITIES AND NET PARTNERS' (HERCULES GROUP) INVESTMENT		
Current liabilities		
Accounts payable	\$ 14,354	\$ 17,724
Accrued expenses (Note 7)	25,224	24,172
	-----	-----
Total current liabilities	39,578	41,896
	-----	-----
Pension and other postretirement benefits (Note 10)	--	110
Environmental and other liabilities	19,663	22,526
	-----	-----
Total liabilities	59,241	64,532
Commitments and contingencies (Note 15)	--	--
Net partners' (Hercules Group) investment (Note 13)	148,777	155,953
	-----	-----
Total liabilities and net partners' (Hercules Group) investment	\$208,018	\$220,485
	=====	=====

The accompanying accounting policies and notes are an integral part of the consolidated financial statements.

Edgar Filing: HERCULES INC - Form 10-K/A

	2001	Year Ended December 31 2000
	----	----
CASH FLOW FROM OPERATING ACTIVITIES:		
Net Income	\$ 41,840	\$ 28,198
Adjustments to reconcile net income to net cash provided from operations:		
Depreciation	9,133	9,757
Amortization	1,014	1,014
Loss on disposal (Note 14)	--	6,854
Loss on impairment of fixed assets (Note 11)	--	--
Corporate and other cost allocations	16,433	15,313
Accruals and deferrals of cash receipts and payments:		
Accounts receivable and other assets	8,905	10,103
Inventories	6,069	7,084
Accounts payable and accrued expenses	(2,318)	(8,659)
Environmental and other assets and liabilities	(896)	800
	-----	-----
Net cash provided by operations	80,180	70,464
	-----	-----
CASH FLOW FROM INVESTING ACTIVITIES:		
Capital expenditures	(11,729)	(9,437)
Investment in affiliate	38	(179)
	-----	-----
Net cash used in investing activities	(11,691)	(9,616)
	-----	-----
CASH FLOW FROM FINANCING ACTIVITIES:		
Repayment of debt	--	(1,650)
Transfers to partners' (Hercules Group)	(65,449)	(58,017)
	-----	-----
Net cash used in financing activities	(65,449)	(59,667)
	-----	-----
Net increase (decrease) in cash and cash equivalents	3,040	1,181
Cash and cash equivalents at beginning of year	2,494	1,313
	-----	-----
Cash and cash equivalents at end of year	\$ 5,534	\$ 2,494
	=====	=====
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the year for:		
Interest Paid	\$ 56	\$ 415
Noncash financing activities		
Issuance of note receivable	3,000	6,600
Corporate and other cost allocations	16,433	15,313

The accompanying accounting policies and notes are an integral part of the consolidated financial statements.

## Edgar Filing: HERCULES INC - Form 10-K/A

### 1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

Aqualon Company (Aqualon) is a U.S. partnership which is owned 99.4182% by Hercules Credit, Inc., a U.S. holding company and 0.5818% by WSP, Inc., a U.S. holding company. Hercules Credit, Inc. and WSP, Inc. are wholly owned subsidiaries of Hercules Incorporated (Hercules). Aqualon is engaged in providing products and services to manage the properties of aqueous (water-based) and non-aqueous systems. These products are principally derived from renewable natural raw materials and are sold as thickeners, emulsifiers, and stabilizers to other manufacturers, including makers of oral hygiene and personal care products, construction materials and latex paints, and are used in the oil and gas industry for drilling and recovery.

In June 2000, Aqualon sold its nitrocellulose operation in Parlin, NJ to Greentree Chemical Technologies, Inc.

Historically, separate company stand-alone financial statements were not prepared for Aqualon. In November 2000, Hercules amended its senior credit facility and ESOP credit facility (the "Facilities"). The Facilities, as amended, are secured by liens on Hercules' property and assets (and those of Hercules' Canadian Subsidiaries), a pledge of the stock and partnership interests of substantially all of Hercules' domestic subsidiaries (including Aqualon) and 65% of the stock of foreign subsidiaries directly owned by Hercules, and a pledge of Hercules' domestic intercompany indebtedness. These financial statements present the financial information on Aqualon, a collateral party to the Hercules debt, based on Hercules' understanding of Securities and Exchange Commission's interpretation and application of Rule 3-16 under the Securities and Exchange Commission's Regulation S-X. These statements were derived from historical accounting records.

On April 29, 2002, in connection with Hercules' sale of its Water Treatment Business (see Note 17) and the repayment of the Facilities, the stock pledges were released. As a result, based on Hercules' current debt structure, these separate company stand-alone financial statements will not be required for the fiscal year ending December 31, 2002.

Aqualon participates in Hercules' centralized cash management system. Accordingly, cash received from Aqualon operations is transferred to Hercules on a periodic basis, and Hercules funds all operational and capital requirements.

The financial statements of Aqualon reflect certain allocated support costs incurred by other entities in the Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations and charges included in Aqualon's financial statements were based on either a direct cost pass-through for items directly identified as related to Aqualon's activities; a percentage allocation for such services provided based on factors such as sales, net assets, or cost of sales; or a relative weighting of geographic activity. Management believes that the allocation methods are reasonable.

During 1989, Hercules acquired the 50% shareholding held by Henkel [its joint venture partner] to make this a wholly owned subsidiary. These financial statements include the push-down of fair value adjustments to assets and liabilities, including goodwill, other intangible assets and property, plant, and equipment and their related amortization and depreciation adjustments.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### PRINCIPLES OF CONSOLIDATION

## Edgar Filing: HERCULES INC - Form 10-K/A

The consolidated financial statements include the accounts of Aqualon and its wholly-owned subsidiary, Organa Trust. All intercompany transactions and profits have been eliminated.

### USE OF ESTIMATES

Preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

### REVENUE RECOGNITION

Aqualon recognizes revenue when the earnings process is complete. This generally occurs when products are shipped to the customer or services are performed in accordance with terms of the agreement, title and risk of loss have been transferred, collectibility is probable, and pricing is fixed and determinable. Accruals are made for sales returns and other allowances based on Aqualon's experience. Shipping and handling costs that are billed to customers are included in revenue; shipping and handling costs that are incurred by Aqualon are included in cost of sales.

5

### AQUALON COMPANY CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

---

### ENVIRONMENTAL EXPENDITURES

Environmental expenditures that pertain to current operations or future revenues are expensed or capitalized according to Aqualon's capitalization policy, which is to charge repairs and maintenance to expense and capitalize replacements or betterments. Expenditures for remediation of an existing condition caused by past operations that do not contribute to current or future revenues are expensed. Liabilities are recognized for remedial activities when the cleanup is probable and can be reasonably estimated.

### CASH AND CASH EQUIVALENTS

Cash equivalents include commercial paper and other securities with original maturities of 90 days or less. Book value approximates fair value because of the short maturity of those instruments.

### INVENTORIES

Inventories are stated at the lower of cost or market. Inventories are valued at standard cost which approximates the average cost method.

### PROPERTY AND DEPRECIATION

Property, plant, and equipment are stated at cost and depreciated using the straight-line method. The estimated useful lives of depreciable assets are as follows: buildings - 30 years; plant, machinery and equipment - 15 years; other machinery and equipment - 3 to 15 years.

## Edgar Filing: HERCULES INC - Form 10-K/A

Maintenance, repairs, and minor renewals are charged to income; major renewals and betterments are capitalized. Upon normal retirement or replacement, the net book value of property (less proceeds of sale or salvage) is charged to income.

### GOODWILL

Goodwill and other intangible assets are amortized on a straight-line basis over the estimated future periods to be benefited, generally 40 years for goodwill, customer relationships, and trademarks and tradenames and 5 to 15 years for other intangible assets.

Pursuant to Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (SFAS 142), beginning January 1, 2002, goodwill will not be amortized but will be tested for impairment annually and any necessary adjustment charged to expense. Intangible assets with finite lives will be amortized over their useful lives.

### LONG-LIVED ASSETS

Aqualon reviews its long-lived assets, including goodwill and other intangibles, for impairment on an exception basis whenever events or changes in circumstances indicate carrying amounts of the assets may not be recoverable through undiscounted future cash flows. If an impairment loss has occurred based on expected future cash flows (undiscounted), the loss is recognized in the income statement. The amount of the impairment loss is the excess of the carrying amount of the impaired asset over the fair value of the asset. The fair value represents expected future cash flows from the use of the assets, discounted at the rate used to evaluate potential investments.

### CONCENTRATIONS OF CREDIT

Financial instruments that potentially subject Aqualon to concentrations of credit risk consist principally of trade receivables. Concentrations of credit risk with respect to trade receivables are limited due to the Company's large number of customers and their dispersion across many different industries and locations.

### FINANCIAL INSTRUMENTS

Aqualon uses various non-derivative financial instruments, including letters of credit, and generally does not require collateral to support its financial instruments.

### STOCK-BASED COMPENSATION

Compensation costs attributable to stock option and similar plans are recognized based on any excess of the quoted market price of the stock on the date of grant over the amount the employee is required to pay to acquire the stock (the intrinsic-value method under Accounting Principles Board Opinion 25 (APB 25)). Such amount, if any, is accrued over the related vesting period, as appropriate. Statement of Financial Accounting Standard No. 123, "Accounting for Stock-based Compensation," requires companies electing to continue to use the intrinsic-value method to make pro forma disclosures of net income as if the fair-value-based method of accounting had been applied.



## Edgar Filing: HERCULES INC - Form 10-K/A

### AQUALON COMPANY CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

---

#### COMPUTER SOFTWARE COSTS

Effective January 1, 1999, Aqualon adopted the American Institute of Certified Public Accountants Statement of Position 98-1, "Accounting for the Cost of Computer Software Developed or Obtained for Internal Use" (SOP 98-1). Our prior accounting was generally consistent with the requirements of SOP 98-1 and, accordingly, adoption of SOP 98-1 had no material effect. Computer software costs are being amortized over a period of 5 to 10 years.

#### INCOME TAXES

Income taxes have not been provided in the accompanying financial statements, as the tax effects of the operating partnership's operations accrue directly to the partners.

#### NET PARTNERS' (HERCULES GROUP) INVESTMENT

The net partners' (Hercules Group) investment account reflects the balance of Aqualon's historical earnings, intercompany amounts, post-employment liabilities and other transactions between Aqualon and the partners/Hercules Group.

#### NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, the FASB issued Statement of Financial Accounting Standards No. 141, "Business Combinations" ("SFAS 141") and Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"). SFAS 141 supersedes Accounting Principles Board Opinion ("APB") No. 16, Business Combinations. The provisions of SFAS 141 (1) require that the purchase method of accounting be used for all business combinations initiated after June 30, 2001, (2) provide specific criteria for the initial recognition and measurement of intangible assets apart from goodwill and (3) require that unamortized negative goodwill be written off immediately as extraordinary gain instead of being deferred and amortized. SFAS 141 also requires that upon adoption of SFAS 142 the Company reclassify the carrying amounts of certain intangible assets into or out of goodwill, based on certain criteria. SFAS 142 supersedes APB No. 17, Intangible Assets, and is effective for fiscal years beginning after December 15, 2001. SFAS 142 primarily addresses the accounting for goodwill and intangible assets subsequent to their initial recognition. The provisions of SFAS 142 (1) prohibit the amortization of goodwill and indefinite-lived intangible assets, (2) require that goodwill and indefinite-lived intangible assets be tested annually for impairment (and in interim periods if certain events occur indicating that the carrying value of goodwill and/or indefinite-lived intangible assets may be impaired), based on fair value (as opposed to cost recovery using future undiscounted cash flows), (3) require that reporting units be identified for the purpose of assessing potential future impairments of goodwill and (4) remove the forty-year limitation on the amortization period of intangible assets that have finite lives.

Effective January 1, 2002 Hercules adopted the provisions of SFAS 142. Hercules identified the following reporting units: BetzDearborn, Pulp and Paper, Aqualon, FiberVisions and Resins. In the first quarter 2002, Hercules completed its transitional impairment, determined that reported goodwill was impaired in the BetzDearborn and FiberVisions reporting units, and recognized an after-tax impairment loss of \$368 million as a cumulative effect of a change in

## Edgar Filing: HERCULES INC - Form 10-K/A

accounting principle. As a result of Hercules' adoption of SFAS 142, the Company will no longer record \$1.0 million of annual amortization relating to existing goodwill and intangibles, as adjusted for the reclassifications just mentioned.

In June 2001, the FASB approved the issuance of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143"). SFAS 143 establishes accounting standards for the recognition and measurement of legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 will become effective for Aqualon in January 1, 2003 and requires recognition of a liability for an asset retirement obligation in the period in which it is incurred. The Company does not believe this statement will have a material effect on its financial statements.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company does not believe this statement will have a material effect on its financial statements.

In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections." The Company has elected to early adopt the provisions of SFAS 145 related to the rescission of SFAS 4, "Reporting Gains and Losses for the Extinguishment of Debt" ("SFAS" 4). Early adoption had no effect on the Company's financial statements.

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146"). SFAS 146 addresses financial accounting and reporting for

7

### AQUALON COMPANY CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

---

costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs in a Restructuring)". SFAS 146 defines the timing of the recognition of costs associated with exit or disposal activities, the types of costs that may be recognized and the methodology for calculating the fair value of such costs. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. The Company does not believe this statement will have a material effect on its financial statements.

#### RECLASSIFICATIONS

Certain amounts in the 2000 and 1999 consolidated financial statements and notes have been reclassified to conform to the 2001 presentation.

#### 3. ACCOUNTS RECEIVABLE, NET

Accounts receivable, net, consists of:

(Dollars in thousands)

Edgar Filing: HERCULES INC - Form 10-K/A

	2001 ----	2000 ----
Trade	\$ 31,365	\$ 36,413
Less allowance for doubtful accounts	(441)	(670)
	-----	-----
Total	\$ 30,924 =====	\$ 35,743 =====

4. NOTE RECEIVABLE

Notes receivable as of December 31, 2001, consists of an unsecured demand note to Greentree Chemical Technologies, Inc. (Greentree) for \$3,000 thousand, due June 30, 2005. The note carried an interest rate of 13.5% until May 1, 2001; thereafter, the interest rate is equal to Prime +7.5% for the remaining duration of the note. Notes receivable as of December 31, 2000, consist of a \$6,600 thousand 30-day demand note from Greentree, related to the divestiture of the Nitrocellulose business in June 2000. On January 8, 2001, Aqualon received \$3,600 thousand in cash from Greentree and issued the unsecured demand note to Greentree for \$3,000 thousand, due June 30, 2005.

5. INVENTORIES

The components of inventories are:

	(Dollars in thousands)	
	2001 ----	2000 ----
Finished products	\$22,480	\$27,754
Raw material and supplies	14,280	15,613
Work in process	2,580	2,042
	-----	-----
Total	\$39,340 =====	\$45,409 =====

6. LONG-TERM INCENTIVE COMPENSATION PLANS

Aqualon participates in long-term incentive compensation plans sponsored by Hercules. These plans provide for the grant of stock options and the award of common stock and other market-based units to certain key employees and non-employee directors.

In 1995, Hercules changed the structure of the long-term incentive compensation plans to place a greater emphasis on shareholder value creation through grants of regular stock options, performance-accelerated stock options, and Cash Value Awards (performance-based awards denominated in cash and payable

## Edgar Filing: HERCULES INC - Form 10-K/A

in shares of common or restricted stock, subject to the same restrictions as restricted stock). Restricted stock and other market-based units are awarded with respect to certain programs. The number of awarded shares outstanding was 189,704 at December 31, 2001, and 491,488 and 926,689 at December 31, 2000 and 1999, respectively.

At December 31, 2001, under Hercules' incentive compensation plans, 1,265,493 shares of common stock were available for grant as stock awards or stock option awards. Stock awards are limited to approximately 15% of the total authorizations. Regular stock options are granted at the market price on the date of grant and are exercisable at various periods from one to five years after date of grant. Performance-accelerated stock options are also granted at the market price on the date of grant and are normally exercisable at nine and one-half years. Exercisability may be accelerated based upon the achievement of predetermined performance goals. Both regular and performance-accelerated stock options expire 10 years after the date of grant.

Restricted shares, options and performance-accelerated stock options are forfeited and revert to Hercules in the event of employment termination, except in the case of death, disability, retirement, or other specified events.

The Company applies APB Opinion 25 in accounting for its plans. Accordingly, no compensation cost has been recognized for the stock option plans. There were no charges to income for the cost of stock awards over the restriction or performance period for 2001, 2000 and 1999, respectively.

Below is a summary of outstanding stock option grants under the incentive compensation plans during 1999, 2000 and 2001:

	Regular		Performance-Accelerated	
	Number of Shares	Weighted-average price	Number of Shares	Weighted- pri
December 31, 1998	337,405	\$39.48	136,645	\$46.
Granted	71,875	\$37.73	69,980	\$37.
Exercised	(1,050)	\$16.21	--	
Forfeited	(3,910)	\$39.50	--	
	-----	-----	-----	-----
December 31, 1999	404,320	\$39.23	206,625	\$43.
Granted	129,800	\$17.20	--	
Exercised	--	--	--	
Forfeited	(39,250)	\$39.50	--	
	-----	-----	-----	-----
December 31, 2000	494,870	\$33.43	206,625	\$43.
Granted	131,925	\$14.22	--	
Exercised	--	--	--	
Forfeited	(40,710)	\$39.56	--	
	-----	-----	-----	-----
December 31, 2001	586,085	\$28.01	206,625	\$43.

The weighted-average fair value of regular stock options granted during 1999, 2000 and 2001 was \$8.26, \$8.85 and \$5.69, respectively. The weighted-average fair value of performance-accelerated stock options granted during 1999, 2000 and 2001 was \$8.01, \$0 and \$0, respectively.

Following is a summary of regular stock options exercisable at December 31, 1999, 2000, and 2001, and their respective weighted-average share prices:

Edgar Filing: HERCULES INC - Form 10-K/A

Options Exercisable	Number of Shares	Weighted-average exercise price
-----	-----	-----
1999	224,230	\$40.49
2000	293,370	\$39.20
2001	368,975	\$35.01

There were no performance-accelerated stock options exercisable at December 31, 1999, 2000 and 2001.

9

AQUALON COMPANY  
CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

---

Following is a summary of stock options outstanding at December 31, 2001:

Exercise Price Range	Outstanding Options		
	Number Outstanding at 12/31/2001	Weighted-average Remaining Contractual Life	Weighted- average exercise price
-----	-----	-----	-----
Regular Stock Options			
\$11 - \$20	261,725	8.90	\$ 14.22
\$20 - \$30	76,475	6.67	\$ 25.56
\$30 - \$40	135,515	6.33	\$ 38.68
\$40 - \$50	84,120	5.73	\$ 47.26
\$50 - \$60	28,250	4.56	\$ 54.01
	-----		
	586,085		
	-----		
Performance-Accelerated Stock Options			
\$14 - \$40	104,655	6.69	\$ 38.16
\$40 - \$50	81,270	5.70	\$ 47.40
\$50 - \$61	20,700	4.18	\$ 55.40
	-----		
	206,625		
	-----		

Hercules currently expects that 100% of performance-accelerated stock options will eventually vest.

Aqualon employees may also participate in the Hercules Employee Stock Purchase Plan ("ESPP"). The ESPP is a qualified non-compensatory plan, which allows eligible employees to acquire shares of common stock through systematic

## Edgar Filing: HERCULES INC - Form 10-K/A

payroll deductions. The plan consists of three-month subscription periods, beginning July 1 of each year. The purchase price is 85% of the fair market value of the common stock on either the first or last day of that subscription period, whichever is lower. Purchases may range from 2% to 15% of an employee's base salary each pay period, subject to certain limitations. Currently, there are no shares of Hercules common stock registered for offer and sale under the plan. Shares issued at December 31, 2001 and 2000, were 1,758,081 and 1,597,861, respectively. The Company applies APB Opinion 25 and related interpretations in accounting for its Employee Stock Purchase Plan. Accordingly, no compensation cost has been recognized for the Employee Stock Purchase Plan.

Had compensation cost for Hercules' Stock-Based Incentive Plans and Employee Stock Purchase Plan been determined on the basis of fair value according to SFAS No. 123, the fair value of each option granted or share purchased would be estimated on the grant date using the Black-Scholes option pricing model.

The following weighted-average assumptions would be used in estimating fair value for 1999, 2000 and 2001:

Assumption -----	Regular Plan ----	Performance Accelerated Plan ----	Employee Stock Purchase Plan -----
Dividend yield	0.96%	3.83%	0.0%
Risk-free interest rate	5.80%	5.57%	4.86%
Expected life	7.1 yrs.	5 yrs.	3 mos.
Expected volatility	33.36%	29.78%	49.11%

The Company's net income and earnings per share for 2001, 2000 and 1999 would approximate the pro forma amounts below:

	(Dollars in thousands)		
	2001 ----	2000 ----	1999 ----
Net income			
As reported	\$41,840	\$28,198	\$36,971
Pro forma	\$41,070	\$26,573	\$35,422

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousands)	
	2001	2000
	----	----
Property, plant, and equipment		
Land	\$ 527	\$ 527
Buildings and equipment	369,708	363,737
Construction in progress	16,185	11,909
	-----	-----
Total	386,420	376,173
Accumulated depreciation and amortization	292,082	284,431
	-----	-----
Net property, plant, and equipment	\$ 94,338	\$ 91,742
	=====	=====
Accrued expenses		
Payroll and employee benefits	\$ 5,416	\$ 4,685
Nitrocellulose inventory disposal cost reserve	5,917	6,478
Current environmental reserve	5,222	4,686
Restructuring reserve	1,762	--
Other	6,907	8,323
	-----	-----
Total	\$ 25,224	\$ 24,172
	=====	=====

8. GOODWILL

Goodwill relates to Hercules' 1989 purchase of Henkel's portion of ownership in Aqualon. At December 31, 2001 and December 31, 2000, goodwill was \$27,536 thousand and \$28,550 thousand, respectively, (net of accumulated amortization of \$13,008 thousand and \$11,994 thousand respectively). Through December 31, 2001, the goodwill was being amortized over 40 years.

9. RESTRUCTURING

In 2001 and 2000, Aqualon incurred \$6,000 thousand and \$1,662 thousand, respectively, in other operating expenses related to employee severance benefits for workforce reductions at Parlin, NJ, Louisiana, MO, and Hopewell, VA, manufacturing sites and Wilmington, DE headquarters in business support functions.

During 2001, management authorized and committed to a plan to reduce the workforce as part of the comprehensive cost reduction and work process redesign program. Under this plan, 97 employees have left or will leave Aqualon, of which 74 employees were terminated pursuant to this plan through December 31, 2001.

The 2000 restructuring costs are related to workforce reductions in the Aqualon manufacturing cost reduction plan. The total number of employee terminations relating to the 2000 plan is 35, and the actions under the 2000 plan are complete.

Severance benefits were paid in accordance with Hercules' standard severance pay plan. A reconciliation of activity with respect to the liabilities established for these plans is as follows:

	(Dollars in thousands)	
	2001	2000
	----	----

Edgar Filing: HERCULES INC - Form 10-K/A

Balance at beginning of year	\$ --	\$ --
Additional termination benefits and other exit costs	6,000	1,662
Cash payments	(4,238)	(1,662)
	-----	-----
Balance at end of year	\$ 1,762	\$ --
	=====	=====

11

AQUALON COMPANY  
CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

---

10. PENSION AND OTHER POSTRETIREMENT BENEFITS

Aqualon participates in a defined benefit pension plan sponsored by Hercules, which covers substantially all employees of Hercules in the U.S. Benefits under this plan are based on the average final pay and years of service. Hercules also provides post-retirement health care and life insurance benefits to eligible retired employees and their dependents.

Information on the actuarial present value of the benefit obligation and fair value of the plan assets is not presented as Hercules manages its U.S. employee benefit plans on a consolidated basis and such information is not maintained separately for the U.S. employees of the Company. The Company's statement of operations includes an allocation of the costs of the U.S. benefits plans. The pension costs were allocated based on percentage of pensionable wages, for each of the years presented, post-retirement benefit costs were allocated using factors derived from the relative net assets and revenues. Net pension income of Hercules allocated to the Company was \$1,719 thousand, \$3,367 thousand, and \$3,810 thousand for the years ended December 31, 2001, 2000 and 1999, respectively, and post-retirement benefit expense was \$2,125 thousand, \$2,462 thousand, and \$1,774 thousand for the years ended December 31, 2001, 2000 and 1999, respectively.

11. OTHER OPERATING EXPENSES, NET

Other operating expenses, net, consists of the following:

	(Dollars in thousands)		
	2001	2000	1999
	----	----	----
Loss on disposal of Nitrocellulose	\$ --	\$ 25,241	\$ 6,500
Asset impairments	--	--	2,000
Environmental charges	2,344	2,617	3,020
Restructuring charges	6,000	1,662	446
Royalties received	(10,473)	(7,613)	(8,474)
Other	--	352	62
	-----	-----	-----
Total	\$ (2,129)	\$ 22,259	\$ 3,554
	=====	=====	=====



## Edgar Filing: HERCULES INC - Form 10-K/A

In 1999, the remaining Nitrocellulose fixed assets at Parlin, NJ were deemed to be impaired.

### 12. OTHER FINANCING ARRANGEMENTS

Hercules manages Aqualon's cash and indebtedness. The majority of the cash provided by or used by Aqualon is provided through this consolidated cash and debt management system. As a result, the amount of domestic cash or debt historically related to Aqualon is not determinable. For purposes of Aqualon's historical financial statements all of Aqualon's positive or negative cash flows have been treated as cash transferred to or from its partners (parent).

### 13. NET PARTNERS' (HERCULES GROUP) INVESTMENT

Changes in net partners' (Hercules Group) investment were as follows:

	(Dollars in thousands)
Balance, January 1, 1999	\$ 191,922
Net income	36,971
Intercompany transactions, net	(58,434)
	-----
Balance, December 31, 1999	170,459
Net income	28,198
Intercompany transactions, net	(42,704)
	-----
Balance, December 31, 2000	155,953
Net income	41,840
Intercompany transactions, net	(49,016)
	-----
Balance, December 31, 2001	\$ 148,777
	=====

12

## AQUALON COMPANY CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

---

### 14. DIVESTITURES

In June 2000, Aqualon divested its Nitrocellulose operation at Parlin, NJ to Greentree Chemical Technologies, Inc. As a result of the transaction, Aqualon received a \$6,600 thousand note (see note 4) and recorded a one-time pre-tax loss of \$25,241 thousand, primarily for employee termination benefits, inventory transfer and disposal, environmental liabilities, and other miscellaneous expenses, of which \$20,316 thousand has been expensed as of December 31, 2001. Aqualon terminated approximately 100 employees associated with the Nitrocellulose operation at Parlin, NJ, which resulted in severance payments of \$4 million. Nitrocellulose revenues were \$23,503 thousand and \$58,526 thousand in 2000 and 1999, respectively.

## Edgar Filing: HERCULES INC - Form 10-K/A

### 15. COMMITMENTS AND CONTINGENCIES

#### Leases

Aqualon has operating leases (including office space, transportation, and data processing equipment) expiring at various dates. Rental expense was \$1,533 thousand in 2001, \$553 thousand in 2000, and \$661 thousand in 1999.

At December 31, 2001, minimum rental payments under noncancelable leases aggregated \$737 thousand. The net minimum payments over the next five years are \$403 thousand in 2002, \$242 thousand in 2003, \$61 thousand in 2004, \$22 thousand in 2005, and \$9 thousand in 2006.

#### Litigation

Aqualon currently and from time to time is involved in litigation incidental to the conduct of its business. In the opinion of Aqualon's management, none of such litigation as of December 31, 2001 is likely to have a material adverse effect on the financial position and results of operations of Aqualon.

#### Environmental

Aqualon has established accruals for the estimated cost of environmental remediation and/or cleanup at various sites. The estimated range of the reasonable possible share of costs for investigation and cleanup is between \$25 million and \$42 million. The actual costs will depend upon numerous factors, including the number of parties found to be responsible at each environmental site and their ability to pay; the actual methods of remediation required or agreed to; the outcomes of negotiations with regulatory authorities; outcomes of litigation; changes in environmental laws and regulations; technological developments; and the number of years of remedial activity required, which could range from 0 to 30 years. As of December 31, 2001, the accrued liability of \$25 million for environmental remediation represents management's best estimate of the probable and reasonably estimable costs related to environmental remediation. Aqualon estimates that these liabilities will be paid over the next five years. The extent of liability is evaluated quarterly. The measurement of the liability is evaluated based on currently available information, including the process of remedial investigations at each site and the current status of negotiations with regulatory authorities regarding the method and extent of apportionment of costs among other potentially responsible parties. Aqualon is unaware of any unasserted claims and has not reflected them in the reserve. While it is not feasible to predict the outcome of all pending suits and claims, the ultimate resolution of these environmental matters could have a material effect upon the results of operations and the financial position of Aqualon.

#### Other

As of December 31, 2001, Aqualon had \$4.3 million in letters of credit outstanding with lenders.

### 16. RELATED PARTY TRANSACTIONS

Aqualon has entered into certain agreements with affiliated entities. These agreements were developed in the context of parent/subsidiary relationship and therefore may not necessarily reflect the result of arms-length negotiations between independent parties. Aqualon records sales with affiliates based on a cost-plus formula developed and agreed-upon by both parties.

Corporate and other allocations: As discussed in Note 1, the financial statements of Aqualon reflect certain allocated support costs incurred by other entities in the Hercules group. These costs include executive, legal,

## Edgar Filing: HERCULES INC - Form 10-K/A

accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, research & development overhead, investor relations and other corporate services. Allocations and charges included in Aqualon's financial statements were based on either a direct cost pass-through for items directly identified as related to Aqualon's activities; a percentage allocation for such services provided based on factors such as revenues, net assets, costs of sales or a relative weighting of geographic activity. These allocations are reflected in the

13

### AQUALON COMPANY CONSOLIDATED NOTES TO FINANCIAL STATEMENTS

---

selling, general and administrative line item in the statement of operations. Such allocations and corporate charges totaled \$16,433 thousand, \$15,313 thousand, and \$21,444 thousand in 2001, 2000 and 1999, respectively.

**Royalties:** Aqualon entered into a license agreement in respect of the use of manufacturing formulations and specifications by affiliated companies which are developed and owned by Aqualon. Aqualon received royalties in respect of this agreement of \$10,473 thousand, \$7,613 thousand, and \$8,474 thousand in 2001, 2000 and 1999, respectively. The royalties are included as reductions to other operating expenses in the financial statements.

**Purchases from affiliates:** Aqualon purchases a broad range of products in the normal course of business from affiliated companies. Aqualon's purchases from affiliated companies were \$21,391 thousand, \$23,457 thousand, and \$23,598 thousand in 2001, 2000 and 1999, respectively.

#### 17. SUBSEQUENT EVENTS

On April 29, 2002, Hercules completed the sales of its Water Treatment Business to GE Specialty Materials (GESM). Pursuant to the Stock and Asset Purchase Agreement for the transaction, the sale included the stock of BetzDearborn Inc. and certain specified assets and liabilities. Hercules used the proceeds from the sale to prepay borrowings under its Facilities. Pursuant to the prepayment, among other things, the Company's stock, which had been pledged as collateral to the Facilities, was released.

14

#### REPORT OF INDEPENDENT ACCOUNTANTS

TO THE SHAREHOLDERS AND THE BOARD OF DIRECTORS OF  
HERCULES INCORPORATED  
WILMINGTON, DELAWARE

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income and comprehensive loss and of cash flows present fairly, in all material respects, the financial position of

## Edgar Filing: HERCULES INC - Form 10-K/A

BetzDearborn Inc., a subsidiary of Hercules Incorporated, and its subsidiaries at December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP  
Philadelphia, Pennsylvania  
December 9, 2002

15

BETZDEARBORN INC.  
CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE LOSS

	(Dollars in millions)		
	Year Ended December 31,		
	2001	2000	1999
	-----	-----	-----
Sales to third parties	\$ 1,105	\$ 1,170	\$ 1,203
Sales to Hercules Group	89	108	69
	-----	-----	-----
	1,194	1,278	1,272
Cost of sales	581	632	588
Selling, general, and administrative expenses	379	404	423
Corporate and other cost allocations	35	27	19
Research and development	16	20	36
Goodwill and intangible asset amortization	61	71	70
Other operating expenses, net (Note 14)	55	22	11
	-----	-----	-----
Profit from operations	67	102	125
Interest expense, net	21	30	37
Other expense, net (Note 16)	7	2	--
	-----	-----	-----
Income before income taxes and minority interest	39	70	88
Provision for income taxes (Note 19)	32	40	51
	-----	-----	-----
Income before minority interest	7	30	37
Minority interest	3	5	4
	-----	-----	-----
Net income	4	25	33
Additional minimum pension liability, net of tax	(15)	--	--
Translation adjustments	(41)	(46)	(47)
	-----	-----	-----
Comprehensive loss	\$ (52)	\$ (21)	\$ (14)
	=====	=====	=====

## Edgar Filing: HERCULES INC - Form 10-K/A

The accompanying notes are an integral part of the consolidated financial statements.

16

BETZDEARBORN INC.  
CONSOLIDATED BALANCE SHEETS

	(Dollars in millions)	
	December 31,	
	2001	2000
	-----	-----
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 25	\$ 21
Accounts receivable, net (Note 3)	173	215
Miscellaneous receivable	15	15
Inventories (Note 4)	83	91
Deferred income taxes (Note 19)	18	20
	-----	-----
Total current assets	314	362
	-----	-----
Property, plant, and equipment, net (Note 9)	270	304
Investments in affiliates (Note 5)	150	150
Goodwill and other intangible assets, net (Note 10)	2,212	2,276
Prepaid pension (Note 13)	15	13
Deferred charges and other assets	57	57
	-----	-----
Total assets	\$ 3,018	\$ 3,162
	=====	=====
<b>LIABILITIES AND NET HERCULES GROUP INVESTMENT</b>		
Current liabilities		
Current income tax liability	\$ 38	\$ 62
Accounts payable	64	69
Short-term debt (Note 6)	8	26
Accrued expenses (Note 9)	74	93
	-----	-----
Total current liabilities	184	250
Long term debt (Note 7)	148	181
Deferred income taxes (Note 19)	259	262
Pension and other postretirement benefits (Note 13)	45	34
Deferred credits and other liabilities	7	8
	-----	-----
Total liabilities	643	735
Commitments and contingencies (Note 17)	--	--
Minority Interest	22	23
Net Hercules Group Investment (Note 15)		
Accumulated other comprehensive loss	(133)	(77)
Intercompany balances, net	2,486	2,481
	-----	-----
Total Net Hercules Group Investment	2,353	2,404
	-----	-----
Total liabilities and Net Hercules Group Investment	\$ 3,018	\$ 3,162
	=====	=====

## Edgar Filing: HERCULES INC - Form 10-K/A

The accompanying notes are an integral part of the consolidated financial statements.

17

BETZDEARBORN INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS

	(Dollars in million)	
	Year Ended December	
	2001	2000
	-----	-----
<b>CASH FLOW FROM OPERATING ACTIVITIES:</b>		
Net Income	\$ 4	\$ 25
Adjustments to reconcile net income to net cash provided by operations:		
Depreciation	35	48
Amortization	61	71
Loss on disposal	15	3
Deferred income taxes	(5)	19
Minority interest	3	5
Corporate and other cost allocations	35	27
Other noncash charges (income)	--	5
Accruals and deferrals of cash receipts and payments:		
Accounts and miscellaneous receivables	42	91
Inventories	8	30
Accounts payable and accrued expenses	(24)	(66)
Noncurrent assets and liabilities	14	(67)
Transfers (to) from Hercules Group from operations	(223)	(97)
	-----	-----
Net cash (used in) provided by operations	(35)	94
	-----	-----
<b>CASH FLOW FROM INVESTING ACTIVITIES:</b>		
Capital expenditures	(15)	(27)
Proceeds from fixed asset disposals	2	13
Other, net	(3)	(13)
	-----	-----
Net cash used in investing activities	(16)	(27)
	-----	-----
<b>CASH FLOW FROM FINANCING ACTIVITIES:</b>		
Long-term debt proceeds	--	6
Long-term debt repayments	(33)	(9)
Changes in short-term debt	(18)	(2)
Transfers from (to) Hercules Group	108	(75)
	-----	-----
Net cash used in financing activities	57	(80)
	-----	-----
Effect of exchange rate changes on cash	(2)	2
	-----	-----
Net increase (decrease) in cash and cash equivalents	4	(11)
Cash and cash equivalents at beginning of year	21	32
	-----	-----
Cash and cash equivalents at end of year	\$ 25	\$ 21
	=====	=====
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>		
Cash paid during the year for:		
Interest	\$ 22	\$ 29

## Edgar Filing: HERCULES INC - Form 10-K/A

Income taxes, net	61	34
Noncash financing activities:		
Corporate and other cost allocations	35	27

The accompanying notes are an integral part of the consolidated financial statements.

18

BETZDEARBORN INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

### 1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

BetzDearborn Inc. ("BetzDearborn" or the "Company") is a wholly owned subsidiary of Hercules Incorporated ("Hercules"). The Company is a global engineered specialty chemical company engaged in the treatment of water and industrial process systems operating in a wide variety of industrial and commercial applications with particular emphasis on the chemical, petroleum refining, paper, food processing, automotive, steel and power industries.

On October 15, 1998, Hercules acquired all of the outstanding shares of the Company for \$2,235 million in cash and \$186 million in common stock exchanged for the shares held by the BetzDearborn ESOP Trust. The shares were valued using the quoted market price of the stock at the time of exchange. In addition, Hercules assumed debt with a fair value of \$117 million and repaid \$557 million of other long-term debt held by the Company.

In accordance with the purchase method of accounting, the adjusted purchase price was allocated to the estimated fair value of net assets acquired, with the excess recorded as goodwill. Goodwill is amortized over 40 years on a straight-line basis. Identified intangibles are amortized over 10 to 40 years, on a straight-line basis. Additionally, approximately \$130 million of the purchase price was allocated to purchased in-process research and development and was charged to expense at the date of acquisition.

As a result of this acquisition the Company, as a part of an effort by Hercules, entered into several internal reorganization transactions during 1999 and 2000. The transactions included the Company selling several of its investments in subsidiaries to Hercules affiliates, purchasing several investments in subsidiaries from Hercules affiliates, merging companies, and acquiring certain investments in Hercules group companies that are valued at cost. As all investments in this reorganization are under the common control of Hercules, these transactions have been accounted for in a manner similar to pooling of interests.

Separate company stand-alone financial statements were not prepared for the Company since its acquisition and subsequent reorganization within Hercules. In November 2000, Hercules amended its senior credit facility and ESOP credit facility (the "Facilities"). The Facilities, as amended, are secured by liens on Hercules' property and assets (and those of Hercules' Canadian Subsidiaries), a pledge of the stock and partnership and member interests of substantially all of Hercules' domestic subsidiaries (including the Company) and 65% of the stock of foreign subsidiaries directly owned by Hercules, and a pledge of Hercules' domestic intercompany indebtedness. These financial statements present the financial information on the Company, a collateral party to the Hercules debt, based on Hercules' understanding of Securities and Exchange Commission's interpretation and application of Rule 3-16 under the Securities and Exchange

## Edgar Filing: HERCULES INC - Form 10-K/A

Commission's Regulation S-X. These statements were derived from historical accounting records.

On April 29, 2002, in connection with Hercules' sale of its Water Treatment Business (see Note 20) and the repayment of the Facilities, the stock pledges were released. As a result, based on Hercules' current debt structure, these separate company stand-alone financial statements will not be required for the fiscal year ending December 31, 2002.

The Company participates in Hercules' centralized cash management system. Accordingly, cash received from Company operations is transferred to Hercules on a periodic basis, and Hercules funds all operational and capital requirements.

The consolidated financial statements of the Company reflect certain allocated support costs incurred by other entities in the Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations and charges included in the Company's financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on factors such as sales, net assets, or cost of sales; or a relative weighting of geographic activity. Management believes that the allocation methods are reasonable.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries where control exists. Following the acquisition of the Company by Hercules, the Company continued its practice of using a November 30 fiscal year-end for certain non-U.S. subsidiaries to expedite the year-end closing process. All intercompany transactions and profits have been eliminated.

19

BETZDEARBORN INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

#### USE OF ESTIMATES

Preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

#### REVENUE RECOGNITION

The Company recognizes revenue when the earnings process is complete. This generally occurs when products are shipped to the customer or services are performed in accordance with terms of the agreement, title and risk of loss have been transferred, collectibility is probable, and pricing is fixed and determinable. Accruals are made for sales returns and other allowances based on the Company's experience. The corresponding shipping and handling costs are included in cost of sales.

#### ENVIRONMENTAL EXPENDITURES



## Edgar Filing: HERCULES INC - Form 10-K/A

Environmental expenditures that pertain to current operations or future revenues are expensed or capitalized according to the Company's capitalization policy, which is to charge repairs and maintenance to expense and capitalize replacements or betterments. Expenditures for remediation of an existing condition caused by past operations that do not contribute to current or future revenues are expensed. Liabilities are recognized for remedial activities when the cleanup is probable and can be reasonably estimated.

### CASH AND CASH EQUIVALENTS

Cash equivalents include commercial paper and other securities with original maturities of 90 days or less. Book value approximates fair value because of the short maturity of those instruments.

### INVENTORIES

Inventories are stated at the lower of cost or market. Domestic inventories are valued predominantly on the last-in, first - out (LIFO) method. Foreign and certain domestic inventories, which in the aggregate represent 45% of total inventories at December 31, 2001, are valued principally at standard cost, which approximates the average cost method.

### PROPERTY AND DEPRECIATION

Property, plant, and equipment are stated at cost and depreciated using the straight-line method. The estimated useful lives of depreciable assets are as follows: buildings - 30 years; plant, machinery and equipment - 15 years; other machinery and equipment - 3 to 15 years.

Maintenance, repairs, and minor renewals are charged to income; major renewals and betterments are capitalized. Upon normal retirement or replacement, the net book value of property (less proceeds of sale or salvage) is charged to income.

### INVESTMENTS

Investments in affiliated companies with a greater than 20% or 50% or less ownership interest are accounted for using the equity method of accounting. Accordingly, these investments are included in investments in affiliates on the Company's balance sheet and the income or loss from these investments is included in equity income (loss) of affiliated companies in the Company's statement of income.

Investments in affiliated companies in which the Company does not have a controlling interest, or an ownership and voting interest so large as to exert significant influence, are accounted for using the cost method of accounting. Accordingly, these investments are included in investments in affiliates on the Company's balance sheet.

### GOODWILL

Goodwill and other intangible assets are amortized on a straight-line basis over the estimated future periods to be benefited.

Pursuant to Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (SFAS 142), beginning January 1, 2002, goodwill will not be amortized but will be tested for impairment annually and any necessary adjustment charged to expense. Intangible assets with finite lives will be amortized over their useful lives.

BETZDEARBORN INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS-----  
LONG-LIVED ASSETS

The Company reviews its long-lived assets, including goodwill and other intangibles, for impairment on an exception basis whenever events or changes in circumstances indicate carrying amounts of the assets may not be recoverable through undiscounted future cash flows. If an impairment loss has occurred based on expected future cash flows (undiscounted), the loss is recognized in the income statement. The amount of the impairment loss is the excess of the carrying amount of the impaired asset over the fair value of the asset. The fair value represents expected future cash flows from the use of the assets, discounted at the rate used to evaluate potential investments.

## CONCENTRATIONS OF CREDIT RISK

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of trade receivables. Concentrations of credit risk with respect to trade receivables are limited due to the Company's large number of customers and their dispersion across many different industries and locations.

## DERIVATIVE INSTRUMENTS AND HEDGING

Derivative financial instruments have been used to hedge risk caused by fluctuating currency and interest rates. The Company enters into forward-exchange contracts and currency swaps to hedge foreign currency exposure. Decisions regarding hedging are made on a case-by-case basis, taking into consideration the amount and duration of the exposure, market volatility, and economic trends. The Company uses the fair-value method of accounting, recording realized and unrealized gains and losses on these contracts monthly. They are included in other income (expense), net, except for gains and losses on contracts to hedge specific foreign currency commitments, which are deferred and accounted for as part of the transaction. Gains or losses on instruments which have been used to hedge the value of investments in certain non-U.S. subsidiaries are included in the foreign currency translation adjustment. It is the Company's policy to match the term of financial instruments with the term of the underlying designated item. If the designated item is an anticipated transaction no longer likely to occur, gains or losses from the instrument designated as a hedge are recognized in current period earnings. The Company does not hold or issue financial instruments for trading purposes. In the Consolidated Statement of Cash Flow, the Company reports the cash flows resulting from its hedging activities in the same category as the related item that is being hedged.

The Company used interest rate swap agreements to manage interest costs and risks associated with changing rates. The differential to be paid or received is accrued as interest rates change and is recognized in interest expense over the life of the agreements. Counter parties to the forward exchange, currency swap, and interest rate swap contracts are major financial institutions. Credit loss from counter party nonperformance is not anticipated. During 2000 the interest rate swap portfolio was terminated due to the conversion of foreign denominated debt to U.S. dollar denominated debt and a debt restructuring that replaced variable rate debt with fixed rate debt.

## STOCK-BASED COMPENSATION

Compensation costs attributable to stock option and similar plans are

## Edgar Filing: HERCULES INC - Form 10-K/A

recognized based on any excess of the quoted market price of the stock on the date of grant over the amount the employee is required to pay to acquire the stock (the intrinsic-value method under Accounting Principles Board Opinion 25 (APB 25)). Such amount, if any, is accrued over the related vesting period, as appropriate. Statement of Financial Accounting Standard No. 123, "Accounting for Stock-based Compensation," requires companies electing to continue to use the intrinsic-value method to make pro forma disclosures of net income as if the fair-value-based method of accounting had been applied.

### COMPUTER SOFTWARE COSTS

Effective January 1, 1999, the Company adopted the American Institute of Certified Public Accountants Statement of Position 98-1, "Accounting for the Cost of Computer Software Developed or Obtained for Internal Use" (SOP 98-1). The Company's prior accounting was generally consistent with the requirements of SOP 98-1 and, accordingly, adoption of SOP 98-1 had no material effect. Computer software costs are being amortized over a period of 5 to 10 years.

### INCOME TAXES

The Company's operations since acquisition have been included in the consolidated income tax returns filed by its parent. Income tax expense in the accompanying financial statements has been computed assuming the Company filed separate income tax returns. Differences between this calculation of income taxes currently payable and consolidated amounts reported in the consolidated financial statements of the parent have been reflected as net Hercules Group investment.

21

BETZDEARBORN INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

### RESEARCH AND DEVELOPMENT

Research and development expenditures are expensed as incurred.

### NET HERCULES GROUP INVESTMENT

The net Hercules Group investment account reflects the balance of the Company's historical earnings, intercompany amounts, income taxes, taxes accrued and deferred, post-employment liabilities, foreign currency translation and other transactions between the Company and the Hercules Group.

### NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 141, "Business Combinations" ("SFAS 141"), and SFAS No. 142. SFAS 141 supersedes Accounting Principles Board Opinion ("APB") No. 16, Business Combinations. The provisions of SFAS 141 (1) require that the purchase method of accounting be used for all business combinations initiated after June 30, 2001, (2) provide specific criteria for the initial recognition and measurement of intangible assets apart from goodwill and (3) require that unamortized negative goodwill be written off immediately as extraordinary gain instead of being deferred and amortized. SFAS 141 also requires that upon adoption of SFAS 142 the Company reclassify the carrying amounts of certain intangible assets into or out of goodwill, based on certain criteria. SFAS 142 supersedes APB No. 17, Intangible Assets, and is effective for fiscal years beginning after December 15, 2001. SFAS 142 primarily addresses the accounting for goodwill and intangible assets subsequent to their initial

## Edgar Filing: HERCULES INC - Form 10-K/A

recognition. The provisions of SFAS 142 (1) prohibit the amortization of goodwill and indefinite-lived intangible assets, (2) require that goodwill and indefinite-lived intangible assets be tested annually for impairment (and in interim periods if certain events occur indicating that the carrying value of goodwill and/or indefinite-lived intangible assets may be impaired), based on fair value (as opposed to cost recovery using future undiscounted cash flows), (3) require that reporting units be identified for the purpose of assessing potential future impairments of goodwill and (4) remove the forty-year limitation on the amortization period of intangible assets that have finite lives.

Effective January 1, 2002 Hercules adopted the provisions of SFAS 142. Hercules identified the following reporting units: BetzDearborn, Pulp and Paper, Aqualon, FiberVisions and Resins. In connection with Hercules' transitional review, recorded goodwill was determined to be impaired in the BetzDearborn and FiberVisions reporting units. In the first quarter 2002, Hercules completed its transitional impairment review of the identified reporting units and recognized an after tax impairment loss of \$368 million as a cumulative effect of a change in accounting principle, of which \$263 million related to the BetzDearborn reporting unit. As a result of Hercules' adoption of SFAS 142, the Company will no longer record \$61 million of annual amortization relating to existing goodwill and intangibles.

Goodwill related to the BetzDearborn business was evaluated for impairment at December 31, 2001 under Statement of Financial Accounting Standards No. 121 "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed of". Such evaluation indicated that goodwill associated with the business was recoverable from anticipated future undiscounted cash flows. Accordingly, no impairment loss was recorded in the December 31, 2001 financial statements.

In June 2001, the Financial Accounting Standards Board ("FASB") approved the issuance of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143"). SFAS 143 establishes accounting standards for the recognition and measurement of legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 will become effective for the Company on January 1, 2003 and requires recognition of a liability for an asset retirement obligation in the period in which it is incurred. The Company does not believe this statement will have a material effect on its financial statements.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company does not believe this statement will have a material effect on its financial statements.

In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment to FASB Statement No. 13, and Technical Corrections." The Company has elected to early adopt the provisions of SFAS 145 related to the rescission of SFAS 4, "Reporting Gains and Losses from the Extinguishment of Debt" ("SFAS 4"). The early adoption of SFAS 145 had no effect on the Company's financial statements.

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146"). SFAS 146 addresses financial accounting and reporting for

## Edgar Filing: HERCULES INC - Form 10-K/A

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs in a Restructuring)". SFAS 146 defines the timing of the recognition of costs associated with exit or disposal activities, the types of costs that may be recognized and the methodology for calculating the fair value of such costs. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. The Company does not believe this statement will have a material effect on its financial statements.

#### RECLASSIFICATIONS

Certain amounts in the 2000 and 1999 consolidated financial statements and notes have been reclassified to conform to the 2001 presentation.

#### 3. ACCOUNTS RECEIVABLE, NET

Accounts receivable, net, consists of:

	(Dollars in millions)	
	2001	2000
	-----	-----
Trade	\$ 189	\$ 233
Less allowance for doubtful accounts	(16)	(18)
	-----	-----
Total	\$ 173	\$ 215
	=====	=====

#### 4. INVENTORIES

The components of inventories are:

	(Dollars in millions)	
	2001	2000
	-----	-----
Finished products	\$ 48	\$ 54
Materials, supplies and work in process	35	37
	-----	-----
Total	\$ 83	\$ 91
	=====	=====

Inventories valued on the LIFO method were lower than if valued under the average-cost method, which approximates current cost, by \$1 million and \$0 at December 31, 2001, and 2000 respectively.

#### 5. INVESTMENTS

Total investments in affiliated companies were as follows:

## Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in millions)	
	2001	2000
	-----	-----
Investment in Hercules International Limited	\$ 137	\$ 137
Investment in Hercules Quimica SA	13	13
	-----	-----
Total	\$ 150	\$ 150
	=====	=====

At December 31, 2001 the Company's investment consist of a 38.97% ownership of Hercules Quimica S.A., a Hercules affiliate, and a 16% ownership of Hercules International Limited, a Hercules affiliate. The Company's carrying value of Hercules Quimica S.A. at December 31, 2001 and 2000 equals its share of the underlying equity in net assets of the affiliate. The investment in Hercules International Limited is recorded at cost at December 31, 2001 and 2000. Each of these entities operates in lines of business similar to the Company, supplying engineered chemical treatment programs for water and process systems in industrial, commercial and institutional establishments.

23

BETZDEARBORN INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

### 6. SHORT-TERM DEBT

A summary of short-term debt follows:

	(Dollars in millions)	
	2001	2000
	-----	-----
Banks	\$ 4	\$ 21
Current maturities of long-term debt	4	5
	-----	-----
	\$ 8	\$ 26
	=====	=====

Bank borrowings represent primarily foreign overdraft facilities and short-term lines of credit, which are generally payable on demand with interest at various rates. These borrowings approximate market value because of their short maturity period.

At December 31, 2001, the Company had \$7 million of unused short-term lines of credit that may be drawn as needed, with interest at a negotiated spread over lenders' cost of funds. Lines of credit in use at December 31, 2001, were \$4 million. Weighted-average interest rates on short-term borrowings at December 31, 2001 and 2000 were 15% and 5.66%, respectively.

### 7. LONG-TERM DEBT AND OTHER FINANCING ARRANGEMENTS

Long-term debt with third parties at December 31, 2001 and 2000 is summarized below.

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in millions)	
	2001	2000
	-----	-----
Canadian revolving loan facility (a)	\$ 65	\$ 83
ESOP debt (b)	84	101
Other	3	2
	-----	-----
	152	186
Less current maturities of long-term debt	4	5
	-----	-----
	\$ 148	\$ 181
	=====	=====

- (a) The Company's Canadian subsidiary has a bank loan facility of up to the equivalent of US \$100 million from select lenders in Canada, which is part of the Hercules \$3,650 million credit facility with a syndicate of banks. The bank loan facility is repayable in Canadian funds and bears interest at bankers' acceptance rates plus 2.25%. The interest prepaid on the bankers' acceptances is included in the net payable amount. The Company's Canadian subsidiary's assets and 65% of its common stock are pledged as collateral to the Hercules credit facility.
- (b) The proceeds of this loan were originally used by the BetzDearborn ESOP Trust for the purchase of BetzDearborn preferred shares that, upon acquisition by Hercules, were converted into equivalent shares of Hercules common stock. At the date of acquisition by Hercules, the loan was recorded at a fair market value of \$110 million which included a \$16 million fair value step-up that is being amortized over the life of the debt. The loan matures in June 2009. Effective November 14, 2000, the ESOP credit facility together with the Hercules senior credit facility were amended. The senior credit facility and ESOP credit facility, as amended are secured by liens on the Hercules' property and assets, a pledge of the stock of the Company and all its domestic subsidiaries and 65% of the stock of first tier foreign subsidiaries and a pledge of domestic intercompany indebtedness. Effective with the third amendment, the interest rate was increased to 11.95%.

Effective January 23, 2001, as a result of the lowered credit rating of Hercules, the interest rate on the loan and guarantee increased to 12.95%. As a result of Hercules' divestiture in May 2001 of the Eastman and Peroxide businesses, the Company was required to use a portion of the proceeds to prepay the ESOP facility. Hercules paid \$13 million against the loan principal, resulting in the incurrence of \$5 million in pre-payment penalties which were expensed. Both Hercules' senior credit facility and the ESOP credit facility require quarterly compliance with certain financial covenants.

Effective March 6, 2002, the facilities were amended to (i) modify certain financial covenants; (ii) change the mandatory prepayment provisions; (iii) permit the reorganization of the Company in order to effect the separation of the Water Treatment Business; and (iv) permanently reduce the revolving committed amount

## Edgar Filing: HERCULES INC - Form 10-K/A

BETZDEARBORN INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

under the credit facility to \$200 million. The amendment to the credit facility also included provisions that are effective only upon the consummation of the sale of the Water Treatment Business and the prepayment of the credit facility, which occurred on April 29, 2002. These additional provisions include the following: (i) the release of the subsidiary stock pledge to the collateral agent; (ii) the elimination of the requirement that stock of any additional subsidiaries be pledged in the future; and (iii) the revision of the permitted amount of asset purchases and dispositions.

Hercules used the net proceeds of approximately \$1.7 billion from the sale of the Water Treatment Business to pay in full the amounts outstanding under the Facilities. Concurrently, the Canadian revolving credit facility was cancelled.

For the year ended 2001, the Company has \$130 million of long term debt payable to affiliates that is primarily held by Hercules, Hercules Shared Services Center, Inc., and SA Hercules Europe NV. For the year ended 2000, the Company had \$289 million in long-term debt payable to affiliates with the same parties. The long-term debt payable to affiliates primarily has no set payment schedule and carry interest rates ranging from 4.60% to 12.42%. The long term debt payable to affiliates is recorded in the Net Hercules Group Investment account in the financial statements.

Net interest expense in 2001, 2000 and 1999 was \$21 million, \$30 million, and \$37 million respectively, of which \$16 million, \$19 million and \$25 million respectively, was related party net interest expense.

### 8. LONG-TERM INCENTIVE COMPENSATION PLANS

The Company participates in long-term incentive compensation plans sponsored by Hercules. These plans provide for the grant of stock options and the award of common stock and other market-based units to certain key employees and non-employee directors.

In 1995, Hercules changed the structure of the long-term incentive compensation plans to place a greater emphasis on shareholder value creation through grants of regular stock options, performance-accelerated stock options, and Cash Value Awards (performance-based awards denominated in cash and payable in shares of common or restricted stock, subject to the same restrictions as restricted stock). Restricted stock and other market-based units are awarded with respect to certain programs. The number of awarded shares outstanding was 189,704 at December 31, 2001, and 491,488 and 926,689 at December 31, 2000 and 1999, respectively.

At December 31, 2001, under Hercules' incentive compensation plans, 1,265,493 shares of common stock were available for grant as stock awards or stock option awards. Stock awards are limited to approximately 15% of the total authorizations. Regular stock options are granted at the market price on the date of grant and are exercisable at various periods from one to five years after date of grant. Performance-accelerated stock options are also granted at the market price on the date of grant and are normally exercisable at nine and one-half years. Exercisability may be accelerated based upon the achievement of predetermined performance goals. Both regular and performance-accelerated stock options expire 10 years after the date of grant.

Restricted shares, options and performance-accelerated stock options are forfeited and revert to Hercules in the event of employment termination, except in the case of death, disability, retirement, or other specified events.



## Edgar Filing: HERCULES INC - Form 10-K/A

The Company applies APB Opinion 25 in accounting for its plans. Accordingly, no compensation cost has been recognized for the stock option plans. There were no charges to income for the cost of stock awards over the restriction or performance period for 2001, 2000 and 1999, respectively.

Below is a summary of outstanding stock option grants under the incentive compensation plans during 1999, 2000 and 2001:

25

BETZDEARBORN INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

	Regular		Performance-Accelerated	
	Number of Shares	Weighted-average Price	Number of Shares	Weighted-average Price
	-----		-----	
December 31, 1998	48,625	\$37.59	-	-
Granted	219,750	\$37.47	120,625	\$37.29
Exercised	-	-	-	-
Forfeited	(28,000)	\$35.02	(14,042)	\$37.56
-----				
December 31, 1999	240,375	\$37.78	106,583	\$37.26
Granted	240,300	\$17.13	-	-
Exercised	-	-	-	-
Forfeited	(9,100)	\$37.56	(1,400)	\$37.56
-----				
December 31, 2000	471,575	\$27.26	105,183	\$37.26
Granted	290,875	\$11.28	-	-
Exercised	-	-	-	-
Forfeited	(39,800)	\$28.46	(1,500)	\$35.96
-----				
December 31, 2001	722,650	\$20.76	103,683	\$37.27

The weighted-average fair value of regular stock options granted during 1999, 2000 and 2001 was \$8.25, \$8.84 and \$5.69, respectively. The weighted-average fair value of performance-accelerated stock options granted during 1999, 2000 and 2001 was \$7.99, \$0 and \$0, respectively.

Following is a summary of regular stock options exercisable at December 31, 1999, 2000 and 2001, and their respective weighted-average share prices:

Options Exercisable	Number of Shares	Weighted-average Exercise Price
	-----	
December 31, 1999	32,490	\$39.04
December 31, 2000	143,115	\$36.62
December 31, 2001	315,630	\$29.09

There were no performance-accelerated stock options exercisable at

## Edgar Filing: HERCULES INC - Form 10-K/A

December 31, 1999, 2000 and 2001.

Following is a summary of stock options outstanding at December 31, 2001:

Exercise Price Range -----	Number Outstanding at 12/31/01 -----	Outstanding Options Weighted-average Remaining Contractual Life -----	Weighted- average Exercise Price -----
Regular Stock Options			
\$11 - \$20	513,475	9.00	\$13.81
\$30 - \$40	206,225	7.15	\$37.69
\$40 - \$50	2,950	6.35	\$47.81
	----- 722,650 =====		
Performance-Accelerated Stock Options			
\$14 - \$40	103,683	7.37	\$37.27
	----- 103,683 =====		

The Company currently expects that 100% of performance-accelerated stock options will eventually vest.

The Company's employees may also participate in the Hercules Employee Stock Purchase Plan ("ESPP"). The ESPP is a qualified non-compensatory plan, which allows eligible employees to acquire shares of common stock through systematic payroll deductions. The plan consists of three-month subscription periods, beginning July 1 of each year. The purchase price is 85% of the fair market value of the common stock on either the first or last day of that subscription

26

BETZDEARBORN INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

period, whichever is lower. Purchases may range from 2% to 15% of an employee's base salary each pay period, subject to certain limitations. Currently, there are no shares of Hercules common stock registered for offer and sale under the plan. Shares issued at December 31, 2001 and 2000, were 1,758,081 and 1,597,861, respectively. The Company applies APB Opinion 25 and related interpretations in accounting for its Employee Stock Purchase Plan. Accordingly, no compensation cost has been recognized for the Employee Stock Purchase Plan.

Had compensation cost for Hercules' Stock-Based Incentive Plans and Employee Stock Purchase Plan been determined on the basis of fair value according to SFAS No. 123, the fair value of each option granted or share purchased would be estimated on the grant date using the Black-Scholes option pricing model.

The following weighted-average assumptions would be used in estimating fair value for 2001, 2000 and 1999:

Edgar Filing: HERCULES INC - Form 10-K/A

Assumption	Regular Plan	Performance Accelerated Plan	Employee Stock Purchase Plan
Dividend yield	0.96%	3.83%	0.0%
Risk-free interest rate	5.80%	5.57%	4.86%
Expected life	7.1	5 yrs.	3 mos.
Expected volatility	33.36%	29.78%	49.11%

The Company's net income and earnings per share for 2001, 2000 and 1999 would approximate the pro forma amounts below:

	(Dollars in millions)		
	2001	2000	1999
Net income			
As reported	\$ 4	\$ 25	\$ 33
Pro forma	\$ 3	\$ 24	\$ 33

9. ADDITIONAL BALANCE SHEET DETAIL

	(Dollars in millions)	
	2001	2000
Property, plant, and equipment		
Land	\$ 19	\$ 22
Buildings and equipment	396	399
Construction in progress	6	16
Total	421	437
Accumulated depreciation and amortization	151	133
Net property, plant, and equipment	\$ 270	\$ 304
Accrued expenses		
Payroll and employee benefits	\$ 19	\$ 29
Claims and litigation	3	8
Restructuring reserves (Note 11)	17	24
Other	35	32
Total	\$ 74	\$ 93

## Edgar Filing: HERCULES INC - Form 10-K/A

At December 31, 2001 and 2000, the goodwill and identified intangible assets, net were:

	(Dollars in millions)	
	2001	2000
	-----	-----
Goodwill	\$ 1,692	\$ 1,692
Customer relationships	330	330
Trademarks and tradenames	250	250
Other intangibles	145	145
	-----	-----
Total	2,417	2,417
Less accumulated amortization	(205)	(141)
	-----	-----
Net goodwill and other intangible assets	\$ 2,212	\$ 2,276
	=====	=====

### 11. RESTRUCTURING

The consolidated balance sheet reflects liabilities for employee severance benefits and other exit costs of \$17 million and \$24 million, respectively, at December 31, 2001 and 2000. During the third quarter of 2001, management authorized and committed to a plan to reduce the workforce as part of the comprehensive cost reduction and work process redesign program. The Company incurred restructuring charges of \$16 million, for employee termination benefits and exit costs related to facility closures. Under this plan, approximately 377 employees have left or will leave the Company. The plan includes reductions throughout the Company with the majority of them from support functions as well as the BetzDearborn and Pulp and Paper units.

The restructuring liabilities also include amounts relating to the 1998 plan initiated upon the acquisition of BetzDearborn and additional plans that the Company committed to in 2000 relating to the restructuring of the BetzDearborn and Pulp and Paper units. As a result of these plans, we estimate approximately 1,554 employees will be terminated, most of which have occurred since the inception of the aforementioned plans. Actions under the 1998 and 2000 plans were substantially complete as of December 31, 2000 and December 31, 2001, respectively.

Pursuant to the above plans, approximately 374 employees were terminated during the year ended December 31, 2001. Cash payments during 2001 and 2000 included \$16 million and \$23 million, respectively, for severance benefits and other exit costs. Severance benefits paid during the current year represent the continuing benefit streams of previously terminated employees as well as those terminated in the current year. During the second and third quarters of 2001, the Company completed assessments of the remaining expenditures for the 1998 BetzDearborn plan and the 2000 plans, respectively. As a result of these assessments, the estimates for severance benefits and other exit costs were lowered by \$22 million, with corresponding reductions to goodwill of \$10 million and \$12 million, respectively. The lower than planned severance benefits are the result of higher than anticipated attrition, with voluntary resignations not requiring the payment of termination benefits.

A reconciliation of activity with respect to the liabilities established for these plans is as follows:

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in millions)	
	2001	2000
	-----	-----
Balance at beginning of year	\$ 24	\$ 56
Cash payments	(16)	(23)
Additional termination benefits and exit costs	22	3
Reversals against goodwill	(10)	(12)
Other	(3)	--
	-----	-----
Balance at end of year	\$ 17	\$ 24
	=====	=====

12. EMPLOYEE STOCK OWNERSHIP PLAN (ESOP)

In connection with the acquisition of BetzDearborn in 1998, the Company acquired BetzDearborn's ESOP and related trust as a long-term benefit for substantially all of BetzDearborn's U.S. employees. The plan is a supplement to BetzDearborn's 401(k) plan. The ESOP trust had long-term debt of \$75 million and \$91 million at December 31, 2001

28

BETZDEARBORN INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

and 2000, respectively, which is guaranteed by Hercules. Upon acquisition, the debt had a fair value in excess of its recorded amount for which a \$16 million step-up was recorded and is being amortized over the remaining term of the debt. The fair value, included in long-term debt, was \$84 million and \$101 million at December 31, 2001 and 2000, respectively. The proceeds of the original loan were used to purchase BetzDearborn convertible preferred stock, which, at the date of acquisition, was converted into Hercules common stock.

Under the provisions of the BetzDearborn 401(k) program, employees may invest 2% to 15% of eligible compensation. The Company's matching contributions, made in the form of Hercules common stock, are equal to 50% of the first 6% of employee contributions, and fully vest to employees upon the completion of 5 years of service. The Company's matching contributions are included in ESOP expense.

The Company's contributions and dividends on the shares held by the trust are used to repay the loan, and the shares are allocated to participants as the principal and interest are paid. The Company's common stock dividends were suspended during the fourth quarter of 2000. Long-term debt is reduced as payments are made on the third party financing. In addition, unearned compensation is also reduced as the shares are allocated to employees. The unallocated shares held by the trust are reflected in unearned compensation as a reduction in net Hercules Group Investment on the balance sheet for \$104 million and \$115 million at December 31, 2001 and 2000, respectively.

	2001	2000
	-----	-----
Allocated	2,075,687	1,858,459

## Edgar Filing: HERCULES INC - Form 10-K/A

Unallocated	3,228,690	3,582,334
	-----	-----
Total shares held by ESOP	5,304,377	5,440,793
	=====	=====

The ESOP expense is calculated using the shares-allocated method and includes net interest incurred on the debt of \$8 million, \$6 million and \$5 million for 2001, 2000 and 1999, respectively. The Company is required to make quarterly contributions to the plan, which enable the trust to service its indebtedness. Net ESOP expense is comprised of the following elements:

	(Dollars in millions)		
	2001	2000	1999
	-----	-----	-----
ESOP expense	\$ 19	\$ 13	\$ 13
Common stock dividends (charged to net Hercules Group Investment)	--	(3)	(6)
	-----	-----	-----
Net ESOP expense	19	10	7
	-----	-----	-----
ESOP Contributions	\$ 15	\$ 10	\$ 9
	=====	=====	=====

### 13. PENSION AND OTHER POSTRETIREMENT BENEFITS

The Company participates in a defined benefit pension plan sponsored by Hercules, which covers substantially all employees of Hercules in the U.S. Benefits under this plan are based on average final pay and years of service. Hercules also provides post-retirement health care and life insurance benefits to eligible retired employees and their dependents.

Information on the actuarial present value of the benefit obligation and fair value of the plan assets is not presented as Hercules manages its U.S. employee benefit plans on a consolidated basis and such information is not maintained separately for the U.S. employees of the Company. The Company's statement of operations includes an allocation of the costs of the U.S. benefits plans. The pension costs were allocated based on percentage of pensionable wages, for each of the years presented; post-retirement benefit costs were allocated using factors derived from the relative net assets and revenues. Net pension income of Hercules allocated to the Company were \$6 million, \$8 million and \$7 million for the years ended December 31, 2001, 2000 and 1999, respectively, and post-retirement benefit expense was \$5.1 million, \$1 million and \$.6 million for the years ended December 31, 2001, 2000 and 1999, respectively.

The Company also has a number of defined pension plans which it provides to employees in locations other than the U.S. The following table lists benefit obligations, plan assets, and the funded status of these plans.

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in millions)	
	Pension benefits	
	2001	2000
	-----	-----
CHANGE IN BENEFIT OBLIGATION		
Benefit Obligation at January 1	\$ 108	\$ 104
Service cost	3	4
Interest cost	7	6
Assumption change	1	1
Employee contributions	1	1
Translation adjustment	(4)	(8)
Actuarial loss (gain)	11	3
Benefits paid from plan assets	(3)	(3)
	-----	-----
Benefit Obligation at December 31	\$ 124	\$ 108
	-----	-----
CHANGE IN PLAN ASSETS		
Fair value of plan assets at January 1	\$ 125	\$ 127
Actual return plan assets	(12)	7
Employee contributions	1	1
Company contributions	2	3
Actuarial loss (gain)	--	(2)
Translation adjustment	(4)	(8)
Benefits paid from plan assets	(3)	(3)
	-----	-----
Fair value of plan assets at December 31	\$ 109	\$ 125
	-----	-----
Funded status of the plans	\$ (15)	\$ 17
Unrecognized actuarial (gain)/loss	29	(4)
Unrecognized prior service cost	1	--
	-----	-----
Prepaid benefit cost	\$ 15	\$ 13
	-----	-----
AMOUNTS RECOGNIZED IN THE STATEMENT OF FINANCIAL POSITION CONSIST OF:		
Additional minimum liability	\$ (22)	\$ --
Intangible asset	1	--
Other comprehensive income	21	--
Prepaid benefit cost	15	13
	-----	-----
	\$ 15	\$ 13
	-----	-----
ASSUMPTIONS AS OF DECEMBER 31		
Weighted average discount rate	7.25%	6.5%
Expected return on plan assets	9.25%	6.7%
Rate of compensation increase	4.50%	4.5%
Health care term rate	N/A	N/A

	2001	2000	1999
	-----	-----	-----
COMPONENTS OF NET PERIODIC PENSION COST:			
Service cost	\$ 3	\$ 4	\$ 4
Interest cost	7	6	6
Return on plan assets expected	(10)	(9)	(8)
	-----	-----	-----

Edgar Filing: HERCULES INC - Form 10-K/A

Benefit cost	\$ --	\$ 1	\$ 2
	----	----	----

30

BETZDEARBORN INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

14. OTHER OPERATING EXPENSES, NET

Other operating expenses, net, consist of the following:

	(Dollars in millions)		
	2001	2000	1999
	----	----	----
Loss on asset dispositions	\$ 8	\$ 3	\$ --
Integration expenses	--	2	9
Royalties expense, net	25	16	(1)
Restructuring charges	16	1	2
Other	6	--	1
	----	----	----
	\$ 55	\$ 22	\$ 11
	=====	=====	=====

15. NET HERCULES GROUP INVESTMENT

Changes in Net Hercules Group Investment were as follows:

	(Dollars in millions)
Balance, January 1, 1999	\$ 2,541
Net income	33
Other comprehensive loss	(47)
Impact of shares held by ESOP	8
Intercompany balances, net	(102)
	-----
Balance, December 31, 1999	\$ 2,433
Net income	25
Other comprehensive loss	(46)
Impact of shares held by ESOP	7
Intercompany balances, net	(15)
	-----
Balance, December 31, 2000	\$ 2,404
Net income	4
Other comprehensive loss	(56)
Impact of shares held by ESOP	11
Intercompany balances, net	(10)
	-----
Balance, December 31, 2001	\$ 2,353
	=====



## Edgar Filing: HERCULES INC - Form 10-K/A

The Company includes accumulated other comprehensive loss in Net Hercules Group Investment. At December 31, 2001 accumulated and other comprehensive losses consisted of an additional minimum pension liability and foreign currency translation adjustments of \$15 million and \$118 million respectively. At December 31, 2000 and 1999, accumulated other comprehensive losses included \$77 million and \$31 million of foreign currency translation adjustments, respectively.

### 16. OTHER EXPENSE, NET

	(Dollars in millions)		
	2001	2000	1999
	----	----	----
Foreign currency transaction losses	\$ 1	\$ 5	\$ 5
Miscellaneous (income) expense	8	(2)	(4)
Equity in (income) of affiliated company	(2)	(1)	(1)
	---	---	---
	\$ 7	\$ 2	\$--
	===	===	===

31

### BETZDEARBORN INC NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### 17. COMMITMENTS AND CONTINGENCIES

##### Leases

-----

The Company has operating leases (including office space, transportation, and data processing equipment) expiring at various dates. Rental expense was \$27 million in 2001, \$22 million in 2000 and \$18 million in 1999.

At December 31, 2001, minimum rental payments under noncancelable leases aggregated \$30 million. The net minimum payments over the next five years are \$11 million in 2002, \$9 million in 2003, \$7 million in 2004, \$2 million in 2005 and \$1 million in 2006 and thereafter.

##### Litigation

-----

The Company is a defendant in numerous lawsuits that arise out of, and are incidental to the conduct of its business. In these legal proceedings, no specifically identified officer or affiliate is a party or a named defendant. These suits concern issues such as product liability, labor-related matters, property damage and personal injury matters.

At December 31, 2001 and 2000, the consolidated balance sheet reflects a current liability of approximately \$3 million and \$8 million, respectively, for litigation and claims. These amounts represent management's best estimate of the probable and reasonably estimable losses and recoveries related to litigation or claims. The extent of the liability and recovery is evaluated quarterly. While it is not feasible to predict the outcome of all pending suits and claims, the ultimate resolution of these matters could have a material effect upon the financial position of the Company, and the resolution of any of the matters

## Edgar Filing: HERCULES INC - Form 10-K/A

during a specific period could have a material effect on the quarterly or annual operating results for that period.

### Environmental

-----

The Company becomes aware of sites in which it may be named a PRP in investigatory and/or remedial activities through correspondence from the U.S. Environmental Protection Agency, or other government agencies, or through correspondence from previously named PRPs, who either request information or notify us of our potential liability. We have established procedures for identifying environmental issues at our plant sites. In addition to environmental audit programs, we have environmental coordinators who are familiar with environmental laws and regulations and act as a resource for identifying environmental issues.

The Company has established accruals for the estimated cost of environmental remediation and/or cleanup at various sites. The estimated range of the reasonable possible share of costs for investigation and cleanup is between \$1 million and \$3 million at December 31, 2001. The actual costs will depend upon numerous factors, including the number of parties found to be responsible at each environmental site and their ability to pay; the actual methods of remediation required or agreed to; the outcomes of negotiations with regulatory authorities; outcomes of litigation; changes in environmental laws and regulations; technological developments; and the number of years of remedial activity required, which could range from 0 to 30 years. As of December 31, 2001, the accrued liability of \$1 million for environmental remediation represents management's best estimate of the probable and reasonably estimable costs related to environmental remediation. The Company estimates that these liabilities will be paid over the next five years. The extent of liability is evaluated quarterly. The measurement of the liability is evaluated based on currently available information, including the process of remedial investigations at each site and the current status of negotiations with regulatory authorities regarding the method and extent of apportionment of costs among other potentially responsible parties. The Company is unaware of any unasserted claims and has not reflected them in the reserve. While it is not feasible to predict the outcome of all pending suits and claims, the ultimate resolution of these environmental matters could have a material effect upon the results of operations and the financial position of the Company.

### Other

-----

As of December 31, 2001, the Company had \$1.8 million in letters of credit outstanding with lenders.

## 18. RELATED PARTY TRANSACTIONS

The Company has entered into certain agreements with affiliated entities. These agreements were developed in the context of parent/subsidiary relationship and therefore may not necessarily reflect the result of arms-length negotiations between independent parties. The Company records sales with affiliates based on a cost-plus formula developed and agreed-upon by both parties.

Corporate and other allocations: As discussed in Note 1, the financial statements of the Company reflect certain allocated support costs incurred by other entities in Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, research & development overhead, investor relations and other corporate services. Allocations and

## Edgar Filing: HERCULES INC - Form 10-K/A

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

charges included in the Company's financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on factors such as revenues, net assets, costs of sales or a relative weighting of geographic activity. These allocations are presented separately in the consolidated statement of income.

**Royalty expense:** The Company entered into license agreements with affiliated companies, which pertain to licensing rights for certain patents, trademarks and know-how (technology) related to manufacturing formulations and specifications of specialty chemical products. Fees are both earned by and paid outside of this consolidated group. Beginning in the year 2000 and for seven years thereafter certain fees are to be split between BL Technologies, Inc. (a member of this consolidated group) and Hercules on a declining rights basis favoring Hercules in the later years. The net royalty expense is included as part of other operating expenses in the financial statements.

**Sales to affiliates:** The Company sells raw material and finished goods inventory in the normal course of business to affiliated companies. The Company's revenues from sales to affiliated companies are presented separately in the consolidated statement of income.

**Purchases from affiliates:** The Company purchases certain raw material and finished goods inventory from affiliated companies in the normal course of business. These purchases of inventory from affiliated companies are reflected in cost of sales in the consolidated statement of income and totaled \$45 million, \$62 million and \$56 million for the years ended 2001, 2000 and 1999 respectively.

**Intercompany borrowing and interest:** The Company has \$130 and \$289 million of intercompany loans with affiliated entities in 2001 and 2000, respectively. These intercompany loans are primarily with Hercules, the Hercules Shared Services Center, Inc., and SA Hercules Europe NV. The long-term debt payable to affiliates primarily has no set payment schedule and carry interest rates ranging from 4.60% to 12.42%. The loans with affiliates are recorded in the Net Hercules Group Investment in the consolidated balance sheet. Net interest paid to affiliated entities was \$16 million and \$19 million in 2001 and 2000, respectively.

#### 19. INCOME TAXES

The components of domestic and foreign income before taxes and minority interest are presented below:

	(Dollars in millions)		
	2001	2000	1999
	----	----	----
Domestic	\$ 35	\$ 46	\$ 78
Foreign	4	24	10
	----	----	----
	\$ 39	\$ 70	\$ 88
	=====	=====	=====

A summary of the components of the tax provision follows:

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in millions)		
	2001	2000	1999
	----	----	----
Currently payable			
Domestic	\$ 26	\$ 11	\$ 37
Foreign	11	10	5
Deferred			
Domestic	(1)	17	5
Foreign	(4)	2	4
	----	----	----
Provision for income taxes	\$ 32	\$ 40	\$ 51
	=====	=====	=====

33

BETZDEARBORN INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Deferred tax liabilities (assets) at December 31, consist of the following:

	(Dollars in millions)	
	2001	2000
	----	----
Depreciation	\$ 34	\$ 36
Intangible asset revaluation	\$ 1	\$ --
Amortization of intangible asset	241	249
Prepaid pension and post-retirement benefits	1	4
Other	2	2
	-----	-----
Gross deferred tax liabilities	279	291
Pension and other postretirement benefits	(19)	(26)
Accrued expenses	(6)	(17)
Loss carryforwards	(18)	(15)
Inventory	(4)	
Other	(8)	(6)
	-----	-----
Gross deferred tax assets	(55)	(64)
	-----	-----
Valuation allowance	17	15
	-----	-----
	\$ 241	\$ 242
	=====	=====

A reconciliation of the statutory income tax rate to the effective rate follows:

Edgar Filing: HERCULES INC - Form 10-K/A

	2001	2000	1999
	----	----	----
Statutory income tax rate	35.00%	35.00%	35.00%
Goodwill amortization	42.21	20.73	17.76
Non-deductible expenses	1.72	2.88	2.97
Valuation allowance	3.38	2.87	4.82
Other	--	(4.35)	(2.60)
	-----	-----	-----
Effective tax rate	82.31%	57.13%	57.95%
	=====	=====	=====

The Company provides taxes on undistributed earnings of foreign subsidiaries and affiliates included in Net Hercules Group Investment to the extent such earnings are planned to be remitted and not reinvested permanently. The undistributed foreign earnings of subsidiaries and affiliates on which no provision for foreign withholding or U.S. income taxes has been made amounted to approximately \$41 million, \$42 million and \$27 million at December 31, 2001, 2000 and 1999, respectively.

20. SUBSEQUENT EVENT

On April 29, 2002, Hercules completed the sale of its Water Treatment Business to GE Specialty Materials (GESM). Pursuant to the Stock and Asset Agreement for the transaction, the sale included all of the stock of BetzDearborn and the Company. Hercules used the proceeds from the sale to prepay borrowings under its Senior Credit Facility and ESOP Credit Facility. Pursuant to the prepayment, among other things, the stock pledges were released.

34

REPORT OF INDEPENDENT ACCOUNTANTS

TO THE SHAREHOLDERS AND THE BOARD OF DIRECTORS OF

HERCULES INCORPORATED  
WILMINGTON, DELAWARE

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations and comprehensive (loss) income and of cash flows present fairly, in all material respects, the financial position of BetzDearborn Canada, Inc., a subsidiary of Hercules Incorporated, and its majority controlled partnership at December 31, 2001 and 2000 and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

Edgar Filing: HERCULES INC - Form 10-K/A

PricewaterhouseCoopers LLP  
 Mississauga, Ontario  
 January 25, 2002, except for note 2, New accounting pronouncements, and note 18,  
 Subsequent event, which are as of November 8, 2002

35

BETZDEARBORN CANADA, INC.

Consolidated Statements of Operations and Comprehensive (Loss) Income

	(thousands of U.S. dollars)		
	Year ended December 31,		
	2001	2000	1999
	-----	-----	-----
Sales to third parties	\$ 136,404	\$ 167,668	\$ 158,833
Sales to Hercules Group	13,420	10,844	7,033
	-----	-----	-----
Net sales	149,824	178,512	165,866
Cost of sales	86,942	107,811	94,629
Selling, general and administrative expenses	35,827	40,979	48,114
Goodwill and intangible asset amortization	7,825	8,137	8,056
Other operating expense	11,367	6,487	5,203
	-----	-----	-----
Profit from operations	7,863	15,098	9,864
Interest and debt expense	4,996	5,075	7,717
Interest income	(1,071)	(1,090)	(529)
Other expense (income) (note 12)	1,057	540	(1,266)
	-----	-----	-----
Income before income taxes	2,881	10,573	3,942
Provision for income taxes (note 13)	2,205	5,362	2,685
	-----	-----	-----
Income before minority interest	676	5,211	1,257
Minority interest - held by affiliate	1,726	4,003	3,221
	-----	-----	-----
Net (loss) income	(1,050)	1,208	(1,964)
Translation adjustments	(15,359)	(8,897)	16,261
	-----	-----	-----
Comprehensive (loss) income	\$ (16,409)	\$ (7,689)	\$ 14,297
	=====	=====	=====

The accompanying accounting policies and notes are an integral part of the consolidated financial statements.

36

Edgar Filing: HERCULES INC - Form 10-K/A

BETZDEARBORN CANADA, INC.

Consolidated Balance Sheets

	(thousands of U.S. dollars)	
	December 31,	
	2001	2000
	-----	-----
ASSETS		
Current assets		
Cash and cash equivalents	\$ --	\$ 4
Accounts receivable - net (note 3)	21,619	28,896
Inventories (note 4)	10,886	13,465
Assets held for sale	3,419	--
	-----	-----
Total current assets	35,924	42,365
Property, plant and equipment - net (note 8)	15,155	21,595
Goodwill and other intangible assets - net (note 9)	265,197	288,307
Pension and other post-retirement benefits (note 11)	4,388	5,095
Deferred charges and other assets	736	773
	-----	-----
Total assets	\$ 321,400	\$ 358,135
	=====	=====
LIABILITIES AND NET HERCULES GROUP INVESTMENT		
Current liabilities		
Bank overdraft (note 5)	\$ 3,298	\$ 1,351
Accounts payable	11,377	10,272
Accrued expenses (note 8)	11,035	4,415
	-----	-----
Total current liabilities	25,710	16,038
Long-term debt (note 6)	65,427	83,434
Deferred income taxes (note 13)	--	2,449
Deferred charges	235	--
	-----	-----
Total liabilities	91,372	101,921
	-----	-----
Commitments and contingencies (note 16)	--	--
	-----	-----
Minority interest - held by affiliate	7,442	11,874
	-----	-----
Net Hercules Group investment (note 15)		
Accumulated other comprehensive (loss) income	(10,517)	4,842
Intercompany transactions (note 14)	233,103	239,498
	-----	-----
Net Hercules Group investment	222,586	244,340
	-----	-----
Total liabilities and net Hercules Group investment	\$ 321,400	\$ 358,135
	=====	=====

The accompanying accounting policies and notes are an integral part of the

# Edgar Filing: HERCULES INC - Form 10-K/A

consolidated financial statements.

37

BETZDEARBORN CANADA, INC.

## Consolidated Statements of Cash Flows

	(thousands of U.S. dollars)	
	2001	2000
	-----	-----
<b>CASH FLOW FROM OPERATING ACTIVITIES:</b>		
Net (loss) income	\$ (1,050)	\$ 1,208
Adjustments to reconcile net income (loss) to net cash provided from operations:		
Minority interest - held by affiliate	1,726	4,003
Depreciation	2,634	2,492
Amortization	7,825	8,137
Loss on disposals of property, plant and equipment	--	--
Write-off of property, plant and equipment	906	21
Deferred tax (recovery) expense	(2,296)	776
Pension and other post-retirement benefits expense	626	496
Corporate and other cost allocations	1,180	3,067
Accruals and deferrals of cash receipts and payments		
Accounts receivable	8,047	(3,445)
Income taxes receivable/payable	(1,075)	2,888
Inventories	2,967	973
Prepaid expenses	--	--
Pension and other post-retirement benefit contributions	(173)	(902)
Accounts payable and accrued expenses	8,064	1,312
Non-current assets and liabilities	322	(558)
Transfers (to) from Hercules Group	(14,518)	2,793
Net cash provided by operations	15,185	23,261
<b>CASH FLOW FROM INVESTING ACTIVITIES:</b>		
Capital expenditures	(1,552)	(2,424)
Software expenditures	--	(114)
Proceeds of disposal of property, plant and equipment	--	--
Net cash used in investing activities	(1,552)	(2,538)
<b>CASH FLOW FROM FINANCING ACTIVITIES:</b>		
Transfers from (to) Hercules Group	5,649	(13,566)
Long-term debt repayments	(14,454)	(54)
Payments to minority interest - affiliated company	(6,524)	(7,904)
Increase (decrease) in bank overdraft	1,947	(970)
Net cash used in financing activities	(13,382)	(22,494)
Effect of exchange rate changes on cash	(255)	(338)



## Edgar Filing: HERCULES INC - Form 10-K/A

Net decrease in cash and cash equivalents	(4)	(2,109)
Cash and cash equivalents - Beginning of year	4	2,113
Cash and cash equivalents - End of year	\$ --	\$ 4

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:

Cash paid during the year for:

Interest	\$ 5,032	\$ 5,256
Income taxes	5,573	1,747

Non-cash financing activities:

Corporate and other cost allocations	\$ 1,180	\$ 3,067
--------------------------------------	----------	----------

The accompanying accounting policies and notes are an integral part of the consolidated financial statements.

38

BETZDEARBORN CANADA, INC.

Notes to Consolidated Financial Statements

1 DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

BetzDearborn Canada, Inc. (BDCI or the Company) is 100% owned by BetzDearborn Inc., which in turn is 100% owned by Hercules Incorporated (Hercules). BDCI is engaged in providing products and services in the areas of process chemicals and services, functional products, and chemical specialties to the Canadian marketplace.

Historically, separate company stand-alone financial statements were not prepared for BDCI. In November 2000, Hercules amended its senior credit facility and ESOP credit facility (the Facilities). The Facilities, as amended, were secured by liens on Hercules' property and assets (and those of Hercules' Canadian subsidiaries, including BDCI), a pledge of the stock and partnership and member interests of substantially all of Hercules' U.S.A. subsidiaries and 65% of the stock of non-U.S.A. subsidiaries directly owned by Hercules, including BDCI, and a pledge of Hercules' U.S. intercompany indebtedness. These financial statements present the financial information on BDCI, a collateral party to the Hercules debt, based on Hercules' understanding of the Securities and Exchange Commission's interpretation and application of Rule 3-16 under the Securities and Exchange Commission's Regulation S-X. These statements were derived from historical accounting records.

On April 29, 2002, in connection with Hercules' sale of its Water Treatment Business (Water Treatment Business) (notes 6 and 18) and the repayment of the Facilities, the stock pledges were released. As a result, based on Hercules' current debt structure, these separate company stand-alone financial statements will not be required for the fiscal year ending December 31, 2002.

When Hercules acquired all of the outstanding shares of BetzDearborn Inc. on October 15, 1998, it paid \$2,235 million in cash and \$186 million in common stock exchanged for the shares held by the BetzDearborn ESOP Trust.

## Edgar Filing: HERCULES INC - Form 10-K/A

As a result of this acquisition, Hercules initiated a global process of internal reorganization, in which the Company entered into an agreement with Hercules Canada, Inc. to transfer its business to a newly created partnership, Hercules Canada Partnership (HCP or the partnership). The Company has a 71.92% share of future profits from the partnership. Since this reorganization is under the common control of Hercules, the transactions have been accounted for in a manner similar to a pooling of interest. The purchase price allocated to the Company and its subsidiary was approximately \$295 million. During 1999, Hercules completed the purchase price allocation and the final determination of goodwill was \$2,170 million of which the amount attributable to the Company was approximately \$300 million. These financial statements include the push down of fair value adjustments to assets and liabilities, including goodwill, other intangible assets and property, plant and equipment and their related amortization and depreciation adjustments.

The financial statements of BDCI reflect certain allocated support costs incurred by other entities in the Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations and charges included in BDCI's financial statements were based on either a direct cost pass-through for items directly identified as related to BDCI's activities; a percentage allocation for such services provided based on factors such as sales, net assets, or cost of sales; or a relative weighting of geographic activity. Management believes that the allocation methods are reasonable.

39

BETZDEARBORN CANADA, INC.

Notes to Consolidated Financial Statements

-----

### 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of BetzDearborn Canada, Inc. and its majority controlled partnership, Hercules Canada Partnership. This partnership is located in Mississauga, Ontario, Canada. All material intercompany transactions and profits have been eliminated.

#### USE OF ESTIMATES

Preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

#### REVENUE RECOGNITION

The Company recognizes revenue when the earnings process is complete. This generally occurs when products are shipped to the customer or services are performed in accordance with terms of the agreement, title and risk of loss have been transferred, collectibility is probable, and pricing is fixed and determinable. Accruals are made for sales returns and other allowances based on the Company's experience. Gross shipping and handling

## Edgar Filing: HERCULES INC - Form 10-K/A

charges are included in revenue with the corresponding shipping and handling costs included in cost of sales.

### CASH AND CASH EQUIVALENTS

Cash equivalents include commercial paper and other securities with original maturities of 90 days or less. Book value approximates fair value because of the short maturity of those instruments.

### INVENTORIES

Inventories are stated at the lower of cost or market. Cost includes the cost of raw materials, direct labor and an allocation of overhead. Inventories are valued on the standard cost method, which approximates average cost.

### PROPERTY AND DEPRECIATION

Property, plant and equipment are stated at cost and depreciated using the straight-line method. The estimated useful lives of depreciable assets are as follows: buildings - 30 years; plant, machinery and equipment - 15 years; other machinery and equipment - 3 to 15 years.

Maintenance, repairs, and minor renewals are charged to income; major renewals and betterments are capitalized. Upon normal retirement or replacement, the net book value of property (less proceeds of sale or salvage) is charged to income.

40

BETZDEARBORN CANADA, INC.

Notes to Consolidated Financial Statements

---

### GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill and other intangible assets are amortized on a straight-line basis over the estimated future periods to be benefited, generally 40 years for goodwill and 5 to 15 years for other intangible assets.

### LONG-LIVED ASSETS

The Company reviews its long-lived assets, including goodwill and other intangibles, for impairment whenever events or changes in circumstances indicate carrying amounts of the assets may not be recoverable through undiscounted future cash flows. If an impairment loss has occurred based on expected future cash flows (undiscounted), the loss is recognized in the consolidated statements of operations. The amount of the impairment loss is the excess of the carrying amount of the impaired asset over the fair value of the asset. The fair value represents expected future cash flows from the use of the assets, discounted at the rate used to evaluate potential investments.

### INCOME TAXES

The provisions for income taxes have been determined using the asset and liability approach of accounting for income taxes. Under this approach, deferred income taxes represent the future tax consequences expected to occur when the reported amounts of assets and liabilities are recovered or paid. The provision for income taxes represents income taxes paid or

## Edgar Filing: HERCULES INC - Form 10-K/A

payable for the current year plus the change in deferred taxes during the year. Deferred income taxes result from differences between the financial and tax basis of the Company's assets and liabilities and are adjusted for changes in tax rates and tax laws when changes are enacted. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized.

### FOREIGN CURRENCY TRANSLATION AND TRANSACTIONS

The accompanying consolidated financial statements are reported in U.S. dollars. The Canadian dollar is the functional currency for the Company and the partnership. The translation of the functional currency into U.S. dollars (reporting currency) is performed for assets and liabilities using the current exchange rates in effect at the balance sheets dates, and for revenues, costs and expenses using average exchange rates prevailing during the reporting periods. Adjustments resulting from the translation of functional currency financial statements to reporting currency are accumulated and reported as other comprehensive (loss) income, a component of net Hercules Group investment.

Transactions in foreign currency are recorded at the exchange rate prevailing on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are expressed in the functional currency at the exchange rates in effect at the balance sheets dates. Revenues, costs and expenses are recorded using average exchange rates prevailing during the reporting periods. Gains or losses resulting from foreign currency transactions are included in the consolidated statements of operations.

41

BETZDEARBORN CANADA, INC.

Notes to Consolidated Financial Statements

---

### CONCENTRATION OF CREDIT RISK

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of trade receivables. Concentrations of credit risk with respect to trade receivables are limited due to the Company's large number of customers and their dispersion across many different industries and locations.

### FINANCIAL INSTRUMENTS

The Company uses various non-derivative financial instruments, including letters of credit, and generally does not require collateral to support its financial instruments.

### STOCK-BASED COMPENSATION

Compensation costs attributable to stock option and similar plans are recognized based on any excess of the quoted market price of the stock on the date of grant over the amount the employee is required to pay to acquire the stock (the intrinsic-value method under Accounting Principles Board Opinion 25 (APB 25)). Such amount, if any, is accrued over the related vesting period, as appropriate. Statement of Financial Accounting Standard No. 123, Accounting for Stock-based Compensation, requires companies electing to continue to use the intrinsic-value method to make

## Edgar Filing: HERCULES INC - Form 10-K/A

pro forma disclosures of net income as if the fair value based method of accounting had been applied.

### NET HERCULES GROUP INVESTMENT

The net Hercules Group investment account reflects the balance of BDCI's historical earnings, intercompany amounts, foreign currency translation and other transactions between BDCI and the Hercules Group.

### NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 141, "Business Combinations" (SFAS 141), and Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (SFAS 142). SFAS 141 supersedes Accounting Principles Board Opinion (APB) No. 16, Business Combinations. The provisions of SFAS 141 (1) require that the purchase method of accounting be used for all business combinations initiated after June 30, 2001, (2) provide specific criteria for the initial recognition and measurement of intangible assets apart from goodwill and (3) require that unamortized negative goodwill be written off immediately as extraordinary gain instead of being deferred and amortized. SFAS 141 also requires that upon adoption of SFAS 142, the Company reclassify the carrying amounts of certain intangible assets into or out of goodwill, based on certain criteria. SFAS 142 supersedes APB No. 17, Intangible Assets, and is effective for fiscal years beginning after December 15, 2001. SFAS 142 primarily addresses the accounting for goodwill and intangible assets subsequent to their initial recognition. The provisions of SFAS 142 (1) prohibit the amortization of goodwill and indefinite-lived intangible assets, (2) require that goodwill and indefinite-lived intangible assets be tested annually for impairment (and in interim periods if certain events occur indicating that the carrying value of goodwill and/or indefinite-lived intangible assets may be impaired), based on fair value (as opposed to cost recovery using future undiscounted cash flows), (3) require that reporting units be identified for the purpose of assessing potential future impairments of goodwill and (4) remove the forty-year limitation on the amortization period of intangible assets that have finite lives.

42

BETZDEARBORN CANADA, INC.

Notes to Consolidated Financial Statements

---

Effective January 1, 2002, Hercules adopted the provisions of SFAS 142. Hercules identified the following reporting units: BetzDearborn and Pulp and Paper, Aqualon and Fiber Visions. In connection with Hercules' transitional review, recorded goodwill was determined to be impaired in the BetzDearborn reporting unit. In the first quarter of 2002, Hercules completed its transitional impairment review of the identified reporting units and recognized an after tax impairment loss of \$368 million as a cumulative effect of a change in accounting principle. As a result of Hercules' adoption of SFAS 142, the Company will no longer record \$7,825 thousand of annual amortization relating to existing goodwill and intangibles.

Goodwill related to the BetzDearborn business was evaluated for impairment at December 31, 2001 under Statement of Financial Accounting Standards No. 121, "Accounting for the Impairment of Long-Lived Assets and for

## Edgar Filing: HERCULES INC - Form 10-K/A

Long-Lived Assets to Be Disposed of". Such evaluation indicated that goodwill associated with the business was recoverable from anticipated future undiscounted cash flows. Accordingly, no impairment loss was recorded in the December 31, 2001 financial statements.

In June 2001, the FASB approved the issuance of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" (SFAS 143). SFAS 143 establishes accounting standards for the recognition and measurement of legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 will become effective for the Company on January 1, 2003 and requires recognition of a liability for an asset retirement obligation in the period in which it is incurred. The Company does not believe it will have a material effect on its financial statements.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" (SFAS 144). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company does not believe it will have a material effect on its financial statements.

In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44 and 64, Amendment to FASB Statement No. 13, and Technical Corrections". The Company elected to early adopt the provisions of SFAS 145 related to the rescission of SFAS 4, "Reporting Gains and Losses from the Extinguishment of Debt" (SFAS 4). The early adoption had no effect on the Company's financial statements.

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" (SFAS 146). SFAS 146 addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs in a Restructuring)". SFAS 146 defines the timing of the recognition of costs associated with exit or disposal activities, the types of costs that may be recognized and the methodology for calculating the fair value of such costs. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. The Company is in the process of evaluating the impact of this standard but it does not believe this statement will have a material effect on its financial statements.

43

BETZDEARBORN CANADA, INC.

Notes to Consolidated Financial Statements

---

### 3 ACCOUNTS RECEIVABLE - NET

Accounts receivable - net consist of:

(thousands of U.S. dollars)

2001                      2000

-----                      -----

Edgar Filing: HERCULES INC - Form 10-K/A

Trade	\$21,855	\$27,225
Other	596	2,672
	-----	-----
Gross accounts receivable	22,451	29,897
Less: Allowance for doubtful accounts	832	1,001
	-----	-----
Total	\$21,619	\$28,896
	=====	=====

4 INVENTORIES

The components of inventories are:

	(thousands of U.S. dollars)	
	2001	2000
	-----	-----
Finished products	\$ 5,862	\$ 7,224
Materials, supplies and work-in-process	5,024	6,241
	-----	-----
Total	\$10,886	\$13,465
	=====	=====

5 BANK OVERDRAFT

Bank borrowings represent primarily overdraft facilities and short-term lines of credit, which are payable on demand with interest at various rates. Book values of bank borrowings approximate market value because of their short maturity period.

At December 31, 2001, the Company had \$3,097 thousand of unused lines of credit that may be drawn as needed, with interest at a negotiated spread over lenders' cost of funds. Lines of credit unused at December 31, 2000 totalled \$3,309 thousand. Weighted average interest rates on short-term borrowings at December 31, 2001 and 2000 were 6% and 7.5%, respectively. Lines of credit are repayable in Canadian funds.

6 LONG-TERM DEBT

The Company's bank loan facility of up to the equivalent of US\$100 million from select lenders in Canada (the Canadian Revolver) is a component of the Hercules' \$3,650 million credit facility with a syndicate of banks, which is due in 2003. The bank loan facility is drawn in the form of bankers' acceptances, is repayable in Canadian funds and bears interest at bankers' acceptance rates plus 2.25%. The interest prepaid on the bankers' acceptances is included in the net payable amount. The Company's assets and 65% of its common shares are pledged as collateral on the Hercules'

## Edgar Filing: HERCULES INC - Form 10-K/A

credit facility.

Effective with the consummation of the sale of the Water Treatment Business on April 29, 2002 (Note 18) and the application of the net proceeds by Hercules to repay in full borrowings under the Facilities, the Canadian revolving credit agreement was cancelled.

The Company believes that the carrying value of other borrowings approximates fair market value, based on discounting future cash flows using rates currently available for debt of similar terms and remaining maturities.

Interest expense for the year on long-term debt was \$4,996 thousand (2000 - \$5,075 thousand; 1999 - \$7,717 thousand).

### 7 LONG-TERM INCENTIVE COMPENSATION PLANS

BDCI participates in long-term incentive compensation plans sponsored by Hercules. These plans provide for the grant of stock options and the award of common stock and other market-based units to certain key employees and non-employee directors.

In 1995, Hercules changed the structure of the long-term incentive compensation plans to place a greater emphasis on shareholder value creation through grants of regular stock options, performance-accelerated stock options, and Cash Value Awards (performance-based awards denominated in cash and payable in shares of common or restricted stock, subject to the same restrictions as restricted stock). Restricted stock and other market-based units are awarded with respect to certain programs. The number of awarded shares outstanding was 189,704 at December 31, 2001 and 491,488 and 926,689 at December 31, 2000 and 1999, respectively.

At December 31, 2001, under Hercules' incentive compensation plans, 1,265,493 shares of common stock were available for grant as stock awards or stock option awards. Stock awards are limited to approximately 15% of the total authorizations. Regular stock options are granted at the market price on the date of grant and are exercisable at various periods from one to five years after date of grant. Performance-accelerated stock options are also granted at the market price on the date of grant and are normally exercisable at nine and one-half years. Exercisability may be accelerated based upon the achievement of predetermined performance goals. Both regular and performance-accelerated stock options expire ten years after the date of grant.

Restricted shares, options and performance-accelerated stock options are forfeited and revert to Hercules in the event of employment termination, except in the case of death, disability, retirement, or other specified events.

45

BETZDEARBORN CANADA, INC.

Notes to Consolidated Financial Statements

-----  
The Company applies APB 25 in accounting for its plans. Accordingly, no compensation cost has been recognized for the stock option plans. There were no charges to income for the cost of stock awards over the restriction or performance period for 2001, 2000 and 1999, respectively.

Below is a summary of outstanding stock option grants under the incentive compensation plans during 1999, 2000 and 2001:



Edgar Filing: HERCULES INC - Form 10-K/A

	Regular Number of shares -----	Weighted- average price -----
December 31, 1998	20,100	\$39.71
Granted	33,850	37.75
Exercised	--	--
Forfeited	--	--
-----		
December 31, 1999	53,950	\$38.48
Granted	--	--
Exercised	--	--
Forfeited	--	--
-----		
December 31, 2000	53,950	\$38.48
Granted	--	--
Exercised	--	--
Forfeited	--	--
-----		
December 31, 2001	53,950	\$38.48

There were no performance-accelerated stock options granted or outstanding during 1999, 2000 and 2001.

The weighted-average fair value of regular stock options granted during 1999 was \$8.26.

Following is a summary of regular stock options exercisable at December 31, 1999, 2000 and 2001 and their respective weighted-average share prices:

Options exercisable	Number of shares -----	Weighted- average exercise price -----
December 31, 1999	15,880	\$39.60
December 31, 2000	33,540	38.89
December 31, 2001	47,180	38.58

Following is a summary of stock options outstanding at December 31, 2001:

Edgar Filing: HERCULES INC - Form 10-K/A

Exercise price range	Outstanding options		
	Number outstanding at December 31, 2001	Weighted-average remaining contractual life	Weighted- average exercise price
Regular stock options			
\$30 - \$40	53,450	6.74	\$ 38.39
\$40 - \$50	500	6.35	47.81
	53,950		

The Company's employees may also participate in the Hercules Employee Stock Purchase Plan (ESPP). The ESPP is a qualified non-compensatory plan, which allows eligible employees to acquire shares of common stock through systematic payroll deductions. The plan consists of three-month subscription periods, beginning July 1 of each year. The purchase price is 85% of the fair market value of the common stock on either the first or last day of that subscription period, whichever is lower. Purchases may range from 2% to 15% of an employee's base salary each pay period, subject to certain limitations. Currently, there are no shares of Hercules common stock registered for offer and sale under the plan. Shares issued at December 31, 2001 and 2000 were 1,758,081 and 1,597,861, respectively. The Company applies APB 25 and related interpretations in accounting for the ESPP of Hercules. Accordingly, no compensation cost has been recognized for the ESPP.

Had compensation cost for Hercules' Stock-Based Incentive Plans and ESPP been determined on the basis of fair value according to SFAS 123, the fair value of each option granted or share purchased would be estimated on the grant date using the Black-Scholes option pricing model.

The following weighted-average assumptions would be used in estimating fair value for 2001, 2000 and 1999:

Assumption	Regular plan	Performance accelerated
Dividend yield	0.96%	3%
Risk-free interest rate	5.80%	5%
Expected life	7.1 years	5%
Expected volatility	33.36%	29%

The Company's net income (loss) for 2001, 2000 and 1999 would approximate the pro forma amounts below:

(thousands of U.S. dollars)		
2001	2000	1999

Edgar Filing: HERCULES INC - Form 10-K/A

Net income (loss)			
As reported	\$ (1,050)	\$ 1,208	\$ (1,964)
Pro forma	(1,107)	1,130	(2,028)

47

BETZDEARBORN CANADA, INC.  
Notes to Consolidated Financial Statements

8 ADDITIONAL BALANCE SHEET DETAIL

	(thousands of U.S. dollars)	
	2001	2000
	-----	-----
Property, plant and equipment		
Land	\$ 142	\$ 1,632
Buildings and equipment	26,783	32,134
Construction-in-progress	1,387	1,838
	-----	-----
Total	28,312	35,604
Less: Accumulated depreciation and amortization	13,157	14,009
	-----	-----
Net property, plant and equipment	\$15,155	\$21,595
	=====	=====
Accrued expenses		
Payroll and employee benefits	\$ 1,818	\$ 934
Income taxes payable	2,041	3,104
Restructuring liability (note 10)	4,301	212
Other	2,875	165
	-----	-----
Total	\$11,035	\$ 4,415
	=====	=====

9 GOODWILL AND OTHER INTANGIBLE ASSETS - NET

At December 31, 2001 and 2000, the goodwill and other intangible assets were:

	(thousands of U.S. dollars)	
	2001	2000
	-----	-----
Goodwill	\$298,734	\$298,734
Other intangibles	6,672	6,672
	-----	-----
Total	305,406	305,406
Less: Accumulated amortization	40,209	17,099
	-----	-----
Net goodwill and other intangible assets	\$265,197	\$288,307
	=====	=====

BETZDEARBORN CANADA, INC.  
Notes to Consolidated Financial Statements

---

10 RESTRUCTURING

The consolidated balance sheets reflect liabilities for employee severance benefits and other exit costs of \$4.3 million and \$0.2 million, respectively, at December 31, 2001 and 2000. During the third quarter of 2001, management authorized and committed to a plan to reduce the workforce as part of the comprehensive cost reduction and work process redesign program. The Company incurred restructuring charges of \$4.1 million, which includes charges of \$1.8 million for employee termination benefits and \$2.3 million for exit costs related to facility closures. Under this plan, approximately 48 employees have left or will leave the Company. The plan includes reductions throughout the Company with the majority of them from support functions as well as the Process Chemicals and Services segment.

The restructuring liabilities also include amounts relating to the 1998 plan initiated upon the acquisition of BetzDearborn and additional plans that the Company committed to in 2000 relating to the restructuring of the Process Chemicals and Services segment and corporate realignment due to the divestiture of non-core businesses.

A reconciliation of activity with respect to the liabilities established for these plans is as follows:

	(thousands of U.S. dollars)	
	2001	2000
	-----	-----
Balance - Beginning of year	\$ 212	\$ 2,562
Cash payments	--	(2,317)
Additional termination benefits and exit costs	4,101	--
Translation adjustment	(12)	(33)
	-----	-----
Balance - End of year	\$ 4,301	\$ 212
	=====	=====

Severance benefit payments are based on years of service and generally continue for 3 to 24 months subsequent to termination. Actions under the 1998 and 1999 restructuring plans are substantially complete as of December 31, 2001.

BETZDEARBORN CANADA, INC.  
Notes to Consolidated Financial Statements

---

Edgar Filing: HERCULES INC - Form 10-K/A

11 PENSION AND OTHER POST-RETIREMENT BENEFITS

The Company provides defined benefit pension and post-retirement benefit plans to employees. The following chart lists benefit obligations, plan assets, and funded status of the plans:

	(thousands of U.S. dollars)			
	Pension benefits		Other post-retirement	
	2001	2000	2001	2000
<b>CHANGE IN BENEFIT OBLIGATION</b>				
Benefit obligation at January 1	\$ 28,092	\$ 25,426	\$ 1,635	\$
Service cost	1,115	1,086	42	
Interest cost	1,998	1,994	114	
Assumption change	--	1,371	--	
Translation difference	(1,594)	(876)	(95)	
Actuarial (loss) gain	(752)	(20)	64	
Benefits paid from plan assets	(608)	(889)	(61)	
Benefit obligation at December 31	\$ 28,251	\$ 28,092	\$ 1,699	\$
<b>CHANGE IN PLAN ASSETS</b>				
Fair value of plan assets at January 1	\$ 35,505	\$ 34,825	\$ --	\$
Actual return on plan assets	(2,250)	1,856	--	
Company contributions	112	841	61	
Translation difference	(1,789)	(1,128)	--	
Benefits paid from plan assets	(608)	(889)	(61)	
Fair value of plan assets at December 31	\$ 30,970	\$ 35,505	\$ --	\$
Funded status of the plans	\$ 2,719	\$ 7,413	\$ (1,699)	\$
Unrecognized actuarial gain (loss)	2,824	(1,922)	(214)	
Unrecognized prior service cost	176	269	--	
Unrecognized net transition obligation	(525)	(26)	1,107	
Prepaid (accrued) benefit cost	\$ 5,194	\$ 5,734	\$ (806)	\$
<b>Assumptions as of December 31</b>				
Weighted-average discount rate	7%	7%	6.75%	
Expected return on plan assets	7.5%	7%	N/A	
Rate of compensation increase	4%	4%	4%	
Health-care trend rate	N/A	N/A	4%	
Funded status of plans in deficit position	(943)	(855)	(1,699)	

## Edgar Filing: HERCULES INC - Form 10-K/A

### Notes to Consolidated Financial Statements

	(thousands of U.S. dollars)				
	Pension benefits			Other post-retirement be	
	2001	2000	1999	2001	2000
	-----	-----	-----	-----	-----
Service cost	\$ 1,115	\$ 1,086	\$ 1,027	\$ 42	\$ 42
Interest cost	1,998	1,994	1,800	114	115
Expected return on plan assets	(2,620)	(2,688)	(2,132)	--	--
Amortization and deferrals	9	16	112	--	--
Amortization of transition asset	(183)	(189)	(187)	116	120
Special termination benefit	35	--	--	--	--
	-----	-----	-----	-----	-----
Benefit cost	\$ 354	\$ 219	\$ 620	\$ 272	\$ 277
	=====	=====	=====	=====	=====

#### OTHER POST-RETIREMENT BENEFITS

The non-pension post-retirement benefit plans are contributory health-care and life insurance plans. The assumed participation rate in these plans for future eligible retirees was 95% for health care and 95% for life insurance. A one-percentage point increase or decrease in the assumed health-care cost trend rate would increase or decrease the post-retirement benefit obligation by \$179 thousand or \$157 thousand, respectively, and would not have a material effect on aggregate service and interest cost components.

#### 12 OTHER EXPENSE (INCOME)

Other expense (income) consists of the following:

	(thousands of U.S. dollars)		
	2001	2000	1999
	-----	-----	-----
Foreign exchange loss (gain)	\$ 714	\$ 226	\$ (927)
Miscellaneous expense (income)	343	314	(339)
	-----	-----	-----
	\$ 1,057	\$ 540	\$ (1,266)
	=====	=====	=====

Edgar Filing: HERCULES INC - Form 10-K/A

13 INCOME TAXES

A summary of the components of the tax provision follows:

	(thousands of U.S. dollars)		
	Year ended December 31,		
	2001	2000	1999
	-----	-----	-----
Current	\$ 4,501	\$ 4,586	\$ 783
Deferred	(2,296)	776	1,902
	-----	-----	-----
Provision for income taxes	\$ 2,205	\$ 5,362	\$ 2,685
	=====	=====	=====

The deferred income tax asset (liability) at December 31 is comprised of:

	(thousands of U.S. dollars)	
	2001	2000
	-----	-----
Accrued expenses	\$ 1,267	\$ 90
	-----	-----
Gross deferred tax assets	1,267	90
	-----	-----
Depreciation	127	906
Prepaid pension and post-retirement benefits	1,037	1,599
Other	70	34
	-----	-----
Gross deferred tax liabilities	1,234	2,539
	-----	-----
Total deferred income tax asset (liability)	\$ 33	\$ (2,449)
	=====	=====

A reconciliation of the Canadian statutory income tax rate to the effective rate is as follows:

	2001	2000	1999
	-----	-----	-----
Statutory income tax rate	40.62%	40.14%	40.54%
Minority interest in income	(24.62)	(15.20)	(33.12)
Goodwill amortization	80.39	22.36	53.73
Non-deductible expenses	3.21	1.76	5.07
Large corporations tax	--	1.64	3.43
Change in enacted deferred tax rates	4.10	--	--
Prior year recovery	(29.37)	--	--
Other	2.21	0.01	(1.54)
	-----	-----	-----
Effective tax rate	76.54%	50.71%	68.11%
	=====	=====	=====

BETZDEARBORN CANADA, INC.  
Notes to Consolidated Financial Statements

---

14 INTERCOMPANY NOTES RECEIVABLE

In addition to current receivables and payables with the Hercules Group, BDCI has intercompany notes receivable from the Hercules Group in the amount of \$27,340 thousand (2000 - \$23,088 thousand), which is included in the net Hercules Group investment balance as of December 31, 2001 and 2000. The weighted average rate on the intercompany notes receivable was 6% in 2001 and 10% in 2000. The notes receivable are due on demand. Interest income earned on intercompany notes receivable for the year was \$1,071 thousand (2000 - \$1,090 thousand; 1999 - \$529 thousand).

15 NET HERCULES GROUP INVESTMENT

Changes in net Hercules Group investment were as follows:

	(thousands of U.S. dollars)
Balance - January 1, 1999	\$ 170,317
Net loss	(1,964)
Other comprehensive income	16,261
Intercompany transactions - net	76,920
	-----
Balance - December 31, 1999	261,534
Net income	1,208
Other comprehensive loss	(8,897)
Intercompany transactions - net	(9,505)
	-----
Balance - December 31, 2000	244,340
Net income	(1,050)
Other comprehensive loss	(15,359)
Intercompany transactions - net	(5,345)
	-----
Balance - December 31, 2001	\$ 222,586
	=====

The Company includes accumulated other comprehensive income (loss) in net Hercules Group investment. At December 31, 2001 and 2000, accumulated other comprehensive (loss) income included a cumulative loss of \$10,517 thousand and a cumulative gain of \$4,842 thousand, respectively, of foreign currency translation adjustments.

BETZDEARBORN CANADA, INC.  
Notes to Consolidated Financial Statements

---



## Edgar Filing: HERCULES INC - Form 10-K/A

### 16 COMMITMENTS AND CONTINGENCIES

#### LEASES

The Company has operating leases (including facilities, transportation, and data processing equipment) expiring at various dates. Rental expense was \$2,457 thousand in 2001, \$2,474 thousand in 2000 and \$2,379 thousand in 1999.

At December 31, 2001, minimum rental payments under noncancelable leases aggregated \$4,017 thousand. A significant portion of these payments relates to facilities and vehicles. The net minimum payments over the next three years are \$2,170 thousand in 2002, \$1,310 thousand in 2003, and \$537 thousand in 2004.

#### LITIGATION

The Company currently and from time to time is involved in litigation incidental to the conduct of its business. In the opinion of the Company's management, none of such litigation as of December 31, 2001 is likely to have a material adverse effect on the financial position, results of operations, or cash flows of the Company.

### 17 RELATED PARTY TRANSACTIONS

BDCI has entered into certain agreements with companies under common control (affiliated companies). These agreements were developed in the context of parent/subsidiary relationship and, therefore, may not necessarily reflect the result of arm's length negotiations between independent parties. BDCI records sales with affiliates based on a cost-plus formula developed and agreed upon by both parties.

#### CORPORATE AND OTHER COST ALLOCATIONS

As discussed in note 1, the financial statements of BDCI reflect certain allocated support costs incurred by other entities in the Hercules Group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, research and development overhead, investor relations and other corporate services. Allocations and charges included in BDCI's financial statements were based on either a direct cost pass-through for items directly identified as related to BDCI's activities, a percentage allocation for such services provided based on factors such as revenues, net assets, cost of sales or a relative weighting of geographic activity. These allocations are reflected in the selling, general and administrative line item in the consolidated statements of operations. Such allocations and corporate charges totalled \$1,180 thousand in 2001, \$3,067 thousand in 2000 and \$5,738 thousand in 1999.

#### ROYALTIES

BDCI entered into a licence agreement in respect of the use of manufacturing formulations and specifications, which are developed and owned by affiliated companies. BDCI paid royalties in respect of this agreement of \$5,396 thousand in 2001, \$5,998 thousand in 2000 and \$4,937 thousand in 1999. The royalties are reflected in the other operating expense line item in the consolidated statements of operations.

BETZDEARBORN CANADA, INC.

Notes to Consolidated Financial Statements

---

PURCHASES

BDCI purchases products for resale in the normal course of business from affiliated companies. BDCI's purchases from affiliated companies were \$34,936 thousand in 2001, \$52,639 thousand in 2000 and \$12,502 thousand in 1999.

OTHER

BDCI reimburses affiliated companies for charges incurred on its behalf. These costs are reflected in the selling, general and administrative line item in the consolidated statements of operations. The amount paid was \$274 thousand in 2001, \$874 thousand in 2000 and \$58 thousand in 1999. BDCI receives commissions for sales made on behalf of affiliated companies, which are reflected as a decrease to selling, general and administrative costs in the consolidated statements of operations and comprehensive (loss) income. Total commissions earned from affiliates amounted to \$12 thousand in 2001, \$422 thousand in 2000 and \$291 thousand in 1999.

18 SUBSEQUENT EVENT

On April 29, 2002, Hercules completed the sale of its Water Treatment Business to GE Specialty Materials. Pursuant to the Stock and Asset Agreement for the transaction, the sale included all of the stock of BetzDearborn and the Company. Hercules used the proceeds from the sale to prepay borrowings under its Senior Credit Facility (including the \$65,427 thousand outstanding under the US\$100 million Canadian Revolver) and ESOP Credit Facility. Pursuant to the prepayment, among other things, the stock pledges were released and the Canadian Revolver was cancelled.

REPORT OF INDEPENDENT ACCOUNTANTS

TO THE SHAREHOLDERS AND THE BOARD OF DIRECTORS OF  
HERCULES INCORPORATED  
WILMINGTON, DELAWARE

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations and comprehensive loss and of cash flows present fairly, in all material respects, the financial position of BetzDearborn Europe, Inc., a subsidiary of Hercules Incorporated, and its subsidiaries at December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the

## Edgar Filing: HERCULES INC - Form 10-K/A

United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP  
Philadelphia, Pennsylvania  
November 12, 2002

56

### BETZDEARBORN EUROPE, INC. CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS

	(Dollars in thousands)		
	Year Ended December 31,		
	2001	2000	1999
	----	----	----
Sales to third parties	\$ 136,912	\$ 160,386	\$ 176,145
Sales to Hercules Group	53,634	60,782	64,952
	-----	-----	-----
	190,546	221,168	241,097
Cost of sales	113,768	134,438	142,608
Selling, general, and administrative expenses	50,590	55,405	63,242
Research and development	2,203	2,782	3,931
Goodwill and intangible asset amortization	5,466	6,126	6,696
Other operating expenses, net (Note 13)	23,163	12,432	13,814
	-----	-----	-----
(Loss) profit from operations	(4,644)	9,985	10,806
Interest and debt expense (Note 14)	6,903	9,438	9,277
Other income (expense), net (Note 15)	1,779	998	1,666
	-----	-----	-----
(Loss) income before income taxes and equity income	(9,768)	1,545	3,195
Provision for income taxes (Note 16)	1,885	2,300	6,609
	-----	-----	-----
Loss before equity income	(11,653)	(755)	(3,414)
Equity income of affiliated companies	3,245	3,716	3,104
	-----	-----	-----
Net (loss) income	(8,408)	2,961	(310)
Additional minimum pension liability, net of tax of \$(6,327)	(14,762)	--	--
Foreign currency translation, net of tax of \$0 for each year	(4,481)	(28,564)	(11,658)
	-----	-----	-----
Comprehensive loss	\$ (27,651)	\$ (25,603)	\$ (11,968)
	=====	=====	=====

The accompanying notes are an integral part of the consolidated financial

Edgar Filing: HERCULES INC - Form 10-K/A

statements.

57

BETZDEARBORN EUROPE INC.  
CONSOLIDATED BALANCE SHEETS

	(Dollars in thousands)	
	December 31,	
	2001	2000
	----	----
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 1,837	\$ 2,400
Accounts receivable, net (Note 3)	36,213	44,477
Inventories (Note 4)	12,458	16,222
Deferred income taxes (Note 16)	1,085	1,711
	-----	-----
Total current assets	51,593	64,820
	-----	-----
Property, plant, and equipment, net (Note 9)	47,529	53,380
Investments in affiliates (Note 5)	135,139	152,460
Goodwill and other intangible assets, net (Note 10)	165,248	182,920
Deferred income taxes (Note 16)	2,950	-
Prepaid pension (Note 12)	9,935	7,780
Deferred charges and other assets	3,134	1,280
	-----	-----
Total assets	\$ 415,528	\$ 462,670
	=====	=====
<b>LIABILITIES AND NET HERCULES GROUP INVESTMENT</b>		
Current liabilities		
Accounts payable	\$ 17,214	\$ 17,510
Short-term debt (Note 6)	--	5,730
Accrued expenses (Note 9)	20,245	21,470
	-----	-----
Total current liabilities	37,459	44,710
Deferred income taxes (Note 16)	--	5,410
Pension liability (Note 12)	22,139	-
Deferred credits and other liabilities	--	300
	-----	-----
Total liabilities	59,598	50,150
Commitments and contingencies (Note 17)		
Net Hercules Group investment (Note 20)		
Accumulated other comprehensive losses	(73,311)	(54,060)
Intercompany transactions	429,241	466,580
	-----	-----
Net Hercules Group investment	355,930	412,510
	-----	-----
Total liabilities and net Hercules Group investment	\$ 415,528	\$ 462,670
	=====	=====

The accompanying notes are an integral part of the consolidated financial statements.

Edgar Filing: HERCULES INC - Form 10-K/A

58

BETZDEARBORN EUROPE INC.  
CONSOLIDATED STATEMENT OF CASH FLOWS

	(Dollars in thousands)	
	Year Ended December 31	
	2001	2000
	----	----
CASH FLOW FROM OPERATING ACTIVITIES:		
Net income (loss)	\$ (8,408)	\$ 2,961
Adjustments to reconcile net income (loss) to net cash provided by operations:		
Depreciation and amortization of property, plant and equipment	5,825	7,037
Amortization of goodwill and other intangible assets	5,466	6,126
Restructuring plans	4,153	1,539
Deferred income tax	(1,926)	(372)
Loss on disposals of property, plant and equipment	996	84
Loss on sale of investment	7,194	--
Equity income of affiliates	(3,245)	(3,716)
Dividends from equity method investments	19,932	--
Corporate and other cost allocations	4,806	3,940
Accruals and deferrals of cash receipts and payments:		
Accounts receivable	7,670	(1,215)
Inventories	2,977	4,638
Accounts payable and accrued expenses	(3,251)	(955)
Noncurrent assets and liabilities	(2,988)	(2,850)
Net transfers (to) from Hercules Group	(242)	38,809
	-----	-----
Net cash provided by operations	38,959	56,026
	-----	-----
CASH FLOW FROM INVESTING ACTIVITIES:		
Capital expenditures, net of proceeds from sale	(2,541)	(3,123)
	-----	-----
Net cash (used in) provided by investing activities	(2,541)	(3,123)
	-----	-----
CASH FLOW FROM FINANCING ACTIVITIES:		
Change in short-term debt	(5,743)	(4,341)
Net transfers (to) from Hercules Group	(30,937)	(49,096)
	-----	-----
Net cash provided by (used in) financing activities	(36,680)	(53,437)
	-----	-----
Effect of exchange rate changes on cash	(307)	(173)
	-----	-----
Net decrease in cash and cash equivalents	(569)	(707)
Cash and cash equivalents at beginning of year	2,406	3,113
	-----	-----
Cash and cash equivalents at end of year	\$ 1,837	\$ 2,406
	=====	=====
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the year for:		
Interest (net of amount capitalized)	\$ 6,242	\$ 9,439
Income taxes, net	4,733	4,622

## Edgar Filing: HERCULES INC - Form 10-K/A

Noncash investing and financing activities:		
Corporate and other cost allocations	4,806	3,940
Corporate and other asset allocations	--	4,609

The accompanying notes are an integral part of the consolidated financial statements.

59

BETZDEARBORN EUROPE INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

### 1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

BetzDearborn Europe Inc. (the "Company") is a wholly owned subsidiary of BetzDearborn Inc. (immediate parent) ("BetzDearborn") and Hercules Incorporated (ultimate parent) ("Hercules"). Hercules and its wholly owned subsidiaries comprise the Hercules Group. The Company supplies engineered chemical treatment programs for water and process systems in industrial, commercial and institutional establishments, offering a range of products and services for preserving or enhancing productivity, reliability and efficiency in plant operations and in complying with environmental regulations.

When Hercules acquired all of the outstanding shares of BetzDearborn Inc on October 15, 1998 it paid \$2,235 million in cash and \$186 million in common stock exchanged for the shares held by the BetzDearborn ESOP Trust. The purchase price allocated to the Company and its subsidiaries was approximately \$810 million. During 1999, Hercules completed the purchase price allocation and the final determination of goodwill was \$2,170 million of which the amount attributable to the Company was approximately \$204 million. These financial statements include the push down of fair value adjustments to assets and liabilities, including goodwill, other intangible assets and property, plant and equipment and their related amortization and depreciation adjustments.

As a result of this acquisition, the Company, as a part of an effort by Hercules, entered into several internal reorganization transactions during 2000 and 1999. The transactions included the Company selling several of its investments in subsidiaries to Hercules affiliates, purchasing several investments in subsidiaries from Hercules affiliates, merging companies, and acquiring certain investments in Hercules group companies that are valued at cost. As all investments in this reorganization are under the common control of Hercules, these transactions have been accounted for in a manner similar to pooling of interests

Prior to the fiscal 2000 year, separate company stand-alone financial statements were not prepared for the Company. In November 2000, Hercules amended its senior credit facility and ESOP credit facility (the "Facilities"). The Facilities, as amended, are secured by liens on Hercules' property and assets (and those of Hercules' Canadian Subsidiaries), a pledge of the stock of substantially all of Hercules' domestic subsidiaries (including the Company) and 65% of the stock of foreign subsidiaries directly owned by Hercules, and a pledge of Hercules' domestic intercompany indebtedness. These consolidated financial statements present the financial information of the Company, a collateral party to the Hercules debt, based on the Hercules' understanding of the Securities and Exchange Commission's interpretation and application of Rule 3-16 under the Securities and Exchange Commission's Regulation S-X. These statements were derived from historical accounting records.

## Edgar Filing: HERCULES INC - Form 10-K/A

On April 29, 2002, in connection with Hercules' sale of its Water Treatment Business (see Note 21) and the repayment of the Facilities, the stock pledges were released. As a result, based on Hercules' current debt structure, these separate company stand-alone financial statements will not be required for the fiscal year ending December 31, 2002.

The consolidated financial statements of the Company reflect certain allocated support costs incurred by the Hercules Group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations and charges included in the Company's consolidated financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on factors such as sales, net assets, or cost of sales; or a relative weighting of geographic activity. Management believes that the allocation method is reasonable. (See Note 18)

A number of the Company's operating companies participate in Hercules' centralized cash management system. Accordingly, cash received from operations may be transferred to Hercules on a periodic basis, and Hercules funds operational and capital requirements upon request.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its majority-owned subsidiaries where control exists. Following the acquisition of BetzDearborn by Hercules in 1998, the Company continued BetzDearborn's practice of using a November 30 fiscal year end for certain former BetzDearborn non-U.S. subsidiaries to expedite the year end closing process. All intercompany transactions and profits have been eliminated.

60

#### BETZDEARBORN EUROPE INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

#### USE OF ESTIMATES

Preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

#### REVENUE RECOGNITION

The Company recognizes revenue when the earnings process is complete. This generally occurs when products are shipped to the customer or services are performed in accordance with terms of the agreement, title and risk of loss have been transferred, collectibility is probable, and pricing is fixed and determinable. Accruals are made for sales returns and other allowances based on the Company's experience. The corresponding shipping and handling costs are included in cost of sales.

#### RESEARCH AND DEVELOPMENT EXPENDITURES

Research and development expenditures are expensed as incurred.

## Edgar Filing: HERCULES INC - Form 10-K/A

### ENVIRONMENTAL EXPENDITURES

Environmental expenditures that pertain to current operations or future revenues are expensed or capitalized according to the Company's capitalization policy. Expenditures for remediation of an existing condition caused by past operations that do not contribute to current or future revenues are expensed. Liabilities are recognized for remedial activities when the cleanup is probable and can be reasonably estimated.

### CASH AND CASH EQUIVALENTS

Cash in excess of operating requirements is invested in short-term, income producing instruments. Cash equivalents include commercial paper and other securities with original maturities of 90 days or less. Book value approximates fair value because of the short-term maturity of those instruments.

### INVENTORIES

Inventories are stated at the lower of cost or market. Inventories are valued on the average cost method.

### PROPERTY AND DEPRECIATION

Property, plant, and equipment are stated at cost. The Company changed to the straight-line method of depreciation, effective January 1, 1991, for newly acquired processing facilities and equipment. Assets acquired before then continue to be depreciated by accelerated methods. The Company believes straight-line depreciation provides a better matching of costs and revenues over the lives of the assets. The estimated useful lives of depreciable assets are as follows: buildings - 30 years; plant, machinery and equipment - 15 years; other machinery and equipment - 3 to 15 years.

Maintenance, repairs, and minor renewals are charged to income; major renewals and betterments are capitalized. Upon normal retirement or replacement, the net book value of property (less proceeds of sale or salvage) is charged to income.

### INVESTMENTS

Investments in affiliated companies with a 20% or greater ownership interest in which the Company has significant influence are accounted for using the equity method of accounting. Accordingly, these investments are included in investments in affiliates on the Company's balance sheet and the income or loss from these investments is included in equity in (loss) income of affiliated companies in the Company's statement of income.

Investments in affiliated companies in which the Company does not have a controlling interest, or an ownership and voting interest so large as to exert significant influence, are accounted for using the cost method of accounting. Accordingly, these investments are included in investments in affiliates on the Company's balance sheet.

### GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill and other intangible assets are amortized on a straight-line basis over the estimated future periods to be benefited, generally 40 years for goodwill and 5 to 15 years for other intangible assets. Pursuant to Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (SFAS 142), beginning January 1,



BETZDEARBORN EUROPE INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

2002, goodwill will not be amortized but will be tested for impairment annually and any necessary adjustment charged to expense. Intangible assets with finite lives will be amortized over their useful lives.

LONG-LIVED ASSETS

The Company reviews its long-lived assets, including goodwill and other intangibles, for impairment on an exception basis whenever events or changes in circumstances indicate carrying amounts of the assets may not be recoverable through undiscounted future cash flows. If an impairment loss has occurred based on expected future cash flows (undiscounted), the loss is recognized in the income statement. The amount of the impairment loss is the excess of the carrying amount of the impaired asset over the fair value of the asset. The fair value represents expected future cash flows from the use of the assets, discounted at the rate used to evaluate potential investments.

COMPUTER SOFTWARE COSTS

Effective January 1, 1999, the Company adopted the American Institute of Certified Public Accountants Statement of Position 98-1, "Accounting for the Cost of Computer Software Developed or Obtained for Internal Use" (SOP 98-1). The prior accounting was generally consistent with the requirements of SOP 98-1 and, accordingly, adoption of SOP 98-1 had no material effect. Computer software costs are being amortized over a period of 5 to 10 years.

INCOME TAXES

Income tax expense in the accompanying consolidated financial statements has been computed assuming the Company filed separate income tax returns.

The provisions for income taxes have been determined using the asset and liability approach of accounting for income taxes. Under this approach, deferred taxes represent the future tax consequences expected to occur when the reported amounts of assets and liabilities are recovered or paid. The provision for income taxes represents income taxes paid or payable for the current year plus the change in deferred taxes during the year. Deferred taxes result from differences between the financial and tax basis of the Company's assets and liabilities and are adjusted for changes in tax rates and tax laws when changes are enacted. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized.

The company provides taxes on undistributed earnings of subsidiaries and affiliates included in consolidated retained earnings to the extent such earnings are planned to be remitted and not re-invested permanently. The undistributed (losses)/earnings of subsidiaries and affiliates on which no provision for foreign withholding or US income taxes has been made amounted to approximately \$(10,058 thousand), \$5,380 thousand and \$1,853 thousand at December 31, 2001, 2000 and 1999, respectively. US and foreign income taxes that would be payable if such earnings were distributed may be lower than the amount computed at the US statutory rate because of the availability of tax credits.

FOREIGN CURRENCY TRANSLATION AND TRANSACTIONS

The accompanying consolidated financial statements are reported in U.S. dollars. The U.S. dollar is the functional currency for the Company. The translation of the functional currencies of the Company's subsidiaries into U.S.

## Edgar Filing: HERCULES INC - Form 10-K/A

dollars (reporting currency) is performed for assets and liabilities using the current exchange rates in effect at the balance sheet date, and for revenues, costs and expenses using average exchange rates prevailing during the reporting periods. Adjustments resulting from the translation of functional currency financial statements to reporting currency are accumulated and reported as other comprehensive income (loss), a separate component of net Hercules Group investment.

Transactions in foreign currency are recorded at the exchange rate prevailing on the date of transaction. Monetary assets and liabilities denominated in foreign currencies are expressed in the functional currency at the exchange rates in effect at the balance sheet date. Revenues, costs and expenses are recorded using average exchange rates prevailing during the reporting periods. Gains or losses resulting from foreign currency transactions are included in the statement of income.

### CONCENTRATIONS OF CREDIT RISK

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of trade receivables and receivables from affiliated companies, which are included in the net Hercules Group investment in the consolidated balance sheet. Concentrations of credit risk with respect to trade receivables are limited due to the Company's large number of customers and their dispersion across many different industries and locations.

62

BETZDEARBORN EUROPE INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

### DERIVATIVE INSTRUMENTS AND HEDGING

On January 1, 2001, the Company adopted Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"). SFAS 133, as amended by Statement No. 137, "Accounting for Derivative Instruments and Hedging Activities-Deferral of the Effective Date of FASB Statement No. 133" and Statement No. 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities," requires that all derivative instruments be recorded on the balance sheet at their fair value. The Company has not designated any derivative as a hedge instrument and accordingly, changes in fair value of derivatives are recorded each period in earnings. The adoption of SFAS 133 did not result in a pre-tax or post-tax cumulative-effect-type adjustment to income and did not result in a change to other comprehensive income (loss).

Derivative financial instruments have been used to hedge risk caused by fluctuating currency. The Company enters into forward-exchange contracts to hedge foreign currency exposure. Decisions regarding hedging are made on a case-by-case basis, taking into consideration the amount and duration of the exposure, market volatility, and economic trends. The Company uses the fair-value method of accounting, recording to other income (expense), net realized and unrealized gains and losses on these contracts monthly, except for gains and losses on contracts to hedge specific foreign currency commitments, which are deferred and accounted for as part of the transaction. Gains or losses on instruments which have been used to hedge the value of investments in certain non-U.S. subsidiaries have been accounted for under the deferral method and are included in the foreign currency translation adjustment. It is the Company's policy to match the term of financial instruments with the term of the underlying designated item. If the designated item is an anticipated transaction

## Edgar Filing: HERCULES INC - Form 10-K/A

no longer likely to occur, gains or losses from the instrument designated as a hedge are recognized in current period earnings. The Company does not hold or issue financial instruments for trading purposes. In the consolidated statement of cash flow, the Company reports the cash flows resulting from its hedging activities in the same category as the related item that is being hedged.

### STOCK-BASED COMPENSATION

Compensation costs attributable to stock option and similar plans are recognized based on any excess of the quoted market price of the stock on the date of grant over the amount the employee is required to pay to acquire the stock (the intrinsic-value method under Accounting Principles Board Opinion 25 (APB 25)). Such amount, if any, is accrued over the related vesting period, as appropriate. Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation," requires companies electing to continue to use the intrinsic-value method to make pro forma disclosures of net income as if the fair-value-based method of accounting had been applied.

### NET HERCULES GROUP INVESTMENT

The Net Hercules Group Investment account reflects the balance of the Company's historical earnings, intercompany amounts, foreign currency translation and other transactions between the Company and the Hercules Group.

### NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 141, "Business Combinations" ("SFAS 141"), and Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"). SFAS 141 supersedes Accounting Principles Board Opinion ("APB") No. 16, Business Combinations. The provisions of SFAS 141 (1) require that the purchase method of accounting be used for all business combinations initiated after June 30, 2001, (2) provide specific criteria for the initial recognition and measurement of intangible assets apart from goodwill and (3) require that unamortized negative goodwill be written off immediately as extraordinary gain instead of being deferred and amortized. SFAS 141 also requires that upon adoption of SFAS 142 the Company reclassify the carrying amounts of certain intangible assets into or out of goodwill, based on certain criteria. SFAS 142 supersedes APB No. 17, Intangible Assets, and is effective for fiscal years beginning after December 15, 2001. SFAS 142 primarily addresses the accounting for goodwill and intangible assets subsequent to their initial recognition. The provisions of SFAS 142 (1) prohibit the amortization of goodwill and indefinite-lived intangible assets, (2) require that goodwill and indefinite-lived intangible assets be tested annually for impairment (and in interim periods if certain events occur indicating that the carrying value of goodwill and/or indefinite-lived intangible assets may be impaired), based on fair value (as opposed to cost recovery using future undiscounted cash flows), (3) require that reporting units be identified for the purpose of assessing potential future impairments of goodwill and (4) remove the forty-year limitation on the amortization period of intangible assets that have finite lives.

Effective January 1, 2002 Hercules adopted the provisions of SFAS 142. Hercules identified the following reporting units: BetzDearborn and Pulp and Paper, Aqualon and FiberVisions. In connection with Hercules' transitional

## Edgar Filing: HERCULES INC - Form 10-K/A

review, recorded goodwill was determined to be impaired in the BetzDearborn reporting unit. In the first quarter 2002, Hercules completed its transitional impairment review of the identified reporting units and recognized an after tax impairment loss of \$368 million as a cumulative effect of a change in accounting principle, of which \$263 million related to the BetzDearborn Inc. water business. As a result of Hercules' adoption of SFAS 142, the Company will no longer record approximately \$5.4 million of annual amortization relating to existing goodwill and intangibles.

Goodwill related to the BetzDearborn business was evaluated for impairment at December 31, 2001 under Statement of Financial Accounting Standards No. 121 "Accounting for the Impairment of Long-Fixed Assets and for Long-Lived Assets to Be Disposed of". Such evaluation indicated that goodwill associated with the business was recoverable from anticipated future undiscounted cash flows. Accordingly, no impairment loss was recorded in the December 31, 2001 financial statements.

In June 2001, the Financial Accounting Standards Board ("FASB") approved the issuance of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143"). SFAS 143 establishes accounting standards for the recognition and measurement of legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 will become effective for the Company on January 1, 2003 and requires recognition of a liability for an asset retirement obligation in the period in which it is incurred. The Company does not believe it will have a material effect on its financial statements.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company does not believe it will have a material effect on its financial statements.

In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment to FASB Statement No. 13, and Technical Corrections." The Company elected to early adopt the provisions of SFAS 145 related to the rescission of SFAS 4, "Reporting Gains and Losses from the Extinguishment of Debt" ("SFAS 4"). The early adoption of SFAS 145 had no effect on the Company's financial statements.

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146"). SFAS 146 addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs in a Restructuring)". SFAS 146 defines the timing of the recognition of costs associated with exit or disposal activities, the types of costs that may be recognized and the methodology for calculating the fair value of such costs. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. The Company does not believe this statement will have a material effect on its financial statements.

### RECLASSIFICATIONS

Certain amounts in the 2000 and 1999 consolidated financial statements and notes have been reclassified to conform to the 2001 presentation.

### 3. ACCOUNTS RECEIVABLE, NET

Accounts receivable, net, consists of:

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousands)	
	2001	2000
	----	----
Trade	\$ 35,925	\$ 39,830
Other	3,059	7,413
	-----	-----
	38,984	47,243
Less allowance for doubtful accounts	(2,771)	(2,767)
	-----	-----
Total	\$ 36,213	\$ 44,476
	-----	-----

Other accounts receivable mainly comprise VAT receivable.

64

BETZDEARBORN EUROPE INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

4. INVENTORIES

The components of inventories are:

	(Dollars in thousands)	
	2001	2000
	----	----
Finished products	\$ 7,510	\$ 9,876
Materials, supplies, and work in process	4,948	6,348
	-----	-----
Total	\$12,458	\$16,224
	-----	-----

5. INVESTMENTS

The Company has various equity investments in companies, as described below. Summarized financial information for these equity affiliates at December 31, and for the years then ended is as follows:

	(Dollars in thousands)	
	2001	2000
	----	----
Current assets	\$ 24,137	\$ 26,497
Non-current assets	164,103	210,711
	-----	-----
Current liabilities	\$ 36,895	\$ 23,481
Non-current liabilities	864	25,113

## Edgar Filing: HERCULES INC - Form 10-K/A

	2001 ----	2000 ----	1999 ----
Net sales	\$ 65,250	\$ 62,348	\$62,860
Gross profit	18,829	18,142	17,930
Net earnings	7,447	8,393	6,699

At December 31, 2001, the Company's equity investments consist of a 38.97% ownership of Hercules Quimica S.A., a Hercules affiliate, a 50% ownership of BL Technologies, a Hercules affiliate and a 19.75% ownership of Hercules de Colombia S.A., a Hercules affiliate. The Company's carrying value for these investments at December 31, 2001 and 2000 equals its share of the underlying equity in net assets of the respective affiliates. Dividends paid to the Company from its equity investees were \$19,932 thousand during 2001 and \$1,666 thousand during 1999. No dividends were received by the Company from equity investees in 2000. Each of these entities operates in lines of business similar to the Company, supplying engineered chemical treatment programs for water and process systems in industrial, commercial and institutional establishments. The Company's cost investment consists of a 7.5% ownership of Hercules International Limited, a Hercules affiliate.

### 6. SHORT-TERM DEBT AND OTHER FINANCING ARRANGEMENTS

Short-term debt of \$5,730 thousand at December 31, 2000, consists of bank borrowings primarily representing foreign overdraft facilities and short-term lines of credit, which are generally payable on demand with interest at various rates. Book values of bank borrowings approximate market value because of their short maturity period. There was no short-term debt outstanding at December 31, 2001.

Short-term debt with affiliates of \$55,784 thousand and \$26,856 thousand at December 31, 2001 and 2000, respectively, is recorded in Net Hercules Group Investment in the consolidated balance sheet and is generally payable on demand with interest at various rates.

At December 31, 2001 and 2000, the Company had \$1,413 thousand and \$28,300 thousand, respectively, of unused lines of credit that may be drawn as needed, with interest at a negotiated spread over lenders' cost of funds.

Weighted-average interest rates on all third party and affiliate short-term borrowings at December 31, 2001 and 2000 were 5.3% and 6.3%, respectively.

65

BETZDEARBORN EUROPE INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

### 7. LONG-TERM DEBT AND OTHER FINANCING ARRANGEMENTS

Long-term debt with affiliates at December 31, 2001 and 2000, which is recorded in Net Hercules Group Investment in the consolidated balance sheet, is summarized as follows:

(Dollars in thousand)  
2001                      2000

Edgar Filing: HERCULES INC - Form 10-K/A

	----	----
7.11% variable rate affiliate note	\$ --	\$ 45,195
4.42% variable rate affiliate note	24,162	27,063
LIBOR variable rate affiliate note	27,836	26,278
7.56% variable rate affiliate note	--	5,022
7.15% variable rate affiliate note	2,165	2,196
4.10% variable rate affiliate note	1,685	1,766
	-----	-----
Less current maturities	--	--
	-----	-----
Total	\$55,848	\$107,520
	=====	=====

All of the long-term debt with the Hercules Group has maturity dates after 2005. The fair values of the Company's long-term debt was \$55,848 thousand at December 31, 2001 and \$107,520 thousand at December 31, 2000. The Company believes that the carrying value of long-term debt borrowings approximates fair value, based on discounting future cash flows using rates currently available for debt of similar terms and remaining maturities.

8. LONG-TERM INCENTIVE COMPENSATION PLANS

The Company participates in long-term incentive compensation plans sponsored by Hercules. These plans provide for the grant of stock options and the award of common stock and other market-based units to certain key employees and non-employee directors.

In 1995, Hercules changed the structure of the long-term incentive compensation plans to place a greater emphasis on shareholder value creation through grants of regular stock options, performance-accelerated stock options, and Cash Value Awards (performance-based awards denominated in cash and payable in shares of common or restricted stock, subject to the same restrictions as restricted stock). Restricted stock and other market-based units are awarded with respect to certain programs. The number of awarded shares outstanding was 189,704 at December 31, 2001, and 491,488 and 926,689 at December 31, 2000 and 1999, respectively.

At December 31, 2001, under Hercules' incentive compensation plans, 1,265,493 shares of common stock were available for grant as stock awards or stock option awards. Stock awards are limited to approximately 15% of the total authorizations. Regular stock options are granted at the market price on the date of grant and are exercisable at various periods from one to five years after date of grant. Performance-accelerated stock options are also granted at the market price on the date of grant and are normally exercisable at nine and one-half years. Exercisability may be accelerated based upon the achievement of predetermined performance goals. Both regular and performance-accelerated stock options expire 10 years after the date of grant.

Restricted shares, options and performance-accelerated stock options are forfeited and revert to Hercules in the event of employment termination, except in the case of death, disability, retirement, or other specified events.

The Company applies APB Opinion 25 in accounting for its plans. Accordingly, no compensation cost has been recognized for the stock option plans. There were no charges to income for the cost of stock awards over the restriction or performance period for 2001, 2000 and 1999, respectively.

Edgar Filing: HERCULES INC - Form 10-K/A

BETZDEARBORN EUROPE INC.  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Below is a summary of outstanding stock option grants under the incentive compensation plans during 1999, 2000 and 2001:

	Regular		Performance-Accelerat	
	Number of Shares	Weighted-average price	Number of Shares	Weighted- pri
	-----	-----	-----	-----
December 31, 1998	17,750	\$ 40.27	--	
Granted	25,250	\$ 37.73	1,350	\$ 37
Exercised	--	--	--	
Forfeited	--	--	--	
	-----	-----	-----	-----
December 31, 1999	43,000	\$ 38.78	1,350	\$ 37
Granted	3,850	\$ 17.25	--	
Exercised	--	--	--	
Forfeited	--	--	--	
	-----	-----	-----	-----
December 31, 2000	46,850	\$ 37.01	1,350	\$ 37
Granted	3,850	\$ 11.28	--	
Exercised	--	--	--	
Forfeited	(3,800)	\$ 37.80	--	
	-----	-----	-----	-----
December 31, 2001	46,900	\$ 34.83	1,350	\$ 37

The weighted-average fair value of regular stock options granted during 1999, 2000 and 2001 was \$8.26, \$8.85 and \$5.69, respectively. The weighted-average fair value of performance-accelerated stock options granted during 1999, 2000 and 2001 was \$8.01, \$0 and \$0, respectively.

Following is a summary of regular stock options exercisable at December 31, 1999, 2000 and 2001, and their respective weighted-average share prices:

Options Exercisable	Number of Shares	Weighted-average exercise price
-----	-----	-----
December 31, 1999	13,540	\$39.91
December 31, 2000	27,520	\$39.25
December 31, 2001	36,430	\$38.10

There were no performance-accelerated stock options exercisable at December 31, 1999, 2000 and 2001.

Following is a summary of stock options outstanding at December 31, 2001:

Outstanding Options

-----  
 Weighted-



Edgar Filing: HERCULES INC - Form 10-K/A

Exercise Price Range	Number Outstanding at 12/31/2001	Weighted-average Remaining Contractual Life	average exercise price
Regular Stock Options			
\$11 - \$20	7,700	8.89	\$14.27
\$30 - \$40	37,550	6.59	\$38.48
\$40 - \$50	1,650	6.35	\$47.81
	-----		
	46,900		
	-----		
Performance-Accelerated Stock Options			
\$14 - \$40	1,350	7.34	\$37.56
	-----		
	1,350		
	-----		

The Company currently expects that 100% of performance-accelerated stock options will eventually vest.

The Company's employees may also participate in the Hercules Employee Stock Purchase Plan ("ESSP"). The ESSP is a qualified non-compensatory plan, which allows eligible employees to acquire shares of common stock through systematic payroll deductions. The plan consists of three-month subscription periods, beginning July 1 of each year. The purchase price is 85% of the fair market value of the common stock on either the first or last day of that subscription period, whichever is lower. Purchases may range from 2% to 15% of an employee's base salary each pay period, subject to certain limitations. Currently, there are no shares of Hercules common stock registered for offer and sale under the plan. Shares issued at December 31, 2001 and 2000, were 1,758,081 and 1,597,861, respectively. The Company applies APB Opinion 25 and related interpretations in accounting for its Employee Stock Purchase Plan. Accordingly, no compensation cost has been recognized for the Employee Stock Purchase Plan.

67

BETZDEARBORN EUROPE INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Had compensation cost for Hercules' Stock-Based Incentive Plans and Employee Stock Purchase Plan been determined on the basis of fair value according to SFAS No. 123, the fair value of each option granted or share purchased would be estimated on the grant date using the Black-Scholes option pricing model.

The following weighted-average assumptions would be used in estimating fair value for 2001, 2000 and 1999:

Assumption	Regular Plan	Performance Accelerated Plan	Employee Stock Purchase Plan
Dividend yield	0.96%	3.83%	0.0%
Risk-free interest rate	5.80%	5.57%	4.86%
Expected life	7.1 yrs.	5 yrs.	3 mos.
Expected volatility	33.36%	29.78%	49.11%

## Edgar Filing: HERCULES INC - Form 10-K/A

The Company's net income and earnings per share for 2001, 2000 and 1999 would approximate the pro forma amounts below:

	(Dollars in thousands)		
	2001	2000	1999
	----	----	----
Net (loss) income			
As reported	\$ (8,408)	\$ 2,961	\$ (310)
Pro forma	\$ (8,464)	\$ 2,885	\$ (370)

### 9. ADDITIONAL BALANCE SHEET DETAIL

	(Dollars in thousands)	
	2001	2000
	----	----
Property, plant, and equipment		
Land	\$ 4,295	\$ 5,221
Buildings and equipment	74,756	77,036
	-----	-----
Total	79,051	82,257
Accumulated depreciation and amortization	(31,522)	(28,875)
	-----	-----
Net property, plant, and equipment	\$ 47,529	\$ 53,382
	=====	=====
Accrued expenses		
Payroll and employee benefits	\$ 2,249	\$ 1,432
Income taxes payable	6,907	6,386
Restructuring (Note 11)	2,349	2,989
Other	8,740	10,670
	-----	-----
	\$ 20,245	\$ 21,477
	=====	=====

### 10. GOODWILL AND OTHER INTANGIBLE ASSETS

At December 31, 2001 and 2000, the goodwill and other intangible assets were:

	(Dollars in thousands)	
	2001	2000
	----	----
Goodwill	\$178,017	\$191,224
Other intangibles	7,175	6,882
	-----	-----
Total	185,192	198,106
Less accumulated amortization	(19,944)	(15,179)
	-----	-----
Net goodwill and other intangible assets	\$165,248	\$182,927

Goodwill and other intangible assets primarily represent amounts capitalized from the Hercules acquisition of BetzDearborn (Note 1).

68

BETZDEARBORN EUROPE INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

#### 11. RESTRUCTURING

The consolidated balance sheet reflects liabilities for employee severance benefits and other exit costs, primarily related to the plans initiated upon the creation of the European Shared Service Center in 1997, the acquisition of BetzDearborn in 1998 and the Work Process Redesign ("WPR") program in 2001. During the third quarter of 2001, Hercules started a Work Process Redesign program. The WPR program has been set up to analyze and change the way we work to improve the mechanics of how we do business - to do it better, quicker and at less costs. Teams were established to focus initially on seven work processes of our business that needed major improvement: manufacturing, solicit order to cash, finance and control fundamentals, logistics, information technology, purchase to pay and discovery to commercialization.

Pursuant to the plans in place to merge the operations of BetzDearborn with Hercules and to rationalize the support infrastructure and other existing operations, facilities were closed and approximately 14 employees were terminated during the year 2000. Cash payments for the year included approximately \$2.5 million for severance benefits and other exit costs. The estimate for the remaining plans was decreased by \$444 thousand against goodwill due to lower than planned severance benefits as the result of higher than anticipated attrition, with voluntary resignations not requiring the payment of termination benefits. The estimate for the plans related to the shared services center were decreased by \$626 thousand against operating expense.

As a result of the WPR program, we estimate approximately 64 employees to leave and have charged \$5.3 million to operating expense for these costs. These employees come from various parts of the business, including but not limited to all above-mentioned processes.

During the year 2001, approximately 79 employees were terminated and cash worth approximately \$3.4 million was paid for severance benefits and other exit costs. The estimate for the remaining plans was decreased by approximately \$1.4 million against goodwill due to lower than planned severance benefits as the result of higher than anticipated attrition, with voluntary resignations not requiring the payment of termination benefits. The estimate for the plans related to the shared service center was decreased by approximately \$1.1 million against operating expense.

Severance benefits payments are based on years of service and generally continue for 3 months to 24 months subsequent to termination. We expect to substantially complete the remaining actions under the plans in 2002.

A reconciliation of activity with respect to the liabilities established for these plans, which is included in accrued expenses in the consolidated balance sheet, is as follows:

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousands)	
	2001	2000
	----	----
Balance at beginning of year	\$ 2,989	\$ 4,353
Cash payments	(3,410)	(2,459)
Additional termination benefits and exit costs	5,254	2,165
Reversals against goodwill	(1,383)	(444)
Reversals against earnings	(1,101)	(626)
	-----	-----
Balance at end of year	\$ 2,349	\$ 2,989
	=====	=====

69

BETZDEARBORN EUROPE INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

12. PENSIONS

The Company has a number of defined benefit pension plans in Europe, covering substantially all employees. The following chart lists benefit obligations, plan assets, and funded status of the plans.

	(Dollars in thousands)	
	2001	2000
	----	----
CHANGE IN BENEFIT OBLIGATION		
Benefit obligation at January 1	\$ 77,311	\$ 75,968
Service cost	1,571	2,092
Interest cost	4,941	4,189
Amendments	711	12
Employee contributions	710	760
Translation difference	(1,915)	(6,872)
Actuarial loss	11,658	3,154
Benefits paid from plan assets	(2,019)	(1,992)
	-----	-----
Benefit obligation at December 31	\$ 92,968	\$ 77,311
	=====	=====
CHANGE IN PLAN ASSETS		
Fair value of plan assets at January 1	87,229	89,389
Actual return on plan assets	(9,368)	5,143
Employee contributions	710	760
Company contributions	1,932	1,789
Actuarial loss	--	(1,748)
Translation difference	(2,370)	(6,112)
Benefits paid from plan assets	(2,019)	(1,992)
	-----	-----
Fair value of plan assets at December 31	\$ 76,114	\$ 87,229
	=====	=====
Funded status of the plans	(16,854)	9,918
Unrecognized actuarial loss (gain)	25,880	(2,176)
Unrecognized prior service cost	909	217
Plan amendments	--	(174)
	-----	-----

Edgar Filing: HERCULES INC - Form 10-K/A

Prepaid benefit cost	\$ 9,935	\$ 7,785
	=====	=====

AMOUNTS RECOGNIZED IN THE STATEMENT OF  
FINANCIAL POSITION CONSIST OF:

Additional minimum liability	(22,139)	--
Intangible asset	1,050	--
Other comprehensive income	21,089	--
Prepaid benefit cost	9,935	7,785
	-----	-----
	\$ 9,935	\$ 7,785
	=====	=====

ASSUMPTIONS AS OF DECEMBER 31

Weighted-average discount rate	6.50%	6.50%
Expected return on plan assets	7.00%	8.00%
Rate of compensation increase	3.50%	3.75%

70

BETZDEARBORN EUROPE INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

COMPONENTS OF NET PERIOD PENSION COST

(Dollars in thousands)

	Pension Benefits		
	2001	2000	1999
	----	----	----
Service cost	\$ 1,571	\$ 2,092	\$ 2,313
Interest cost	4,941	4,189	4,326
Expected return on plan assets	(6,825)	(6,291)	(5,912)
Amortization and deferrals	19	(384)	269
Amortization of transition asset	--	(160)	(185)
	-----	-----	-----
Benefit (credit) cost	\$ (294)	\$ (554)	\$ 811
	=====	=====	=====

During 1999 and up to March 1, 2000, the Company's Belgian employees participated in a multi-employer pension fund, which was administered by an affiliated company. Contribution amounts for this fund were \$63 thousand and \$427 thousand in 2000 and 1999, respectively and were allocated to the Company by the Plan administrator.

On March 1, 2000, the Company terminated its participation in the multi-employer pension fund and primarily all Belgian employees were transferred into a Company sponsored defined contribution plan on that date. The Company's cost of the defined contribution plan for the year ended December 31, 2001 was \$193 thousand and for the period March 1, 2000 through December 31, 2000 was \$153 thousand.

13. OTHER OPERATING EXPENSES, NET

Other operating expense, net, in 2001 includes \$7,194 thousand in net losses from the sale of the Company's hydrocarbon resins business, select

## Edgar Filing: HERCULES INC - Form 10-K/A

portions of its rosin resins business, and its peroxy chemicals business. Furthermore, other operating expense, net, includes Hercules Group affiliate royalty costs totaling \$10,776 thousand, net restructuring costs totaling \$4,153 thousand, net losses on asset sales totaling \$996 thousand and net foreign currency losses totaling \$44 thousand.

Other operating expenses, net, in 2000 include Hercules Group affiliate royalty costs totaling \$10,993 thousand, restructuring costs totaling \$1,539 thousand, and foreign currency gains totaling \$100 thousand.

Other operating expenses, net, in 1999 include Hercules Group affiliate royalty costs totaling \$11,764 thousand, restructuring costs totaling \$1,660 thousand and foreign currency losses totaling \$390 thousand.

### 14. INTEREST AND DEBT EXPENSE

No interest and debt costs were capitalized during 2001, 2000 or 1999. The costs incurred are presented separately in the consolidated statement of income and are primarily from debt with affiliates.

### 15. OTHER INCOME (EXPENSE), NET

Other income (expense), net, consists of the following:

	(Dollars in thousands)		
	2001	2000	1999
	----	----	----
Interest income, net	1,741	\$ 359	1,629
Miscellaneous income, net	38	639	37
	-----	-----	-----
	\$1,779	\$ 998	\$1,666
	=====	=====	=====

71

BETZDEARBORN EUROPE INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 16. INCOME TAXES

The domestic and foreign components of (loss) income before taxes are presented below:

	(Dollars in thousands)		
	2001	2000	1999
	----	----	----
Domestic	\$ 6,892	\$ (3,779)	\$ (1,816)
Foreign	(16,660)	5,324	5,011
	-----	-----	-----
	\$ (9,768)	\$ 1,545	\$ 3,195
	=====	=====	=====

## Edgar Filing: HERCULES INC - Form 10-K/A

A summary of the components of the tax provision follows:

	(Dollars in thousands)		
	2001	2000	1999
	----	----	----
Current			
Domestic	\$ 2,683	\$ --	\$1,478
Foreign	1,063	2,672	3,262
Deferred			
Domestic	--	(1,357)	--
Foreign	(1,861)	985	1,869
Provision for income taxes	\$ 1,885	\$ 2,300	\$6,609
	=====	=====	=====

Deferred tax (liabilities) assets at December 31 consist of:

	(Dollars in thousands)	
	2001	2000
	----	----
Depreciation	\$ (4,366)	\$ (4,678)
Intangible asset revaluation	(1,053)	(1,357)
Fixed asset revaluation	(884)	(1,181)
Pension	(2,981)	(2,061)
Gross deferred tax liabilities	(9,284)	(9,277)
Loss carryforwards	\$ 5,339	\$ 2,057
Restructuring expenses	211	1,580
Allowance for doubtful accounts	395	344
Pension	6,789	--
Intangible asset	1,385	1,385
Other	466	393
Gross deferred tax assets	14,585	5,759
Valuation allowance	(1,266)	(177)
	\$ 4,035	\$ (3,695)
	=====	=====

72

BETZDEARBORN EUROPE INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

-----  
A reconciliation of the statutory income tax rate to the effective rate follows:

	2001	2000	1999
--	------	------	------

## Edgar Filing: HERCULES INC - Form 10-K/A

	----	----	----
Statutory income tax rate	35.0 %	35.0 %	35.0 %
Goodwill amortization	(46.5)%	135.2 %	93.1 %
Nondeductible expenses	(4.2)%	24.5 %	14.6 %
Tax rate differences on subsidiary earnings	(3.5)%	(18.7)%	(17.9)%
Cash dividends received from equity investments in affiliates	--	--	18.3 %
Change in tax contingency accrual	--	(30.3)%	(4.9)%
Foreign dividends, net of credits	--	--	66.0 %
Other	(0.1)%	3.2 %	2.7 %
	-----	-----	-----
Effective tax rate	(19.3)%	148.9 %	206.9 %
	=====	=====	=====

The net operating losses have carryforward periods ranging from 10 years to indefinite, but may be limited in their use in any given year.

### 17. COMMITMENTS AND CONTINGENCIES

#### Leases

The Company has operating leases (including office space, transportation, and data processing equipment) expiring at various dates. Rental expense was \$3,579 thousand, \$4,267 thousand and \$6,043 thousand in 2001, 2000 and 1999, respectively.

At December 31, 2001, minimum rental payments under noncancelable leases aggregated \$4,398 thousand. The net minimum payments over the next five years are \$1,739 thousand in 2002, \$1,581 thousand in 2003, \$844 thousand in 2004, \$234 thousand in 2005, and \$0 thousand in 2006.

#### Litigation

The Company currently and from time to time is involved in litigation incidental to the conduct of its business. In the opinion of the Company's management, none of such litigation as of December 31, 2001 is likely to have a material adverse effect on the financial position, results of operations, or cash flows of the Company.

#### Environmental

The Company has potential liability in connection with obligations to authorities of various EU countries in which it has manufacturing facilities, and to private parties pursuant to contract, for the cost of environmental investigation and/or cleanup at several sites. Potential costs will depend upon numerous factors, including the actual methods of remediation required or agreed to; outcomes of negotiations with regulatory authorities and private parties; changes in environmental laws and regulations; technological developments; and the years of remedial activity required, which could range from 0 to 30 years.

The Company becomes aware of its obligations relating to sites in which it may have liability for the costs of environmental investigations and/or remedial activities through correspondence from government authorities, or through correspondence from companies with which the Company has contractual obligations, who either request information or notify us of our potential liability. We have established procedures for identifying environmental issues at our plant sites. In addition to environmental audit programs, we have environmental coordinators who are familiar with environmental laws and regulations and act as a resource for identifying environmental issues.



## Edgar Filing: HERCULES INC - Form 10-K/A

Testing performed at the Herentals, Belgium plant indicates that the soil is contaminated around the area of an underground wastewater tank that was removed in 1990. Studies have been performed to evaluate the extent of the contamination and nature of the contaminants. This information is required for the Company to develop a remediation plan satisfactory to governmental authorities. On April 29, 2002, the Company was transferred to and the liability for the environmental remediation was assumed by GE Betz (Note 21).

At this moment no accrual is included in the balance sheet as of December 31, 2001, as a reliable estimate of the remediation costs cannot be made.

73

BETZDEARBORN EUROPE INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

### 18. RELATED PARTY TRANSACTIONS

The Company has entered into certain agreements with affiliated entities. These agreements were developed in the context of a Hercules Group/subsidiary relationship and therefore may not necessarily reflect the result of arm's-length negotiations between independent parties. All transactions described below are eliminated on consolidation of Hercules.

**Intercompany borrowing and interest:** The Company has intercompany loans with Hercules affiliated entities. The loans with affiliates are presented in Net Hercules Group Investment in the consolidated balance sheet. Interest paid to affiliated entities was \$5,717 thousand, \$8,490 thousand and \$8,924 thousand in 2001, 2000 and 1999, respectively.

**Corporate, regional and other allocations:** As discussed in Note 1, the consolidated financial statements of the Company reflect certain allocated support costs incurred by other entities in the Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations and charges included in the Company's consolidated financial statements were based either on a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on factors such as sales, net assets, cost of sales; or a relative weighting of geographic activity. These allocations are reflected in the selling, general and administrative line item in the consolidated statement of income. Such allocations and corporate charges totaled approximately \$15,606 thousand, \$9,494 thousand and \$12,925 thousand in 2001, 2000 and 1999, respectively.

**Sales to affiliates:** The Company sells raw material and finished goods inventory in the normal course of business to affiliated companies. The Company's revenues from sales to affiliated companies are presented separately in the consolidated statement of income.

**Purchases from affiliates:** The Company purchases in the normal course of business raw material and finished goods inventory from affiliated companies. The Company's purchases of inventory from affiliated companies is reflected in costs of sales in the consolidated statement of income and totaled \$23,067 thousand, \$34,688 thousand and \$40,153 thousand in 2001, 2000 and 1999, respectively.

**Royalties:** The Company entered into a license agreement in respect of the

## Edgar Filing: HERCULES INC - Form 10-K/A

use of manufacturing formulations and specifications developed and owned by an affiliated entity. Total royalties accrued in respect of this agreement are included in the other operating expense line item in the consolidated statement of income and totaled \$10,776 thousand, \$10,993 thousand and \$11,764 thousand in 2001, 2000 and 1999, respectively.

### 19. DERIVATIVE INSTRUMENTS AND RISK MANAGEMENT

The Company enters into forward-exchange contracts to hedge currency exposure.

#### NOTIONAL AMOUNTS AND CREDIT EXPOSURE OF DERIVATIVES

The notional amounts of derivatives summarized below do not represent amounts exchanged by the parties and, thus, are not a measure of the exposure of the Company through its use of derivatives. The amounts exchanged are calculated on the basis of the notional amounts and the other terms of the derivatives, which relate to interest rates or exchange rates.

#### FOREIGN EXCHANGE RISK MANAGEMENT

The Company has selectively used foreign currency forward contracts to offset the effects of exchange rate changes on reported earnings, cash flow, and net asset positions. The primary exposures are denominated in the U.S. Dollar and the British Pound Sterling. Some of the contracts involve the exchange of two foreign currencies, according to local needs in foreign subsidiaries. The term of the currency derivatives is rarely more than three months. At December 31, 2001, the Company had outstanding forward-exchange contracts to purchase foreign currencies aggregating \$9,150 thousand, and to sell foreign currencies aggregating \$9,160 thousand. The Company had no material outstanding forward-exchange contracts at December 31, 2000. The foreign exchange contracts outstanding at December 31, 2001 will mature during 2002.

74

BETZDEARBORN EUROPE INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

#### FAIR VALUES

The following table presents the carrying amounts and fair values of the Company's financial instruments at December 31, 2001 and 2000:

	(Dollars in thousands)	
	2001	
	Carrying Amount	Fair Value
	-----	-----
Foreign exchange contracts	\$ (9)	\$ (9)

The carrying amount represents the net unrealized gain or net interest payable associated with the contracts at the end of the period. Fair values of derivative contracts are indicative of cash that would have been required had settlement been December 31, 2001. Foreign exchange contracts are valued based on year-end exchange rates.

## Edgar Filing: HERCULES INC - Form 10-K/A

### 20. NET HERCULES GROUP INVESTMENT

Changes in Net Hercules Group Investment were as follows:

(Dollars in thousands)	
Balance, January 1, 1999	\$ 483,857
Net loss	(310)
Other comprehensive loss	(11,658)
Intercompany transactions, net	(26,944)
	-----
Balance, December 31, 1999	\$ 444,945
Net income	2,961
Other comprehensive loss	(28,564)
Intercompany transactions, net	(6,828)
	-----
Balance, December 31, 2000	412,514
Net loss	(8,408)
Other comprehensive loss	(19,243)
Intercompany transactions, net	(28,933)
	-----
Balance, December 31, 2001	\$ 355,930
	=====

The Company includes accumulated other comprehensive losses in Net Hercules Group Investment. At December 31, 2001, accumulated other comprehensive losses consisted of an additional minimum pension liability and foreign currency translation adjustments, net of tax, of \$(14,762) thousand and \$(58,549) thousand, respectively. At December 31, 2000 and 1999, accumulated other comprehensive losses consisted of foreign currency translation adjustments, net of tax, of \$(54,068) thousand and \$(25,504) thousand, respectively.

### 21. SUBSEQUENT EVENTS

On April 29, 2002, Hercules completed the sale of its Water Treatment Business to GE Specialty Materials (GSM). Pursuant to the Stock and Asset Agreement for the transaction, the sale included all of the stock of BetzDearborn and the Company. Hercules used the proceeds from the sale to prepay borrowings under its Senior Credit Facility and ESOP Credit Facility. Pursuant to the prepayment, among other things, the stock pledges were released.

75

BETZDEARBORN INTERNATIONAL INCORPORATED  
 REPORT OF INDEPENDENT ACCOUNTANTS

-----

REPORT OF INDEPENDENT ACCOUNTANTS

TO THE SHAREHOLDERS AND THE BOARD OF DIRECTORS OF  
 HERCULES INCORPORATED

# Edgar Filing: HERCULES INC - Form 10-K/A

WILMINGTON, DELAWARE

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations and comprehensive loss and of cash flows present fairly, in all material respects, the financial position of BetzDearborn International Inc., a subsidiary of Hercules Incorporated, and its subsidiaries at December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP  
 Philadelphia, Pennsylvania  
 November 21, 2002

76

BETZDEARBORN INTERNATIONAL INCORPORATED  
 CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS

	(Dollars in thousands) Year Ended December 31,	
	2001	2000
	-----	-----
Sales to third parties	\$ 175,907	\$ 183,628
Sales to Hercules Group	2,323	3,097
	-----	-----
	178,230	186,725
Cost of sales	82,297	85,489
Selling, general, and administrative expenses	78,366	79,316
Research and development	136	251
Goodwill amortization	5,068	5,527
Other operating expenses, net (Note 12)	6,425	5,952
	-----	-----
	172,292	176,535
Profit from operations	5,938	10,190
Equity in (income) loss of affiliated companies	(305)	(245)

Edgar Filing: HERCULES INC - Form 10-K/A

Interest expense (Note 6)	4,474	6,252
Other expense, net (Note 13)	26	5,596
	-----	-----
Income (loss) before income taxes and minority interest	1,743	(1,413)
Provision for income taxes (Note 15)	(2,508)	(1,611)
	-----	-----
Net loss before minority interest	(765)	(3,024)
Minority interest	1,638	984
	-----	-----
Net loss	(2,403)	(4,008)
Translation adjustments	(4,568)	(2,061)
	-----	-----
Comprehensive loss	\$ (6,971)	\$ (6,069)
	=====	=====

The accompanying notes are an integral part of the consolidated financial statements.

77

BETZDEARBORN INTERNATIONAL INCORPORATED  
CONSOLIDATED BALANCE SHEETS

	(Dollars in thousands)	
	December 31,	
	2001	2000
	-----	-----
ASSETS		
Current assets		
Cash and cash equivalents	\$ 18,713	\$ 13,622
Accounts receivable, net (Note 3)	37,910	34,755
Inventories (Note 4)	19,293	19,261
Prepaid and other current assets	7,484	9,858
Deferred income taxes (Note 15)	2,995	2,435
	-----	-----
Total current assets	86,395	79,931
	-----	-----
Property, plant, and equipment, net (Note 8)	37,003	41,191
Goodwill, net (Note 9)	187,124	197,496
Investment in affiliates	1,570	1,691
Deferred charges and other assets	5,458	5,783
	-----	-----
Total assets	\$ 317,550	\$ 326,092
	=====	=====
LIABILITIES AND NET HERCULES GROUP INVESTMENT		
Current liabilities		
Accounts payable	\$ 11,390	\$ 11,692
Short-term debt (Note 5)	1,015	14,262

Edgar Filing: HERCULES INC - Form 10-K/A

Accrued expenses (Note 8)	11,471	17,264
Current tax liability (Note 15)	2,300	2,575
	-----	-----
Total current liabilities	26,176	45,793
Long-term debt (Note 6)	2,385	956
Deferred income taxes (Note 15)	1,902	1,175
Deferred credits and other liabilities	2,491	4,278
	-----	-----
Total liabilities	32,954	52,202
Commitments and contingencies (Note 16)	--	--
Minority Interest	13,534	11,489
Net Hercules Group Investment (Note 14)		
Accumulated other comprehensive income	(27,537)	(22,969)
Intercompany balances, net	298,599	285,370
	-----	-----
Net Hercules Group Investment	271,062	262,401
	-----	-----
Total liabilities and Net Hercules Group Investment	\$ 317,550	\$ 326,092
	=====	=====

The accompanying notes are an integral part of the consolidated financial statements.

78

BETZDEARBORN INTERNATIONAL INCORPORATED  
CONSOLIDATED STATEMENTS OF CASH FLOWS

	(Dollars in thousands)	
	2001	2000
	-----	-----
CASH FLOW FROM OPERATING ACTIVITIES:		
Net loss	\$ (2,403)	\$ (2,403)
Adjustments to reconcile net loss to net cash provided by operations:		
Minority interest	1,638	1,638
Depreciation	7,346	7,346
Amortization	5,068	5,068
Provision for bad debts	1,971	1,971
Equity in affiliated companies (income) loss	(305)	(305)
Deferred income taxes	209	209
Corporate and other cost allocations	4,517	4,517
Loss on the disposal of assets	1,788	1,788
Accruals and deferrals of cash receipts and payments:		
Accounts receivable	(5,126)	(5,126)
Inventories	(32)	(32)
Prepaid and other current assets	2,374	2,374
Accounts payable and accrued expenses	(6,095)	(6,095)
Noncurrent assets and liabilities	(1,462)	(1,462)
Transfers (to) from Hercules Group	(10,501)	(10,501)
	-----	-----
Net cash (used in) provided by operations	(1,013)	(1,013)

Edgar Filing: HERCULES INC - Form 10-K/A

CASH FLOW FROM INVESTING ACTIVITIES:		
Capital expenditures	(6,872)	(1
Proceeds from the disposal of property, plant and equipment	1,927	
	-----	-----
Net cash used in investing activities	(4,945)	(
	-----	-----
CASH FLOW FROM FINANCING ACTIVITIES:		
Long-term debt proceeds	1,429	
Long term repayments	--	
Change in short-term debt	(13,247)	
	-----	-----
Transfers from (to) Hercules Group	24,312	(
	-----	-----
Net cash provided by (used in) financing activities	12,494	(
	-----	-----
Effect of exchange rate changes on cash	(1,445)	
	-----	-----
Net increase (decrease) in cash and cash equivalents	5,091	
Cash and cash equivalents at beginning of year	13,622	
	-----	-----
Cash and cash equivalents at end of year	\$ 18,713	\$ 1
	=====	=====
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the year for:		
Interest	\$ 145	\$
Income taxes, net	(2,575)	(
	-----	-----
Noncash financing activities		
Corporate and other cost allocations	4,517	

The accompanying notes are an integral part of the consolidated financial statements.

79

BETZDEARBORN INTERNATIONAL INCORPORATED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

BetzDearborn International Inc. (the "Company"), a subsidiary of Hercules Inc. (Hercules), is engaged in the engineered specialty chemical treatment of water and industrial process systems operating in a wide variety of industrial and commercial applications. The Company develops, produces and markets a broad range of specialty chemical products. The Company also monitors changing water, process and plant operating conditions so as to prescribe the appropriate treatment programs. Operations are conducted primarily in Asia-Pacific, South America and Mexico.

Historically, separate company stand-alone financial statements were not prepared for the Company. In November 2000, Hercules amended its senior credit facility and ESOP credit facility (the "Facilities"). The Facilities, as

## Edgar Filing: HERCULES INC - Form 10-K/A

amended, are secured by liens on Hercules' property and assets (and those of Hercules' Canadian Subsidiaries), a pledge of the stock of substantially all of Hercules' domestic subsidiaries (including the Company) and 65% of the stock of foreign subsidiaries directly owned by Hercules, and a pledge of Hercules' domestic intercompany indebtedness. These financial statements present the financial information on the Company, a collateral party to the Hercules debt, based on the Hercules understanding of Securities and Exchange Commission's interpretation and application of Rule 3-16 under the Securities and Exchange Commission's Regulation S-X. These statements were derived from historical accounting records.

On April 29, 2002, in connection with Hercules' sale of its Water Treatment Business (see Note 18) and the repayment of the Facilities, the stock pledges were released. As a result, based on Hercules' current debt structure, these separate company stand-alone financial statements will not be required for the fiscal year ending December 31, 2002.

As an operating division of Hercules, the Company participates in Hercules' centralized cash management system. Accordingly, cash received from the Company's operations is transferred to Hercules on a periodic basis, and Hercules funds all operational and capital requirements.

The financial statements of the Company reflect certain allocated support costs incurred by other entities in the Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations and charges included in the Company's financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on factors such as sales, net assets, or cost of sales; or a relative weighting of geographic activity. Management believes that the allocation methods are reasonable.

When Hercules acquired all of the outstanding shares of BetzDearborn Inc. on October 15, 1998 it paid \$2,235 million in cash and \$186 million in common stock exchanged for the shares held by the BetzDearborn ESOP Trust. The purchase price allocated to the Company and its subsidiaries was approximately \$232 million. During 1999, Hercules completed the purchase price allocation and the final determination of goodwill was \$1,822 million of which the amount attributable to the Company was approximately \$207 million. These financial statements include the push down of fair value adjustments to assets and liabilities, including goodwill, property, plant and equipment and their related amortization and depreciation adjustments.

As a result of this acquisition the Company, as a part of an effort by Hercules, entered into several internal reorganization transactions during 1999 and 2000. The transactions included the Company selling several of its investments in subsidiaries to Hercules affiliates, purchasing several investments in subsidiaries from Hercules affiliates, merging companies, and acquiring certain investments in Hercules group companies that are valued at cost. As all investments in this reorganization are under the common control of Hercules, these transactions have been accounted for in a manner similar to pooling of interest.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its majority-owned subsidiaries where control exists. Following the acquisition of BetzDearborn, the Company continued BetzDearborn's practice of



BETZDEARBORN INTERNATIONAL INCORPORATED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

using a November 30 fiscal year-end for certain former BetzDearborn non-U.S. subsidiaries to expedite the year-end closing process. Investments in affiliated companies with a 20% to 50% ownership interest are accounted for using the equity method of accounting and, accordingly, consolidated income includes the Company's share of their net income. All intercompany transactions and profits have been eliminated.

USE OF ESTIMATES

Preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

REVENUE RECOGNITION

The Company recognizes revenue when the earnings process is complete. This generally occurs when products are shipped to the customer or services are performed in accordance with terms of the agreement, title and risk of loss have been transferred, collectibility is probable, and pricing is fixed and determinable. Accruals are made for sales returns and other allowances based on the Company's experience. The corresponding shipping and handling costs are included in cost of sales.

ENVIRONMENTAL EXPENDITURES

Environmental expenditures that pertain to current operations or future revenues are expensed or capitalized according to the Company's capitalization policy, which is to charge repairs and maintenance to expense and capitalize replacements or betterments. Expenditures for remediation of an existing condition caused by past operations that do not contribute to current or future revenues are expensed. Liabilities are recognized for remedial activities when the cleanup is probable and can be reasonably estimated.

CASH AND CASH EQUIVALENTS

Cash in excess of operating requirements is invested in short-term, income-producing instruments. Cash equivalents include time deposits and other securities with original maturities of 90 days or less. Book value approximates fair value because of the short maturity of those instruments.

INVENTORIES

Inventories are stated at the lower of cost or market. Inventories are valued on the average cost method.

PROPERTY AND DEPRECIATION

Property, plant and equipment is recorded at cost. Depreciation is computed principally by the straight-line method over the estimated useful lives of the related assets. The estimated useful lives of depreciable assets are as follows: buildings-30 years; plant machinery and equipment-15 years; other

## Edgar Filing: HERCULES INC - Form 10-K/A

machinery and equipment—3 to 15 years.

The Company is engaged in several projects related to process or plant improvements. Costs are capitalized until the project is ready for intended use. The cost of business process reengineering, whether done internally or by a third party is expensed as incurred.

Maintenance, repairs, and minor renewals are charged to income; major renewals and betterments are capitalized. Upon normal retirement or replacement, the net book value of property (less proceeds of sale or salvage) is expensed.

### GOODWILL

Goodwill is amortized on a straight-line basis over 40 years, which is the estimated future period to be benefited.

Pursuant to Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (SFAS 142), beginning January 1, 2002, goodwill will not be amortized but will be tested for impairment annually and any necessary adjustment charged to expense. Intangible assets with finite lives will be amortized over their useful lives.

81

### BETZDEARBORN INTERNATIONAL INCORPORATED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### LONG-LIVED ASSETS

The Company reviews its long-lived assets, including goodwill for impairment on an exception basis whenever events or changes in circumstances indicate carrying amounts of the assets may not be recoverable through undiscounted future cash flows. If an impairment loss has occurred based on expected future cash flows (undiscounted), the loss is recognized in the income statement. The amount of the impairment loss is the excess of the carrying amount of the impaired asset over the fair value of the asset. The fair value represents expected future cash flows from the use of the assets, discounted at the rate used to evaluate potential investments.

### FOREIGN CURRENCY TRANSLATION AND TRANSACTIONS

The accompanying consolidated financial statements are reported in U.S. dollars. The U. S. dollar is the functional currency for the Company and its domestic subsidiaries and associated companies. The functional currencies of its foreign subsidiaries are translated into U.S. dollars for assets and liabilities using the current exchange rates in effect at the balance sheet date, and for revenues, costs and expenses using average exchange rates prevailing during the reporting periods. Adjustments resulting from the translation of functional currency financial statements to reporting currency are accumulated and reported as other comprehensive income (loss).

Transactions in foreign currency are recorded at the exchange rate prevailing on the date of transaction. Monetary assets and liabilities denominated in foreign currencies are expressed in the functional currency at the exchange rates in effect at the balance sheet date. Revenues, costs and expenses are recorded using average exchange rates prevailing during the reporting periods. Gains or losses resulting from foreign currency transactions are included in the statements of operations.

## Edgar Filing: HERCULES INC - Form 10-K/A

### CONCENTRATIONS OF CREDIT RISK

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of short-term cash investments and trade receivables. The Company places its short-term cash investments of \$8,189 thousand at December 31, 2001 and \$7,029 thousand at December 31, 2000 in securities with maturities of 90 days or less. These securities were concentrated in Argentina, Brazil and Chile, in which together held \$7,896 thousand in 2001, and by Brazil and Chile which held \$6,945 thousand in 2000. These securities are primarily denominated in the respective local currencies. Cost approximates market for these securities. Concentrations of credit risk with respect to trade receivables are limited due to the Company's large number of customers and their dispersion across many different industries and locations.

### STOCK-BASED COMPENSATION

Compensation costs attributable to stock option and similar plans are recognized based on any excess of the quoted market price of the stock on the date of grant over the amount the employee is required to pay to acquire the stock (the intrinsic-value method under Accounting Principles Board Opinion 25 (APB 25)). Such amount, if any, is accrued over the related vesting period, as appropriate. Statement of Financial Accounting Standard No. 123, "Accounting for Stock-based Compensation," requires companies electing to continue to use the intrinsic-value method to make pro forma disclosures of net income as if the fair-value-based method of accounting had been applied.

### COMPUTER SOFTWARE COSTS

Effective January 1, 1999, the Company adopted the American Institute of Certified Public Accountants Statement of Position 98-1, "Accounting for the Cost of Computer Software Developed or Obtained for Internal Use" (SOP 98-1). The Company's prior accounting was generally consistent with the requirements of SOP 98-1 and, accordingly adoption of SOP 98-1 had no material effect. Computer software costs are being amortized over a period of 5 to 10 years.

### RESEARCH AND DEVELOPMENT EXPENDITURES

Research and development expenditures are expensed as incurred.

### INCOME TAXES

The Company's operations have historically been included in the consolidated income tax returns filed by its parent. Income tax expense in the accompanying financial statements has been computed assuming the Company filed separate income tax returns. Differences between this calculation of income taxes currently payable and consolidated amounts reported in the consolidated financial statements of the parent have been reflected as Net Hercules Group Investment.

82

### BETZDEARBORN INTERNATIONAL INCORPORATED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### NET HERCULES GROUP INVESTMENT

The Net Hercules Group Investment account reflects the balance of the Company's historical earnings, intercompany amounts, income taxes, taxes accrued

## Edgar Filing: HERCULES INC - Form 10-K/A

and deferred, post-employment liabilities, foreign currency translation and other transactions between the Company and the Hercules Group.

### NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 141, "Business Combinations" ("SFAS 141") and SFAS 142. SFAS 141 supersedes Accounting Principles Board Opinion ("APB") No. 16, Business Combinations. The provisions of SFAS 141 (1) require that the purchase method of accounting be used for all business combinations initiated after June 30, 2001, (2) provide specific criteria for the initial recognition and measurement of intangible assets apart from goodwill and (3) require that unamortized negative goodwill be written off immediately as extraordinary gain instead of being deferred and amortized. SFAS 141 also requires that upon adoption of SFAS 142 the Company reclassify the carrying amounts of certain intangible assets into or out of goodwill, based on certain criteria. SFAS 142 supersedes APB No. 17, Intangible Assets, and is effective for fiscal years beginning after December 15, 2001. SFAS 142 primarily addresses the accounting for goodwill and intangible assets subsequent to their initial recognition. The provisions of SFAS 142 (1) prohibit the amortization of goodwill and indefinite-lived intangible assets, (2) require that goodwill and indefinite-lived intangible assets be tested annually for impairment (and in interim periods if certain events occur indicating that the carrying value of goodwill and/or indefinite-lived intangible assets may be impaired), based on fair value (as opposed to cost recovery using future undiscounted cash flows), (3) require that reporting units be identified for the purpose of assessing potential future impairments of goodwill and (4) remove the forty-year limitation on the amortization period of intangible assets that have finite lives.

Effective January 1, 2002 Hercules adopted the provisions of SFAS 142. Hercules identified the following reporting units: BetzDearborn, Pulp and Paper, Aqualon, FiberVisions and Resins. In connection with Hercules' transitional review, recorded goodwill was determined to be impaired in the BetzDearborn and FiberVisions reporting units. In the first quarter 2002, Hercules completed its transitional impairment review of the identified units and recognized an after tax impairment loss of \$368 million as a cumulative effect of a change of accounting principle, of which \$263 million related to the BetzDearborn reporting unit. As a result of Hercules' adoption of SFAS 142, the Company will no longer record \$5.1 million of annual amortization relating to existing goodwill and intangibles.

Goodwill related to the BetzDearborn business was evaluated for impairment at December 31, 2001 under Statement of Financial Accounting Standards No. 121 "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed of." Such evaluation indicated that goodwill associated with the business was recoverable from anticipated future undiscounted cash flows. Accordingly, no impairment loss was recorded in the December 31, 2001 financial statements.

In June 2001, the FASB approved the issuance of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143"). SFAS 143 establishes accounting standards for the recognition and

## Edgar Filing: HERCULES INC - Form 10-K/A

measurement of legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 will become effective for the Company from January 1, 2003 and requires recognition of a liability for an asset retirement obligation in the period in which it is incurred. The Company does not believe this statement will have a material effect on its financial statements.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company does not believe this statement will have a material effect on its financial statements.

In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment to FASB Statement No. 13, and Technical Corrections." The Company has elected to early adopt the provisions of SFAS 145 related to the rescission of SFAS 4, "Reporting Gains and Losses from the Extinguishment of Debt" ("SFAS 4"). The early adoption of SFAS 145 had no effect on the Company's financial statements.

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146"). SFAS 146 addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs in a Restructuring)." SFAS 146 defines the timing of the recognition of costs associated with exit or disposal activities, the types of costs that may be recognized and the methodology for calculating the fair value of such costs. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. The Company does not believe this statement will have a material effect on its financial statements.

### RECLASSIFICATIONS

Certain amounts in the 2000 and 1999 consolidated financial statements and notes have been reclassified to conform to the 2001 presentation.

84

### BETZDEARBORN INTERNATIONAL INCORPORATED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### 3. ACCOUNTS RECEIVABLE, NET

Accounts receivable, net, consists of:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Trade	\$ 43,701	\$ 38,575
Less allowance for doubtful accounts	(5,791)	(3,820)
	-----	-----
Total	\$ 37,910	\$ 34,755
	=====	=====

## Edgar Filing: HERCULES INC - Form 10-K/A

### 4. INVENTORIES

The components of inventories are:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Finished products	\$10,433	\$ 9,502
Materials, supplies, and work in process	8,860	9,759
	-----	-----
Total	\$19,293	\$19,261
	=====	=====

### 5. SHORT-TERM DEBT

A summary of short-term debt follows:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Lines of credit	\$ 852	\$13,776
Current maturities of long-term debt	163	486
	-----	-----
Total	\$ 1,015	\$14,262
	=====	=====

Lines of credit primarily represent foreign overdraft facilities and short-term lines of credit, which are generally payable on demand with interest at various rates. Book values of bank borrowings approximate market value because of their short maturity period.

At December 31, 2001 and 2000 the Company had \$962 thousand and \$23,467 thousand, respectively, of unused lines of credit that may be drawn as needed, with interest at a negotiated spread over the lenders' cost of funds. Weighted-average interest rates on short-term borrowings at December 31, 2001 and 2000 were 15.0% and 5.66%, respectively.

### 6. LONG-TERM DEBT AND OTHER FINANCING ARRANGEMENTS

Long-term debt with third parties at December 31, 2001 and 2000 is summarized below.

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousands)	
	2001	2000
	-----	-----
Construction loan -Bank of Hong Kong at 13.5%	\$ 2,548	\$ 1,442
Less current maturities	(163)	(486)
	-----	-----
Total	\$ 2,385	\$ 956
	=====	=====

The construction loan with Hong Kong bank has an additional availability of \$117 thousand and payments are due through 2007. The loan features a clause, which allows for no payments to be made for the years 2002 to 2004.

Scheduled annual maturities of long-term debt outstanding in the successive five-year period are summarized as follows:

	(Dollars in thousands)	
	2001	
	-----	
2002	\$	163
2003		--
2004		--
2005		298
2006		596
Thereafter		1,491
		-----
Total	\$	2,548
		-----
Less current maturities		(163)
		-----
Total	\$	2,385
		=====

The Company believes that the carrying value of borrowings approximates fair market value, based on discounting future cash flows using rates currently available for debt of similar terms and remaining maturities.

As of December 31, 2001 the Company had \$68,159 thousand of long term debt payable to affiliates that was primarily held by Hercules Shared Services Corporation, Hercules Europe B.V.B.A., BetzDearborn Canada, Inc., and Hercules Canada Inc., all wholly owned subsidiaries of Hercules. As of December 31, 2000 the Company had \$58,259 thousand of long term debt payable to affiliates that was primarily held by Hercules Shared Services Corporation, BetzDearborn Inc. and by Hercules Europe B.V.B.A., all wholly owned subsidiaries of Hercules. The long-term debt payable to affiliates primarily has no set payment schedule and carry interest rates ranging from 2.5% to 10.5%. The long term debt payable to affiliates is recorded in the Net Hercules Group Investment account in the financial statements.

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousands)		
	Interest Expense		
Components of interest expense:	2001	2000	1999
	-----	-----	-----
Third parties, net (income) expense	\$ (225)	\$ 1,861	\$ 1,507
Related parties, net expense	4,699	4,391	4,639
	-----	-----	-----
Interest expense	\$ 4,474	\$ 6,252	\$ 6,146
	=====	=====	=====

There was no capitalized interest during 2001, 2000 or 1999.

86

BETZDEARBORN INTERNATIONAL INCORPORATED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

7. LONG-TERM INCENTIVE COMPENSATION PLANS

The Company participates in long-term incentive compensation plans sponsored by Hercules. These plans provide for the grant of stock options and the award of common stock and other market-based units to certain key employees and non-employee directors.

In 1995, Hercules changed the structure of the long-term incentive compensation plans to place a greater emphasis on shareholder value creation through grants of regular stock options, performance-accelerated stock options, and Cash Value Awards (performance-based awards denominated in cash and payable in shares of common or restricted stock, subject to the same restrictions as restricted stock). Restricted stock and other market-based units are awarded with respect to certain programs. The number of awarded shares outstanding was 189,704 at December 31, 2001, 491,488 at December 31, 2000 and 926,689 at December 31, 1999.

At December 31, 2001, under Hercules' incentive compensation plans, 1,265,493 shares of common stock were available for grant as stock awards or stock option awards. Stock awards are limited to approximately 15% of the total authorizations. Regular stock options are granted at the market price on the date of grant and are exercisable at various periods from one to five years after date of grant. Performance-accelerated stock options are also granted at the market price on the date of grant and are normally exercisable at nine and one-half years. Exercisability may be accelerated based upon the achievement of predetermined performance goals. Both regular and performance-accelerated stock options expire 10 years after the date of grant.

Restricted shares, options and performance-accelerated stock options are forfeited and revert to Hercules in the event of employment termination, except in the case of death, disability, retirement, or other specified events.

The Company applies APB Opinion 25 in accounting for its plans. Accordingly, no compensation cost has been recognized for the stock option plans. There were no charges to income for the cost of stock awards over the restriction or performance period for 2001, 2000 and 1999.

Below is a summary of outstanding stock option grants under the incentive compensation plans during 1999, 2000 and 2001:



Edgar Filing: HERCULES INC - Form 10-K/A

	Regular		Performance-Accelerated	
	Number of Shares	Weighted-average Price	Number of Shares	Weighted-average Price
December 31, 1998	9,800	\$ 40.60	--	--
Granted	48,200	\$ 37.72	13,150	\$ 37.70
Exercised	--	--	--	--
Forfeited	--	--	--	--
December 31, 1999	58,000	\$ 38.21	13,150	\$ 37.70
Granted	37,675	\$ 17.25	--	--
Exercised	--	--	--	--
Forfeited	--	--	--	--
December 31, 2000	95,675	\$ 29.95	13,150	\$ 37.70
Granted	37,675	\$ 11.28	--	--
Exercised	--	--	--	--
Forfeited	(3,500)	\$ 37.85	--	--
December 31, 2001	129,850	\$ 24.32	13,150	\$ 37.70

The weighted-average fair value of regular stock options granted during 1999, 2000 and 2001 was \$8.26, \$8.85 and \$5.69, respectively. The weighted-average

87

BETZDEARBORN INTERNATIONAL INCORPORATED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

fair value of performance-accelerated stock options granted during 1999, 2000 and 2001 was \$8.01, \$0, and \$0, respectively.

Following is a summary of regular stock options exercisable at December 31, 1999, 2000, and 2001 and their respective weighted-average share prices:

Options Exercisable	Number of Shares	Weighted-average Exercise Price
December 31, 1999	7,320	\$40.09
December 31, 2000	28,820	\$38.61
December 31, 2001	60,590	\$33.09

There were no performance-accelerated stock options exercisable at December 31, 1999, 2000 and 2001.

## Edgar Filing: HERCULES INC - Form 10-K/A

Following is a summary of stock options outstanding at December 31, 2001:

Exercise Price Range	Number Outstanding at 12/31/2001	Weighted-average Remaining Contractual Life	Outstanding Options Weighted-average Exercise Price	Exercis Nu 12/3
Regular Stock Options				
\$11 - \$20	75,350	8.89	\$14.27	1
\$30 - \$40	53,200	7.11	\$37.99	4
\$40 - \$50	1,300	6.35	\$47.81	
	----- 129,850 =====			----- 6 =====
Performance-Accelerated Stock Options				
\$14 - \$40	13,150	7.36	\$37.70	=====

The Company currently expects that 100% of performance-accelerated stock options will eventually vest.

The Company's employees may also participate in the Hercules Employee Stock Purchase Plan ("ESPP"). The ESPP is a qualified non-compensatory plan, which allows eligible employees to acquire shares of common stock through systematic payroll deductions. The plan consists of three-month subscription periods, beginning July 1 of each year. The purchase price is 85% of the fair market value of the common stock on either the first or last day of that subscription period, whichever is lower. Purchases may range from 2% to 15% of an employee's base salary each pay period, subject to certain limitations. Currently, there are no shares of Hercules common stock registered for offer and sale under the plan. Shares issued at December 31, 2001 and 2000 were 1,758,081 and 1,597,861, respectively. The Company applies APB Opinion 25 and related interpretations in accounting for its Employee Stock Purchase Plan. Accordingly, no compensation cost has been recognized for the Employee Stock Purchase Plan.

Had compensation cost for Hercules' Stock-Based Incentive Plans and Employee Stock Purchase Plan been determined on the basis of fair value according to SFAS No. 123, the fair value of each option granted or share purchased would be estimated on the grant date using the Black-Scholes option pricing model.

88

BETZDEARBORN INTERNATIONAL INCORPORATED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following weighted-average assumptions would be used in estimating fair value for 2001, 2000 and 1999.

Regular	Performance	Employee Stock
---------	-------------	----------------

## Edgar Filing: HERCULES INC - Form 10-K/A

Assumption -----	Plan -----	Accelerated Plan -----	Purchase Plan -----
Dividend yield	1%	3.83%	0.0%
Risk-free interest rate	5.80%	5.57%	4.86%
Expected life	7.1 yrs.	5 yrs.	3 mos.
Expected volatility	33.36%	29.78%	49.11%

The Company's net income and earnings for 2001, 2000 and 1999 would approximate the pro forma amounts below:

	(Dollars in thousands)		
	2001 -----	2000 -----	1999 -----
Net loss			
As reported	\$(2,403)	\$(4,008)	\$(4,246)
Pro forma	\$(2,611)	\$(4,213)	\$(4,335)

### 8. ADDITIONAL BALANCE SHEET DETAIL

	(Dollars in thousands)	
	2001 -----	2000 -----
Property, plant, and equipment		
Land	\$ 6,622	\$ 7,085
Buildings and equipment	50,921	48,455
Construction in progress	1,462	4,123
Total	59,005	59,663
Accumulated depreciation and amortization	(22,002)	(18,472)
Net property, plant, and equipment	\$ 37,003 =====	\$ 41,191 =====
Accrued expenses		
Payroll and related taxes	\$ 3,733	\$ 3,623
Incentives / bonus	2,315	2,222
Restructuring liability (Note 10)	1,569	3,861
Pension	637	682
Other	3,217	6,876
	\$ 11,471 =====	\$ 17,264 =====

## Edgar Filing: HERCULES INC - Form 10-K/A

### 9. GOODWILL, NET

Goodwill at December 31, 2001 and 2000 was:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Goodwill	\$ 204,724	\$ 209,973
Less accumulated amortization	(17,600)	(12,477)
	-----	-----
Total	\$ 187,124	\$ 197,496
	=====	=====

### 10. RESTRUCTURING

The consolidated balance sheet reflects liabilities for employee severance benefits and other exit costs of \$1,569 thousand and \$3,861 thousand, respectively at December 31, 2001 and 2000. During 2001, management authorized and committed to a plan to reduce the workforce as part of the comprehensive cost reduction and work process redesign program. The Company incurred restructuring charges of \$2,430 thousand, for employee termination benefits and exit costs related to facility closures. Under this plan, approximately 72 employees have left the Company. The plan includes reductions throughout the Company with the majority of them from support functions as well as the BetzDearborn and Pulp and Paper units.

Pursuant to the plans in place to merge the operations of BetzDearborn with Hercules and to rationalize the support infrastructure and other existing operations, a \$1,328 thousand reserve was established by the Company in 1998 and further increased by \$4,499 thousand in 1999. 35 people were terminated in 1999, 17 in 2000 and 72 in 2001. Cash payments made during 2001 and 2000 include \$1,535 thousand and \$665 thousand, respectively, for severance benefits and \$593 thousand and \$125 thousand, respectively, for other exit costs.

During 2001, the Company completed assessments of the remaining expenditures for the 1998 BetzDearborn plan and the 2000 plans, respectively. As a result of these assessments, the estimates for severance benefits and other exit costs were lowered by \$2,487 thousand, with corresponding reductions to goodwill. The lower than planned severance benefits are the result of higher than anticipated attrition, with voluntary resignations not requiring the payment of termination benefits.

Severance benefit payments are based on years of service and generally continue for 3 months to 24 months subsequent to termination. We expect to substantially complete remaining actions under the plans in 2002. A reconciliation of activity with respect to the liabilities established for these plans is as follows:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Balance at beginning of year	\$ 3,861	\$ 4,554

## Edgar Filing: HERCULES INC - Form 10-K/A

Additional termination benefits and exit costs	2,430	124
Cash payments	(2,128)	(790)
Reversals against goodwill	(2,487)	--
Currency effects	(107)	(27)
	-----	-----
 Balance at end of year	 \$ 1,569	 \$ 3,861
	=====	=====

### 11. PENSION BENEFITS

The Company has a non-contributory defined benefit plan covering all of its employees in the Republic of China. The Company funds the plans through trust arrangements where the assets of the fund are held separately from the employer. The level of funding is in line with local practice and in accordance with the local tax and supervisory requirements. The following table lists benefit obligations, plan assets, and funded status of the plans.

90

BETZDEARBORN INTERNATIONAL INCORPORATED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

	(Dollars in thousands)	
	Pension Benefits	
	2001	2000
	-----	-----
<b>CHANGE IN BENEFIT OBLIGATION</b>		
Benefit obligation at January 1	\$ 2,665	\$ 2,854
Service cost	298	289
Interest cost	148	157
Benefits paid from plan assets	(621)	(489)
Actuarial loss	675	--
Translation adjustments	(115)	(146)
	-----	-----
Benefit obligation at December 31	\$ 3,050	\$ 2,665
	=====	=====
 <b>CHANGE IN PLAN ASSETS</b>		
Fair value of plan assets at January 1	2,069	2,381
Actual return on plan assets	101	144
Company contributions	217	122
Benefits paid from plan assets	(621)	(464)
Translation adjustments	(76)	(114)
	-----	-----
Fair value of plan assets at December 31	\$ 1,690	\$ 2,069
	=====	=====
 Funded status of the plans	 (1,360)	 (595)
Unrecognized net loss	667	540
Unrecognized net transition obligation	488	--
	-----	-----
Accrued prepaid benefit cost	\$ (205)	\$ (55)

Edgar Filing: HERCULES INC - Form 10-K/A

	=====	=====
ASSUMPTIONS AS OF DECEMBER 31		
Weighted-average discount rate	5.00%	6.00%
Expected return on plan assets	5.00%	6.00%
Rate of compensation increase	5.00%	6.00%

	(Dollars in thousands)		
	Pension Benefits		
Components of net periodic benefit cost:	2001	2000	1999
	-----	-----	-----
Service cost	\$ 298	\$ 289	\$ 245
Interest cost	148	157	143
Expected return on plan assets	(105)	(144)	(109)
Amortization of net (gain) loss	--	--	22
Amortization of transition asset	31	34	(16)
	-----	-----	-----
Benefit cost	\$ 372	\$ 336	\$ 285
	=====	=====	=====

91

BETZDEARBORN INTERNATIONAL INCORPORATED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The Company also participates in defined contribution plans, which supplements the local government pension plans. The Company's employees may contribute from 5% to 12% of their annual compensation to the plan each calendar year. The Company's matching contribution was approximately \$270 thousand for 2001, \$520 thousand for 2000 and \$460 thousand for 1999.

12. OTHER OPERATING EXPENSES, NET,

	(Dollars in thousands)		
	Other Operating Expenses		
Components of other operating expenses:	2001	2000	1999
	-----	-----	-----
Royalty expense	\$5,103	\$5,599	\$4,901
Integration	--	68	1,118
Restructuring	1,307	124	531
Miscellaneous other	15	161	548
	-----	-----	-----
Other operating expenses	\$6,425	\$5,952	\$7,098
	=====	=====	=====

13. OTHER EXPENSE, NET

## Edgar Filing: HERCULES INC - Form 10-K/A

Other Expense, net, consists primarily of exchange and transaction losses for 2001, 2000 and 1999.

### 14. NET HERCULES GROUP INVESTMENT

Changes in Net Hercules Group Investment were as follows:

	(Dollars in thousands)
	-----
Balance, December 31, 1998	\$ 286,177
Net loss	(4,246)
Other comprehensive income	(989)
Intercompany balances, net	(1,546)
	-----
Balance, December 31, 1999	\$ 279,396
Net loss	(4,008)
Other comprehensive income	(2,061)
Intercompany balances, net	(10,926)
	-----
Balance, December 31, 2000	\$ 262,401
Net loss	(2,403)
Other comprehensive income	(4,568)
Intercompany balances, net	15,632
	-----
Balance, December 31, 2001	\$ 271,062
	=====

92

### BETZDEARBORN INTERNATIONAL INCORPORATED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The Company includes accumulated other comprehensive income in Net Hercules Group Investment. At December 31, 2001, 2000 and 1999, accumulated other comprehensive income included (\$27,537) thousand, (\$22,969) thousand and (\$20,908) thousand, respectively, of foreign currency translation adjustments.

### 15. INCOME TAXES

The domestic and foreign components of income (loss) before taxes and minority interest are presented below:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Domestic	\$ (4,930)	\$ (4,904)	\$ 1,042
Foreign	6,673	3,491	(2,119)
	-----	-----	-----

Edgar Filing: HERCULES INC - Form 10-K/A

\$ 1,743	\$ (1,413)	\$ (1,077)
=====	=====	=====

A summary of the components of the tax provision follows:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Currently payable			
Domestic	\$ (840)	\$ --	\$ 1,890
Foreign	3,139	2,575	1,017
Deferred			
Domestic	(166)	(698)	133
Foreign	375	(266)	(20)
	-----	-----	-----
Provision for income taxes	\$ 2,508	\$ 1,611	\$ 3,020
	=====	=====	=====

Deferred tax assets (liabilities) at December 31 consisted of:

93

BETZDEARBORN INTERNATIONAL INCORPORATED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

	(Dollars in thousands)	
	2001	2000
	-----	-----
Depreciation	\$ --	\$ (977)
Investments	--	--
Other	(1,902)	(198)
	-----	-----
Gross deferred tax liabilities	\$ (1,902)	\$ (1,175)
	-----	-----
Postretirement benefits other than pensions	\$ 762	\$ 1,047
Inventory	3	316
Accrued expenses	5,187	6,272
Loss carryforwards	10,598	9,175
	-----	-----
Gross deferred tax assets	16,550	16,810
Valuation allowance	(13,555)	(14,375)
	-----	-----
Deferred tax assets, net	2,995	2,435
	-----	-----
	\$ 1,093	\$ 1,260
	=====	=====

A reconciliation of the statutory income tax rate to the effective rate



Edgar Filing: HERCULES INC - Form 10-K/A

follows:

	2001	2000	1999
	----	----	----
Statutory income tax rate	35%	(35)%	(35)%
Goodwill amortization	81	121	168
Meals and entertainment	6	11	17
Foreign dividends net of credits	--	--	9
Valuation allowance	72	80	146
Cash repatriations from non-US subsidiaries	(44)	(84)	(41)
Travel expense	2	5	8
Other	(8)	16	8
	-----	-----	-----
Effective tax rate	144%	114%	280%
	=====	=====	=====

The net operating losses have indefinite carryforward periods, but may be limited in their use in any given year.

The Company provides taxes on undistributed earnings of foreign subsidiaries and affiliates included in Net Hercules Group Investment to the extent such earnings are planned to be remitted and not reinvested permanently. The undistributed earnings of subsidiaries and affiliates on which no provision for foreign withholding or U.S. income taxes has been made amounted to approximately \$19,228 thousand, \$13,740 thousand and \$6,559 thousand at December 31, 2001, 2000 and 1999, respectively.

94

BETZDEARBORN INTERNATIONAL INCORPORATED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

16. COMMITMENTS AND CONTINGENCIES

Leases

The Company has operating leases (including office space, transportation, and data processing equipment) expiring at various dates. Rental expense was \$4,657 thousand in 2001, \$3,065 thousand in 2000 and \$2,726 thousand in 1999.

Future minimum lease payments under noncancellable operating leases are as follows:

	(Dollars in thousands)
	2001
	-----
2002	\$ 2,642
2003	1,303
2004	859
2005	711
2006	707

## Edgar Filing: HERCULES INC - Form 10-K/A

Thereafter	273
	-----
	\$ 6,495
	=====

### Litigation

The Company currently and from time to time is involved in litigation to the conduct of its business. In the opinion of the Company's management none of such litigation as of December 31, 2001 is likely to have a material adverse effect on the financial position and results of operations of the Company.

### 17. RELATED PARTY TRANSACTIONS

The Company has entered into certain agreements with affiliated entities. These agreements were developed in the context of parent/subsidiary relationship and therefore may not necessarily reflect the result of arms-length negotiations between independent parties. The Company records sales with affiliates generally based on a cost-plus formula developed and agreed-upon by both parties.

Corporate and other allocations: As discussed in Note 1, the financial statements of the Company reflect certain allocated support costs incurred by other entities in Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, research & development overhead, investor relations and other corporate services. Allocations and charges included in the Company's financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on factors such as revenues, net assets, costs of sales or a relative weighting of geographic activity. These allocations are reflected in the selling, general and administrative line item in our statement of operations. Such allocations and corporate charges totaled \$4,517 thousand, \$6,055 thousand and \$6,262 thousand in 2001, 2000 and 1999, respectively.

The Company has net advances to affiliates at December 31, 2001 of \$15,037 thousand and at December 31, 2000 of \$16,210 thousand. These advances are to BetzDearborn Inc. and BetzDearborn Europe Inc. The advances are also recorded as part of the Net Hercules Group Investment account.

Royalty expense: The Company entered into a license agreement, which pertains to foreign licensing rights for certain patents, trademarks, and know-how (technology) related to the manufacture of specialty chemical products. The royalties are payable to BL Technologies, Inc., a related party, 50% owned by BetzDearborn Inc. and 50% owned by BetzDearborn Europe, Inc. Royalty expense for 2001, 2000 and 1999 was \$5,103 thousand, \$5,599 thousand and \$4,901 thousand, respectively. Beginning in the year 2000 and for seven years thereafter, the fees are to be split between BL Technologies and Hercules on a declining rights basis favoring Hercules in the "out years." The royalty

expense is included as part of other operating expenses in the financial statements.

## Edgar Filing: HERCULES INC - Form 10-K/A

The Company from time to time will purchase finished or semi finished product from affiliated companies. For the years ended December 31, 2001, 2000 and 1999, these purchases totaled \$13,128 thousand, \$7,171 thousand and \$605 thousand, respectively.

### 18. SUBSEQUENT EVENT

On April 29, 2002, Hercules completed the sale of its Water Treatment Business to GE Specialty Materials (GESM). Pursuant to the Stock and Asset Agreement for the transaction, the sale included all of the stock of BetzDearborn and the Company. Hercules used the proceeds from the sale to prepay borrowings under its Senior Credit Facility and ESOP Credit Facility. Pursuant to the prepayment, among other things, the stock pledges were released.

96

### REPORT OF INDEPENDENT ACCOUNTANTS

TO THE SHAREHOLDERS AND THE BOARD OF DIRECTORS OF  
HERCULES INCORPORATED  
WILMINGTON, DELAWARE

In our opinion, the accompanying balance sheets and the related statements of income and of cash flows present fairly, in all material respects, the financial position of BL Technologies, Inc., a subsidiary of Hercules Incorporated, at December 31, 2001 and 2000, and the results of its operations and of its cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP  
Philadelphia, Pennsylvania  
October 25, 2002

97

BL TECHNOLOGIES, INC.  
STATEMENT OF INCOME

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousands)		
	Year Ended December 31		
	2001	2000	1999
	----	----	----
Royalty income	\$ 21	\$ 172	\$ 139
Royalty income - affiliates	17,485	20,972	22,785
	-----	-----	-----
	17,506	21,144	22,924
Selling, general, and administrative expenses	13	13	15
Corporate and other cost allocations	2,346	2,188	2,941
Amortization of licensing rights	9,464	11,358	13,250
	-----	-----	-----
Profit from operations	5,683	7,585	6,718
Other income, net (Note 4)	7	211	36
	-----	-----	-----
Income before income taxes	5,690	7,796	6,754
Provision for income taxes (Note 5)	1,992	2,729	2,363
	-----	-----	-----
Net income	\$ 3,698	\$ 5,067	\$ 4,391
	=====	=====	=====

The accompanying notes are an  
integral part of the financial statements.

98

BL TECHNOLOGIES, INC.  
BALANCE SHEETS

	(Dollars in thousands)	
	December 31	
	2001	2000
	-----	-----
ASSETS		
Current assets		
Cash and cash equivalents	\$ 732	\$ 19
	-----	-----
Total current assets	732	19
Investment in Hercules International Limited	72,962	72,962
Licensing rights, net (Note 3)	18,928	28,392
	-----	-----
Total assets	\$ 92,622	\$101,373
	=====	=====
LIABILITIES AND NET HERCULES GROUP INVESTMENT		
Liabilities		
Income taxes payable	\$ 5,304	\$ 6,704
Deferred income taxes (Note 5)	6,625	9,937
	-----	-----

Edgar Filing: HERCULES INC - Form 10-K/A

Total liabilities	11,929	16,641
Commitments and contingencies (Note 6)		--
Net Hercules Group Investment (Note 9)		
Intercompany transactions, net	80,693	84,732
	-----	-----
Net Hercules Group Investment	80,693	84,732
	-----	-----
Total liabilities and net Hercules Group investment	\$ 92,622	\$101,373
	=====	=====

The accompanying notes are an integral part of the financial statements.

99

BL TECHNOLOGIES, INC.  
STATEMENTS OF CASH FLOWS

	2001	(Dollars Year End
	-----	-----
CASH FLOW FROM OPERATING ACTIVITIES:		
Net Income	\$ 3,698	\$
Adjustments to reconcile net income to net cash provided by operations:		
Amortization of licensing rights	9,464	
Deferred income taxes	(3,312)	
Corporate and other allocations	2,346	
Accruals and deferrals of cash receipts and payments:		
Foreign currency contract receivable	--	
Income taxes payable	(1,400)	
Transfers to/from Hercules Group	--	
	-----	-----
Net cash provided by operations	10,796	
	-----	-----
CASH FLOW FROM FINANCING ACTIVITIES:		
Transfers to/from Hercules Group	(10,083)	
	-----	-----
Net cash used in financing activities	(10,083)	
	-----	-----
Net decrease in cash and cash equivalents	713	
Cash and cash equivalents at beginning of year	19	
	-----	-----
Cash and cash equivalents at end of year	\$ 732	\$
	=====	=====
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Noncash financing activities:		
Corporate and other cost allocations	\$ 2,346	\$

The accompanying notes are an integral part of the financial statements.

BL TECHNOLOGIES, INC.  
NOTES TO FINANCIAL STATEMENTS

---

1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

BL Technologies, Inc. ("BL Tech" or the "Company") was incorporated in 1994 in the state of Delaware as an Investment Holding Company for the purpose of providing certain financial services to its majority shareholder and former parent company, BetzDearborn Inc. (BetzDearborn). BL Tech and BetzDearborn are wholly owned subsidiaries of Hercules Incorporated ("Hercules"). The Company's primary business activity is the licensing of technologies (e.g., patents, trademarks, and formulations) and the collection of royalties therefrom to foreign based affiliates of the Hercules Group.

When Hercules acquired all of the outstanding shares of BetzDearborn Inc. on October 15 1998, it paid \$2,235 million in cash and \$186 million in common stock in exchange for the shares held by the BetzDearborn ESOP Trust. The purchase price allocated to the Company was approximately \$53 million. During 1999, Hercules completed the purchase price allocation and the final determination of goodwill was \$2,170. These financial statements include the pushdown of fair value adjustments to assets and liabilities including other intangible assets and the related amortization adjustment.

Effective January 1, 2000, Hercules began funding all research and development costs and became the owner of all future technologies. The Company continues to have economic rights to license the technologies in existence prior to January 1, 2000 and receive annual royalties related to such rights from Hercules and its affiliates. Accordingly, as part of recording the acquisition under the purchase accounting method, the Company measured the value of its licensing rights giving consideration to the future cash flows thereby reflecting the licensing rights at fair value.

As a result of the acquisition, during 1999, the Company was a party to one of several reorganization transactions initiated by Hercules. The transaction included the Company exchanging an investment in a BetzDearborn subsidiary for an 8.5% investment in Hercules International Limited. As this investment is under the common control of Hercules, it has been accounted for at book value and consolidated on an "as if" pooling basis for all periods presented.

The Company also has a .001% investment in the stock of Hercules de Colombia S.A., an affiliate.

Historically, separate company stand-alone financial statements were not prepared for the Company. In November 2000, Hercules amended its senior credit facility and ESOP credit facility (the "Facilities"). The Facilities, as amended, are secured by liens on Hercules' property and assets (and those of Hercules' Canadian Subsidiaries), a pledge of the stock of substantially all of Hercules' domestic subsidiaries (including the Company) and 65% of the stock of foreign subsidiaries directly owned by Hercules, and a pledge of Hercules' domestic intercompany indebtedness. These financial statements present the financial information of the Company, a collateral party to the Hercules debt, based on the Company's understanding of the Securities and Exchange Commission's interpretation and application of Rule 3-16 under the Securities and Exchange Commission's Regulation S-X. These statements were derived from historical accounting records.

## Edgar Filing: HERCULES INC - Form 10-K/A

On April 29, 2002, in connection with Hercules' sale of its Water Treatment Business (see Note 8) and the repayment of the Facilities, the stock pledges were released. As a result, based on Hercules' current debt structure, these separate company stand-alone financial statements will not be required for the fiscal year ending December 31, 2002.

The financial statements of the Company reflect certain allocated support costs incurred by other entities in the Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations and charges included in the Company's financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on net assets; or a relative weighting of geographic activity. Management believes that the allocation methods are reasonable.

BL Tech participates in Hercules' centralized cash management system. Accordingly, cash received from BL Tech operations is transferred to Hercules on a periodic basis, and Hercules funds all operational requirements.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### USE OF ESTIMATES

Preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

101

BL TECHNOLOGIES, INC.  
NOTES TO FINANCIAL STATEMENTS

---

#### REVENUE RECOGNITION

Royalty income is based on a fixed percentage of the licensee's sales. The Company recognizes royalty revenue when the earnings process is complete. This generally occurs when the licensee has shipped product to the customer. Accruals are made for royalty refunds and other allowances based on the Company's experience

#### CASH AND CASH EQUIVALENTS

Cash in excess of operating requirements is invested in short-term, income-producing instruments. Cash equivalents include securities with original maturities of 90 days or less. Book value approximates fair value because of the short maturity of those instruments.

#### LICENSING RIGHTS

Licensing rights are amortized on a sum of years digits basis during the economic life of such rights, which is seven years.

#### FOREIGN CURRENCY TRANSACTIONS

Transactions in foreign currency, primarily royalty payments, are recorded at the exchange rate prevailing on the date of transaction. Monetary assets and

## Edgar Filing: HERCULES INC - Form 10-K/A

liabilities denominated in foreign currencies are expressed in the functional currency at the exchange rates in effect at the balance sheet date. Revenues, costs and expenses are recorded using average exchange rates prevailing during the reporting periods. Gains or losses resulting from foreign currency transactions are included in the statement of operations.

### CONCENTRATIONS OF CREDIT RISK

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of short-term cash investments and receivables from affiliated companies. The Company places its short-term cash investments in a highly-liquid money market account at a large financial institution.

### DERIVATIVE INSTRUMENTS AND HEDGING

The Company has entered into forward-exchange contracts to hedge foreign currency exposure. Decisions regarding hedging have been made on a case-by-case basis, taking into consideration the amount and duration of the exposure, market volatility, and economic trends. The Company uses the fair-value method of accounting, recording realized and unrealized gains and losses on these contracts monthly. They are included in other income (expense), net. It is the Company's policy to match the term of financial instruments with the term of the underlying designated item. The Company does not hold or issue financial instruments for trading purposes. In the Statement of Cash Flows, the Company reports the cash flows resulting from its hedging activities in the same category as the related item that is being hedged.

### INCOME TAXES

The Company's operations have historically been included in the consolidated income tax returns filed by its parent. Income tax expense in the accompanying financial statements has been computed assuming the Company filed separate income tax returns. Differences between this calculation of income taxes currently payable and consolidated amounts reported in the consolidated financial statements of the parent have been reflected as net Hercules Group investment.

### NET HERCULES GROUP INVESTMENT

The net Hercules Group investment account reflects the balance of BL Tech's historical earnings, intercompany amounts, income taxes, taxes accrued and deferred, foreign currency translation and other transactions between the Company and the Hercules Group.

### NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, the FASB approved the issuance of Statement of Financial Accounting Standards No. 141, "Business Combinations" ("SFAS 141") and Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"). For BL Tech, these statements will generally become effective January 1, 2002, although business combinations initiated after June 30, 2001 are subject to the non-amortization and purchase accounting provisions.



## Edgar Filing: HERCULES INC - Form 10-K/A

SFAS 142 stipulates that goodwill and other intangible assets with indefinite lives are no longer subject to amortization, but must be evaluated periodically for impairment beginning January 1, 2002. The impairment assessment provisions of SFAS 142 will not have an impact on the Company's financial statements.

In June 2001, the Financial Accounting Standards Board ("FASB") approved the issuance of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143"). SFAS 143 establishes accounting standards for the recognition and measurement of legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 will become effective for the Company on January 1, 2003 and requires recognition of a liability for an asset retirement obligation in the period in which it is incurred. The Company does not believe this statement will have a material effect on its financial statements.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company does not believe this statement will have a material effect on its financial statements.

In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment to FASB Statement No. 13, and Technical Corrections." The Company has elected to early adopt the provisions of SFAS 145 related to the rescission of SFAS 4, "Reporting Gains and Losses from the Extinguishment of Debt" ("SFAS 4"). Accordingly, the prepayment penalties and the write-off of debt issuance costs relating to the April 2002 debt repayment (see Note 11) are reported in net (loss) income from continuing operations. Under SFAS 4, the majority of these costs would have been reported as an extraordinary loss in the Consolidated Statement of Operations.

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146"). SFAS 146 addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs in a Restructuring)". SFAS 146 defines the timing of the recognition of costs associated with exit or disposal activities, the types of costs that may be recognized and the methodology for calculating the fair value of such costs. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. The Company does not believe this statement will have a material effect on its financial statements.

### 3. LICENSING RIGHTS

The Company has an exclusive right to license Hercules technologies for a seven year period from its date of acquisition on October 15, 1998. At December 31, 2001 and 2000, licensing rights were:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Licensing rights	\$ 53,000	\$ 53,000
Less accumulated amortization	(34,072)	(24,608)
	-----	-----
Licensing rights, net	\$ 18,928	\$ 28,392
	=====	=====

Edgar Filing: HERCULES INC - Form 10-K/A

4. OTHER INCOME (EXPENSE), NET

Other income (expense), net, consists of the following:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Interest income, net	\$ 8	\$ 1	\$ 11
Foreign exchanges (loss) gains	(1)	210	25
	-----	-----	-----
	\$ 7	\$ 211	\$ 36
	=====	=====	=====

103

BL TECHNOLOGIES, INC.  
NOTES TO FINANCIAL STATEMENTS

---

5. INCOME TAXES

A summary of the components of the tax provision follows:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Currently payable	\$ 5,304	\$ 6,704	\$ 7,001
Deferred	(3,312)	(3,975)	(4,638)
	-----	-----	-----
Provision for income taxes	\$ 1,992	\$ 2,729	\$ 2,363
	=====	=====	=====

Deferred tax liabilities at December 31 consist of:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Intangible assets	\$6,625	\$9,937
	-----	-----
Gross deferred tax liabilities	6,625	9,937
	-----	-----
Valuation allowance	--	--
	-----	-----
	\$6,625	\$9,937
	=====	=====

## Edgar Filing: HERCULES INC - Form 10-K/A

### 6. COMMITMENTS AND CONTINGENCIES

The Company had an operating lease for office space which expired September 30, 2001. Rental expense was \$2 thousand in 2001 and 2000 and \$1 thousand in 1999.

### 7. RELATED PARTY TRANSACTIONS

BL Tech has entered into certain agreements with affiliated entities. These agreements were developed in the context of parent/subsidiary relationship and therefore may not necessarily reflect the result of arms-length negotiations between independent parties.

Corporate and other allocations: As discussed in Note 1, the financial statements of BL Tech reflect certain allocated support costs incurred by other entities in Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, research & development overhead, investor relations and other corporate services. Allocations and charges included in BL Tech's financial statements were based on either a direct cost pass-through for items directly identified as related to BL Tech's activities; a percentage allocation for such services provided based on factors such as revenues, net assets, or a relative weighting of geographic activity. These allocations are reflected in the corporate and other cost allocations line in our statement of income. Such allocations and corporate charges totaled \$2,346 thousand, \$2,188 thousand and \$2,941 thousand in 2001, 2000 and 1999, respectively.

Royalties: BL Tech has an exclusive right to license Hercules technologies to foreign based affiliates of the Hercules Group and enters into a licensing agreements in respect of the use of manufacturing formulations and specifications with affiliated companies which are developed and owned by Hercules. BL Tech received royalties in respect of this agreement of \$17,485 thousand, \$20,972 thousand and \$22,785 thousand in 2001, 2000 and 1999, respectively.

### 8. SUBSEQUENT EVENTS

On April 29, 2002, Hercules completed the sale of its Water Treatment Business to GE Specialty Materials (GESM). Pursuant to the Stock and Asset Agreement for the transaction, the sale included all of the stock of BetzDearborn and the Company. Hercules used the proceeds from the sale to prepay borrowings under its Senior Credit Facility and ESOP Credit Facility. Pursuant to the prepayment, among other things, the stock pledges were released.

104

BL TECHNOLOGIES, INC.  
NOTES TO FINANCIAL STATEMENTS

---

### 9. NET HERCULES GROUP INVESTMENT

Changes in net parent investment were as follows:

Edgar Filing: HERCULES INC - Form 10-K/A

(Dollars in thousands)

Balance, December 31, 1999	\$ 91,937
Net income	5,067
Intercompany transactions, net	(12,272)
	-----
Balance, December 31, 2000	84,732
Net income	3,698
Intercompany transactions, net	(7,737)
	-----
Balance, December 31, 2001	\$ 80,693
	=====

105

REPORT OF INDEPENDENT ACCOUNTANTS

TO THE SHAREHOLDERS AND THE BOARD OF DIRECTORS OF  
HERCULES INCORPORATED  
WILMINGTON, DELAWARE

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations and comprehensive income (loss) and of cash flows present fairly, in all material respects, the financial position of FiberVisions A/S, a subsidiary of Hercules Incorporated, and its subsidiaries at December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America that require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers  
Skive, Denmark  
November 19, 2002

106

FIBERVISIONS A/S  
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

	(Dollars in thou
	Year ended Decemb
	2001
	2000
	-----
	-----

Edgar Filing: HERCULES INC - Form 10-K/A

Sales to third parties	\$ 87,863	\$ 94,405
Sales to affiliates	15,463	13,414
Sales to Hercules Group	27,780	36,471
	-----	-----
	131,106	144,290
Cost of sales	111,075	128,103
Selling, general, and administrative expenses	3,717	4,586
Research and development	910	1,017
Impairment of long lived assets (Note 12)	--	28,169
Other operating expenses, net (Note 13)	2,984	2,745
	-----	-----
Profit (loss) from operations	12,420	(20,330)
Equity income of affiliated companies	4,409	2,617
Interest expense, net (Note 11)	2,697	2,234
	-----	-----
Income (loss) before income taxes	14,132	(19,947)
Provision for income taxes (Note 14)	5,318	3,430
	-----	-----
Net income (loss)	8,814	(23,377)
Translation adjustments, net of tax	1,274	1,299
	-----	-----
Comprehensive income (loss)	\$ 10,088	\$ (22,078)
	=====	=====

The accompanying notes are an integral part of the consolidated financial statements.

107

FIBERVISIONS A/S  
CONSOLIDATED BALANCE SHEETS

	(Dollars in thousands)	
	December 31,	
	2001	2000
	-----	-----
ASSETS		
Current assets		
Cash and cash equivalents	\$ 5,500	\$ 3,629
Accounts receivable, net (Note 3)	16,452	18,939
Receivables from affiliates (Note 5)	2,522	2,815
Inventories (Note 4)	5,829	6,143
	-----	-----
Total current assets	30,303	31,526
Property, plant, and equipment, net (Notes 8 and 12)	84,482	95,030
Investments (Note 6)	21,215	18,140
Goodwill and other intangible assets, net (Note 9)	95,307	98,058
Deferred charges and other assets	176	198
	-----	-----
Total assets	\$231,483	\$242,952
	=====	=====

## Edgar Filing: HERCULES INC - Form 10-K/A

### LIABILITIES AND NET HERCULES GROUP INVESTMENT

#### Current liabilities

Accounts payable	\$ 8,761	\$ 12,927
Current maturities of long-term debt (Note 7)	7,532	11,588
Accrued expenses (Note 8)	11,051	6,585
	-----	-----
Total current liabilities	27,344	31,100
Long-term debt - third parties (Note 7)	44,489	53,919
Deferred income taxes (Note 14)	22,631	18,737
	-----	-----
Total liabilities	94,464	103,756
Commitments and contingencies (Note 16)	--	--
Net Hercules Group investment (Note 15)		
Accumulated other comprehensive income	3,625	2,351
Intercompany transactions	133,394	136,845
	-----	-----
Net Hercules Group Investment	137,019	139,196
	-----	-----
Total liabilities and net Hercules Group Investment	\$231,483	\$242,952
	=====	=====

The accompanying notes are an integral part of the consolidated financial statements.

108

### FIBERVISIONS A/S CONSOLIDATED STATEMENTS OF CASH FLOWS

-----

	(Dollars in thousands)	
	Year ended December 31,	
	2001	2000
	-----	-----
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	\$ 8,814	\$ (23,377)
Adjustments to reconcile net income (loss) to net cash provided from operations:		
Depreciation	8,707	10,054
Provision for impairment of long-lived assets	--	28,169
Amortization of goodwill and other intangible assets	2,644	2,696
Bad debt expense	--	216
Nonoperating loss on disposals	18	--
Corporate and other cost allocations	226	426
Deferred income taxes	(1,032)	1,642
Affiliates' earnings in excess of dividends received	(3,387)	94
Accruals and deferrals of cash receipts and payments:		
Accounts receivable	1,180	(1,611)
Receivable from affiliates, net	412	(5,030)
Transfers from Hercules Group, net	270	1,481
Inventories	148	1,416
Accounts payable and accrued expenses	1,393	(2,263)
Noncurrent assets and liabilities	82	294

Edgar Filing: HERCULES INC - Form 10-K/A

Net cash provided by operating activities	19,475	14,207
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures	(356)	(11,350)
Acquisition of subsidiaries, net of cash acquired	--	(355)
Other, net	95	47
Net cash used in investing activities	(261)	(11,658)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Long-term debt repayments, third parties	(11,279)	(9,726)
Transfers (to)/from Hercules Group, net	(5,953)	6,150
Change in short-term debt	--	(9)
Net cash used in financing activities	(17,232)	(3,585)
Effect of exchange rate changes on cash	(111)	(464)
Net increase (decrease) in cash and cash equivalents	1,871	(1,500)
Cash and cash equivalents at beginning of year	3,629	5,129
Cash and cash equivalents at end of year	\$ 5,500	\$ 3,629
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the year for:		
Interest (net of amount capitalized)	\$ 3,929	\$ 4,727
Income taxes, net	2,728	1,424
Noncash financing activities		
Corporate and other cost allocations	226	426

The accompanying notes are an integral part of the consolidated financial statements.

109

FIBERVISIONS A/S  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

FiberVisions A/S, based in Varde, Denmark, ("FiberVisions A/S" or the "Company") serves worldwide markets for polypropylene fiber used to make disposable hygiene products. The Company is a wholly owned subsidiary of FiberVisions, L.L.C. ("FiberVisions"). Hercules Inc. acquired the 49% share of FiberVisions from their joint venture partner in July 1998, making FiberVisions a wholly owned subsidiary of Hercules, Inc.

Historically, separate company stand-alone financial statements were not prepared for the Company. In November 2000, Hercules amended its senior credit facility and ESOP credit facility (the "Facilities"). The Facilities, as amended, are secured by liens on Hercules' property and assets (and those of Hercules' Canadian Subsidiaries), a pledge of the stock of substantially all of Hercules' domestic subsidiaries (including FiberVisions A/S) and 65% of the stock of foreign subsidiaries directly owned by Hercules, and a pledge of Hercules' domestic intercompany indebtedness. These financial statements present

## Edgar Filing: HERCULES INC - Form 10-K/A

the financial information on the Company, a collateral party to the Hercules debt, based on the Hercules' understanding of Securities and Exchange Commission's interpretation and application of Rule 3-16 under the Securities and Exchange Commission's Regulation S-X. These statements were derived from historical accounting records.

On April 29, 2002, in connection with Hercules' sale of its Water Treatment Business (see Note 20) and the repayment of the Facilities, the stock pledges were released. As a result, based on Hercules' current debt structure, these separate company stand-alone financial statements will not be required for the fiscal year ending December 31, 2002.

The financial statements of the Company reflect certain allocated support costs incurred by other entities in the Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations and charges included in the Company's financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on factors such as sales, net assets, or cost of sales; or a relative weighting of geographic activity. Management believes that the allocation methods are reasonable.

During 1998, Hercules acquired the Company to make this a wholly owned subsidiary. These financial statements include the push-down of fair value adjustments to assets and liabilities, including goodwill, other intangible assets and property, plant, and equipment and their related amortization and depreciation adjustments.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its majority-owned subsidiaries where control exists. Investments in affiliated companies with a greater than 20% and 50% or less ownership interest are accounted for using the equity method of accounting and, accordingly, consolidated income includes the Company's share of their income. All intercompany transactions and profits have been eliminated.

110

#### FIBERVISIONS A/S NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

#### USE OF ESTIMATES

Preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

#### REVENUE RECOGNITION

The Company recognizes revenue when the earnings process is complete. This generally occurs when products are shipped to the customer or services are



## Edgar Filing: HERCULES INC - Form 10-K/A

performed in accordance with the terms of the agreement, title and risk of loss have been transferred, collectibility is probable, and pricing is fixed and determinable. Accruals are made for sales returns and other allowances based on the Company's experience. The corresponding shipping and handling costs are included in cost of sales.

### CASH AND CASH EQUIVALENTS

Cash and cash equivalents include highly liquid investments with original maturities of three months or less. Cash in excess of operating requirements is transferred to Hercules or invested in interest bearing bank accounts.

### INVENTORIES

Inventories are stated at the lower of cost or market using the average cost method.

### PROPERTY AND DEPRECIATION

Property, plant, and equipment are stated at cost. The Company uses the straight-line method of depreciation. The Company believes straight-line depreciation provides a better matching of costs and revenues over the lives of the assets. The estimated useful lives of depreciable assets are as follows: buildings - 30 years; plant, machinery and equipment - 15 years; other machinery and equipment - 3 to 15 years.

Maintenance, repairs, and minor renewals are charged to income; major renewals and betterments are capitalized. Upon normal retirement or replacement, the net book value of property (less proceeds of sale or salvage) is charged to income.

### GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill and other intangible assets are amortized on a straight-line basis over the estimated future periods to be benefited, generally 40 years for goodwill and 10 years for other intangible assets. Goodwill arises in connection with acquisitions. The purchase price is allocated to the fair value of the assets acquired and liabilities assumed with the excess recorded as goodwill.

Pursuant to Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (SFAS 142), beginning January 1, 2002, goodwill will not be amortized but will be tested for impairment annually and any necessary adjustment charged to expense. Intangible assets with finite lives will be amortized over their useful lives.

### IMPAIRMENT OF LONG LIVED ASSETS

The Company reviews its long-lived assets, including goodwill and other intangibles, for impairment on an exception basis whenever events or changes in circumstances indicate carrying amounts of the assets may not be recoverable through undiscounted future cash flows. If an impairment loss has occurred based on expected future cash flows (undiscounted), the loss is recognized in the income statement. The amount of the impairment loss is the excess of the carrying amount of the impaired asset over the fair value of the asset. The fair value represents expected future cash flows from the use of the assets, discounted at the rate used to evaluate potential investments. During 2000, the Company had long-lived asset impairments of \$28,169 thousand (see Note 12).

### FOREIGN CURRENCY TRANSLATION AND TRANSACTIONS

The accompanying consolidated financial statements are reported in U.S. dollars. The Danish kroner is the functional currency for the Company and its

## Edgar Filing: HERCULES INC - Form 10-K/A

domestic subsidiaries and associated companies. However, the U.S. dollar, Chinese renminbi, EURO and the Swiss franc are the functional currencies for its foreign subsidiaries located in the United States, China, Germany and Switzerland, respectively. The translation of the functional currencies into U.S. dollars (reporting currency) is performed for assets and liabilities using the current exchange rates in effect at the balance sheet date, and for revenues, costs and expenses using average exchange rates prevailing during the reporting periods.

111

### FIBERVISIONS A/S NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

Adjustments resulting from the translation of functional currency financial statements to reporting currency are accumulated and reported as other comprehensive income.

Transactions in foreign currency are recorded at the exchange rate prevailing on the date of transaction. Monetary assets and liabilities denominated in foreign currencies are expressed in the functional currency at the exchange rates in effect at the balance sheet date. Revenues, costs and expenses are recorded using average exchange rates prevailing during the reporting periods. Gains or losses resulting from foreign currency transactions are included in the statement of operations.

#### CONCENTRATIONS OF CREDIT RISK

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of trade receivables. Concentrations of credit risk with respect to trade receivables are limited due to insurance coverage for customers of the Company. As of December 31, 2001 and 2000, the Company's accounts include cash, bank borrowings, trade receivables and accounts payable which are denominated in currencies other than the U.S. Dollar. Wherever possible the Group attempts to limit the exchange rate exposure by matching the receivables, borrowings and payables in the same currency. Operating results, however, are affected by significant fluctuations in exchange rates. Financial instruments, which potentially subject the group to a concentration of credit risk principally, consist of trade receivables. Approximately 82% and 87% of trade receivables were concentrated with 10 customers as of December 31, 2001 and 2000, respectively. There was one customer that accounted for 16% and 21% of total trade receivables as of December 31, 2001 and 2000.

The Company has deposited its cash and cash equivalents with reputable financial institutions and believes the risk of loss due to non-performance by the counter party to be remote.

#### STOCK-BASED COMPENSATION

Compensation costs attributable to stock options and similar plans are recognized based on any excess of the quoted market price of the stock on the date of grant over the amount the employee is required to pay to acquire the stock (the intrinsic-value method under Accounting Principles Board Opinion 25 (APB 25)). Such amount, if any, is accrued over the related vesting period, as appropriate. Statement of Financial Accounting Standard No. 123, "Accounting for Stock-based Compensation," requires companies electing to continue to use the intrinsic-value method to make pro forma disclosures of net income as if the fair-value-based method of accounting had been applied.

## Edgar Filing: HERCULES INC - Form 10-K/A

### NET HERCULES GROUP INVESTMENT

The net Hercules Group investment account reflects the balance of the Company's historical earnings, foreign currency translation, intercompany amounts, income tax, and other transactions between the Company and the Hercules Group.

### INCOME TAXES

The provisions for income taxes has been determined using the asset and liability approach of accounting for income taxes. Under this approach, deferred taxes represent the future tax consequences expected to occur when the reported amounts of assets and liabilities are recovered or paid. The provision for income taxes represents income taxes paid or payable for the current year plus the change in deferred taxes during the year. Deferred taxes result from differences between the financial and tax basis of the Company's assets and liabilities and are adjusted for changes in tax rates and tax laws when changes are enacted. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized.

The Company provides taxes on undistributed earnings of subsidiaries and affiliates included in consolidated retained earnings to the extent such earnings are planned to be remitted and not re-invested permanently. The undistributed earnings of subsidiaries and affiliates on which no provision for foreign withholding or US income taxes has been made amounted to approximately \$63,270 thousand, \$62,410 thousand, and \$61,343 thousand at December 31 2001, 2000, and 1999, respectively. US and foreign income taxes that would be payable if such earnings were distributed may be lower than the amount computed at the US statutory rate because of the availability of tax credits.

### NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 141, "Business Combinations" ("SFAS 141"), and Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"). SFAS 141 supersedes Accounting Principles Board Opinion ("APB") No. 16, Business Combinations. The provisions of SFAS 141 (1) require that the purchase method of

112

### FIBERVISIONS A/S

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

accounting be used for all business combinations initiated after June 30, 2001, (2) provide specific criteria for the initial recognition and measurement of intangible assets apart from goodwill and (3) require that unamortized negative goodwill be written off immediately as extraordinary gain instead of being deferred and amortized. SFAS 141 also requires that upon adoption of SFAS 142 the Company reclassify the carrying amounts of certain intangible assets into or out of goodwill, based on certain criteria. SFAS 142 supersedes APB No. 17, Intangible Assets, and is effective for fiscal years beginning after December 15, 2001. SFAS 142 primarily addresses the accounting for goodwill and intangible assets subsequent to their initial recognition. The provisions of SFAS 142 (1) prohibit the amortization of goodwill and indefinite-lived intangible assets, (2) require that goodwill and indefinite-lived intangible assets be tested annually for impairment (and in interim periods if certain events occur indicating that the carrying value of goodwill and/or indefinite-lived intangible assets may be impaired), based on fair value (as opposed to cost recovery using future undiscounted cash flows), (3) require that reporting units be identified for the purpose of assessing potential future

## Edgar Filing: HERCULES INC - Form 10-K/A

impairments of goodwill and (4) remove the forty-year limitation on the amortization period of intangible assets that have finite lives.

Effective January 1, 2002 Hercules adopted the provisions of SFAS 142 and determined that FiberVisions consists of one reporting unit. In the first quarter 2002, Hercules completed its transitional impairment review and determined that FiberVisions' recorded goodwill was impaired. Accordingly, at March 31, 2002 FiberVisions recognized an after tax impairment loss of \$87 million as a cumulative effect of a change in accounting principle. As a result of Hercules adoption of SFAS 142, the Company will no longer record \$2.6 million of annual amortization relating to existing goodwill and intangibles.

Goodwill was evaluated for impairment at December 31, 2001 under Statement of Financial Accounting Standards No. 121 "Accounting for the Impairment of Long-lived Assets and for Long-Lived Assets to Be Disposed of." Such evaluations indicated that goodwill associated with the business was recoverable from anticipated future undiscounted cash flows. Accordingly, no impairment loss was recorded in the December 31, 2001 financial statements.

In June 2001, the Financial Accounting Standards Board ("FASB") approved the issuance of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143"). SFAS 143 establishes accounting standards for the recognition and measurement of legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 will become effective for the Company on January 1, 2003 and requires recognition of a liability for an asset retirement obligation in the period in which it is incurred. The Company does not believe this statement will have a material effect on its financial statements.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company does not believe this statement will have a material effect on its financial statements.

In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment to FASB Statement No. 13, and Technical Corrections." The Company has elected to early adopt the provisions of SFAS 145 related to the rescission of SFAS 4, "Reporting Gains and Losses from the Extinguishment of Debt" ("SFAS 4"). The early adoption had no effect on the Company's financial statements.

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146"). SFAS 146 addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs in a Restructuring)". SFAS 146 defines the timing of the recognition of costs associated with exit or disposal activities, the types of costs that may be recognized and the methodology for calculating the fair value of such costs. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. The Company does not believe this statement will have a material effect on its financial statements.

## Edgar Filing: HERCULES INC - Form 10-K/A

### 3. ACCOUNTS RECEIVABLE, NET

Accounts receivable, net, consists of:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Trade	\$ 12,940	\$ 15,220
Rebates from suppliers	3,224	2,820
Other	551	1,260
	-----	-----
	16,715	19,300
Less allowance for doubtful accounts	(263)	(361)
	-----	-----
Total	\$ 16,452	\$ 18,939
	=====	=====

### 4. INVENTORIES

The components of inventories are:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Finished products	\$2,330	\$2,647
Materials, supplies, and work in process	3,499	3,496
	-----	-----
Total	\$5,829	\$6,143
	=====	=====

### 5. RECEIVABLES FROM AFFILIATES

Trade receivables from affiliates, consists of \$4,462 thousand and \$5,030 thousand due from ES FiberVisions for years then ended December 31, 2001 and 2000, respectively, and net of \$1,940 and \$2,215 of accumulated losses of unconsolidated companies in excess of investment for years 2001 and 2000, respectively (see Note 6).

### 6. INVESTMENTS IN AFFILIATED COMPANIES

The equity investments in affiliated companies consist of:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Investment in FiberVisions, LP	\$ 21,215	\$18,140
	=====	=====

## Edgar Filing: HERCULES INC - Form 10-K/A

On January 1, 2000 the Company and Chisso Polypro Fiber Co., Ltd formed a 50/50 joint venture, ES FiberVisions, combining their bicomponent fibers businesses outside of Japan. While the Company has a 50% equity interest, it's share of joint venture operations is 67%. The venture extends the Company's strategy to continue globalization of bicomponent fiber by establishing sales support facilities in key regions. Both parent companies supply fiber to the joint venture under manufacturing agreements. The Company manufactures bicomponent fibers for the joint venture at the Varde, Denmark and Athens, Georgia locations. The annual sales of the venture were approximately \$55 million and \$48 million in fiscal 2001 and 2000, respectively. The Company's share of net income was \$1,319 thousand and \$153 thousand in 2001 and 2000, respectively.

In 1998, the Company's majority owned subsidiary FiberVisions Products, Inc. entered into a 50% joint venture with FiberVisions Inc., a wholly owned subsidiary of FiberVisions. FiberVisions Products Inc. and FiberVisions Inc. manufacture products for the joint venture, FiberVisions LP, under a manufacturing agreement. FiberVisions Products' share of the net income was \$3,090 thousand, \$2,464 thousand and \$12,716 thousand in 2001, 2000 and 1999, respectively.

Summarized financial information for the equity affiliates at December 31, and the years then ended is as follows:

114

FIBERVISIONS A/S  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

	(Dollars in thousands)		
	2001	2000	
	-----	-----	
Current assets	\$ 32,002	\$ 38,614	
Non Current assets	22,706	9,925	
Current liabilities	9,389	10,803	
Non Current liabilities	94	--	
	2001	2000	1999
	-----	-----	-----
Net sales	\$169,478	\$197,417	\$150,450
Gross profit	15,414	13,418	27,730
Net earnings	8,149	5,150	25,432

The majority of the investments are partnerships which require the associated tax benefit or tax expense to be recorded by the parent.

7. LONG-TERM DEBT

Long-term at December 31, 2001 and 2000 is summarized as follows:

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars)	
	2001	
	Book Value	Market Value
Revolving credit facility due in varying amounts through 2005 with an average interest rate of 4.15%	\$ 18,533	\$ 18,533
Finansierings Instituttet for Industri og Handvoerk A/S (FIH) term notes at various rates from 6.94% to 9.60% and due in varying amounts through 2006	10,455	10,610
Danmark Finansiering Institut A/S (DFI) term notes at various rates from 6.48% to 8.56% and due in varying amounts through 2006	18,704	19,266
Mortgage at a fixed rate of 7.16% and due in varying amounts through 2014	4,079	4,304
Industrialization Fund for Developing Countries (IFU) at a fixed rate of 5.23% and due in 2001	--	--
Lease purchase obligation	250	250
	-----	-----
	52,021	52,963
Less current maturities	(7,532)	(7,765)
	-----	-----
Total	\$ 44,489	\$ 45,198
	=====	=====

As of December 31, 2001 FIH term notes are collateralized by land, buildings, and plant and machinery of approximately \$27,598 thousand. The DFI loan is collateralized by a letter of indemnification regarding land, buildings and plant and machinery of approximately \$17,843 thousand. The mortgage is collateralized by land and buildings of approximately \$4,079 thousand.

In December 1996 the Company entered into a long-term lease purchase obligation with The Athens-Clark County Industrial Development Authority to purchase land. The interest rate is fixed at 1% per annum and the due date of the obligation is December 2020. The balance of the obligation was \$250 thousand at December 31, 2001 and 2000.

115

FIBERVISIONS A/S  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Scheduled annual maturities of long-term debt outstanding at December 31, 2001 in the successive five-year period are summarized as follows:

	(Dollars in thousands)
2002	\$ 7,532
2003	12,270
2004	12,243
2005	12,692
2006	4,222
Thereafter	3,062
	-----

Edgar Filing: HERCULES INC - Form 10-K/A

Total \$52,021  
=====

8. ADDITIONAL BALANCE SHEET DETAIL

	(Dollars in thousands)	
	2001	2000
	-----	-----
Property, plant, and equipment		
Land	\$ 619	\$ 628
Buildings and equipment	187,338	191,940
Construction in progress	4,952	4,979
	-----	-----
Total	192,909	197,547
Accumulated depreciation and amortization	(108,427)	(102,517)
	-----	-----
Net property, plant, and equipment	\$ 84,482	\$ 95,030
	=====	=====
Accrued expenses		
Payroll and employee benefits	\$ 2,069	\$ 2,168
Accrued interest payable	275	365
Current taxes payable	2,897	--
Miscellaneous	5,810	4,052
	-----	-----
	\$ 11,051	\$ 6,585
	=====	=====

9. GOODWILL AND OTHER INTANGIBLE ASSETS

At December 31, 2001 and 2000, the goodwill and other intangible assets were:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Goodwill from Hercules acquisition	\$ 104,411	\$ 104,411
Other intangibles	1,467	1,598
	-----	-----
Total	105,878	106,009
Less accumulated amortization	(10,571)	(7,951)
	-----	-----
Net goodwill and other intangible assets	\$ 95,307	\$ 98,058
	=====	=====

In July 1998, Hercules completed the acquisition of 49% share of FiberVisions L.L.C. owned by its joint venture partner, Jacob Holm & Son A/S, for approximately \$230 million in cash, plus assumed debt of \$188 million. The allocation of the purchase price resulted in \$188,051 thousand of goodwill for the FiberVisions group, which is being amortized over its estimated useful life



## Edgar Filing: HERCULES INC - Form 10-K/A

of 40 years. Goodwill of \$104,411 thousand was assigned to the Company.

116

FIBERVISIONS A/S  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

10. OTHER FINANCING ARRANGEMENTS

Hercules manages the Company's cash and indebtedness. The majority of the cash provided by or used by the Company is provided through this consolidated cash and debt management system. As a result, the amount of domestic cash or debt historically related to the Company is not determinable. For the purposes of the Company's historical financial statements all of its positive or negative cash flows have been treated as cash transferred to or from its parent.

The Company has an intercompany receivable with the Hercules Group in the amount of \$18,921 thousand and \$16,258 thousand which is included in the net Hercules Group investment balance at December 31, 2001 and 2000, respectively. At December 31, 2001 and 2000 the weighted average interest rate on the intercompany borrowings was 7.6% and 7.4%, respectively.

11. INTEREST EXPENSE, NET

Interest and debt costs are summarized as follows:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Interest expense	\$ 2,737	\$ 2,383	\$ 5,667
Amount capitalized	(13)	(132)	(11)
	-----	-----	-----
Amount expensed	2,724	2,251	5,656
Interest income	(27)	(17)	(901)
	-----	-----	-----
Interest expense, net	\$ 2,697	\$ 2,234	\$ 4,755
	=====	=====	=====

12. IMPAIRMENT OF LONG LIVED ASSETS

In the third quarter of 2000, the Company recorded assets impairments of \$28,169 thousand. Management determined that revised growth projections for the China hygiene non-woven market would indefinitely delay the feasibility of expanding the production capability of the facility. Estimated future cash flows related to this facility without the planned expansion indicated that an impairment had occurred. The impairment charge was required to write off approximately 90% of the net book value of the existing Suzhou, China facility as well as the investment in the new fiber line.

13. OTHER OPERATING EXPENSES, NET

Other operating expenses, net, consists of the following:

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Goodwill amortization	\$ 2,644	\$ 2,644	\$ 2,660
Foreign currency transactions expense (income)	8	106	(327)
Miscellaneous (income) expense, net	332	(5)	17
	-----	-----	-----
	\$ 2,984	\$ 2,745	\$ 2,350
	=====	=====	=====

14. INCOME TAXES

The domestic and foreign components of income before taxes and effect of change in accounting principle are presented below:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Domestic	\$ 1,515	\$ 98	\$ 9,845
Foreign	12,617	(20,045)	11,165
	-----	-----	-----
	\$14,132	\$ (19,947)	\$21,010
	=====	=====	=====

A summary of the components of the tax provision follows:

117

FIBERVISIONS A/S  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Currently payable			
Domestic	\$ --	\$ (438)	\$ (169)
Foreign	6,350	2,225	3,042
Deferred			
Domestic	944	1,009	4,218
Foreign	(1,976)	634	964
	-----	-----	-----
Provision for income taxes	\$ 5,318	\$ 3,430	\$ 8,055
	=====	=====	=====

## Edgar Filing: HERCULES INC - Form 10-K/A

Deferred tax liabilities (assets) at December 31 consist of:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Depreciation	\$ 15,079	\$ 20,091
Accrued expenses	--	1,093
Other	9,881	--
	-----	-----
Gross deferred tax liabilities	24,960	21,184
	-----	-----
Amortization	\$ --	\$ (1,345)
Inventory	--	(108)
Impairment of assets	(3,704)	(3,704)
Loss carryforwards	(6,293)	(5,273)
Other comprehensive income	--	1,005
Other	--	(691)
	-----	-----
Gross deferred tax assets	(9,997)	(10,116)
	-----	-----
Valuation allowance	7,668	7,669
	-----	-----
Total deferred income tax	\$ 22,631	\$ 18,737
	=====	=====

A reconciliation of the statutory income tax rate to the effective rate follows:

	2001	2000	1999
	-----	-----	-----
Statutory income tax rate	35.00%	35.00%	35.00%
Foreign Rate Differential	(4.00)	(24.87)	1.80
Valuation Allowance	0.42	(28.78)	--
Reserves	--	(1.91)	(1.45)
Goodwill	6.00	(3.15)	2.59
Other	0.01	6.52	0.40
State tax	0.19	--	--
	-----	-----	-----
Effective tax rate	37.62%	(17.19)%	38.34%
	=====	=====	=====

118

FIBERVISIONS A/S  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

15. NET HERCULES GROUP INVESTMENT

## Edgar Filing: HERCULES INC - Form 10-K/A

Changes in net Hercules Group Investment were as follows:

	(Dollars in thousands)
	-----
Balance at January 1, 1999	\$ 136,196
Comprehensive income for the year ended December 31, 1999	13,852
Intercompany transactions, net	3,169
	-----
Balance at January 1, 2000	153,217
Comprehensive income for the year ended December 31, 2000	(22,078)
Intercompany transactions, net	8,057
	-----
Balance at December 31, 2000	139,196
Comprehensive income for the year ended December 31, 2001	10,088
Intercompany transactions, net	(12,265)
	-----
Balance at December 31, 2001	\$ 137,019
	=====

The Company includes accumulated other comprehensive income in net parent investment. At December 31, 2001, 2000, and 1999 accumulated other comprehensive income included \$3,625 thousand, \$2,351 thousand, and \$1,052 thousand, respectively, of foreign currency translation adjustments.

### 16. COMMITMENTS AND CONTINGENCIES

#### Leases

FiberVisions A/S has operating leases (including office space, transportation, and data processing equipment) expiring at various dates. Rental expense was \$78 thousand, \$34 thousand, and \$50 thousand in 2001, 2000, and 1999, respectively.

The net minimum future payments at December 31, 2001 are as follows:

	(Dollars in thousands)
2002	\$ 87
2003	69
2004	33
2005	8
2006	8
	-----
Total	\$205
	=====

The Danish tax authorities have increased FiberVisions A/S' taxable income for the tax year 1997. The tax value of the declared increase amounts to approximately \$1,400 thousand. Management does not agree with the assessment of the tax authorities, and the case has been appealed. Consequently, the final outcome of the case is uncertain.

The Company currently and from time to time is involved in litigation incidental to the conduct of its business. In the opinion of the Company's

## Edgar Filing: HERCULES INC - Form 10-K/A

management, none of such litigation as of December 31, 2001 is likely to have a material adverse effect on the financial position, results of operations, or cash flows of the Company.

### 17. PENSION AND POSTRETIREMENT BENEFITS

FiberVisions Products, Inc. participates in a defined benefit pension plan sponsored by Hercules, which covers substantially all employees of Hercules in the U.S. Benefits under this plan are based on the average final pay and years of service. Hercules also provides postretirement health care and life insurance benefits to eligible retired employees and their dependents.

Information on the actuarial present value of the benefit obligation and fair value of the plan assets is not presented as Hercules manages its U.S. employee benefit plans on a consolidated basis and such information is not maintained separately for the U.S. employees of the Company. The Company's statement of operation includes an

119

### FIBERVISIONS A/S NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

allocation of the costs of the U.S. benefits plans. The pension costs were allocated based on percentage of pensionable wages, for each of the years presented, postretirement benefit costs were allocated using factors derived from the relative net assets and revenues. Net pension expense (income) of Hercules allocated to FiberVisions Products, Inc. was (\$112) thousand and (\$129) thousand for the year ended December 31, 2001 and 2000, respectively. There was no allocation in 1999.

FiberVisions A/S maintains a contributory pension plan. The Company's matching contribution was \$940 thousand, \$964 thousand and \$977 thousand for 2001, 2000 and 1999, respectively. FiberVisions Products, Inc. maintains a 401(k) savings plan for its full-time employees in North America. Each participant in the plan may elect to contribute 1 % to 15 % of his or her annual salary to the plan subject to statutory limitations. The company matches employee contributions to the plan at the rate of 50% of the first 6% of salary contributed. The Company's matching contribution was \$59 thousand, \$69 thousand and \$79 thousand for 2001, 2000 and 1999, respectively. FiberVisions (China) Textiles Products, Ltd. provides a housing allowance for their employees. The Company's contribution was \$141 thousand, \$160 thousand, and \$137 thousand in 2001, 2000 and 1999, respectively.

### 18. LONG TERM INCENTIVE COMPENSATION PLAN

The Company participates in long-term incentive compensation plans sponsored by Hercules. These plans provide for the grant of stock options and the award of common stock and other market-based units to certain key employees and non-employee directors.

In 1995, Hercules changed the structure of the long-term incentive compensation plans to place a greater emphasis on shareholder value creation through grants of regular stock options, performance-accelerated stock options, and Cash Value Awards (performance-based awards denominated in cash and payable in shares of common or restricted stock, subject to the same restrictions as restricted stock). Restricted stock and other market-based units are awarded with respect to certain programs. The number of awarded shares outstanding was 189,704 at December 31, 2001, and 491,489 and 926,689 at December 31, 2000 and 1999, respectively.

## Edgar Filing: HERCULES INC - Form 10-K/A

At December 31, 2001, under Hercules' incentive compensation plans, 1,265,493 shares of common stock were available for grant as stock awards or stock option awards. Stock awards are limited to approximately 15% of the total authorizations. Regular stock options are granted at the market price on the date of grant and are exercisable at various periods from one to five years after date of grant. Performance-accelerated stock options are also granted at the market price on the date of grant and are normally exercisable at nine and one-half years. Exercisability may be accelerated based upon the achievement of predetermined performance goals. Both regular and performance-accelerated stock options expire 10 years after the date of grant.

Restricted shares, options and performance-accelerated stock options are forfeited and revert to Hercules in the event of employment termination, except in the case of death, disability, retirement, or other specified events.

The Company applies APB Opinion 25 in accounting for its plans. Accordingly, no compensation cost has been recognized for the stock option plans. There were no charges to income for the cost of stock awards over the restriction or performance period for 2001, 2000 and 1999, respectively.

Below is a summary of outstanding stock option grants under the incentive compensation plans during 1999, 2000 and 2001:

	Regular	
	Number of Shares	Weighted-average price
	-----	-----
December 31, 1999	--	--
Granted	6,875	\$17.25
Exercised	--	--
Forfeited	--	--
	-----	-----
December 31, 2000	6,875	\$17.25
Granted	6,875	\$11.28
Exercised	--	--
Forfeited	--	--
	-----	-----
December 31, 2001	13,750	\$14.27

There were no performance-accelerated stock options granted or outstanding during 1999, 2000 and 2001, and no regular stock options granted or outstanding during 1999. The weighted-average fair value of regular stock options granted during 2000 and 2001 was \$8.85 and \$5.69.

120

FIBERVISIONS A/S  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

-----

Following is a summary of regular stock options exercisable at December 31, 1999, 2000 and 2001, and their respective weighted-average exercise share price.

Edgar Filing: HERCULES INC - Form 10-K/A

Options Exercisable	Number of Shares	Weighted-average exercise price
December 31, 2001	2,750	\$11.28

Following is a summary of stock options outstanding at December 31, 2001:

Exercise Price Range	Outstanding Options		
	Number Outstanding at 12/31/2001	Weighted-average Remaining Contractual Life	Weighted-average exercise price
Regular Stock Options \$11 - \$20	13,750	8.89	\$14.27
	13,750		

The Company's employees may also participate in the Hercules Employee Stock Purchase Plan ("ESSP"). The ESSP is a qualified non-compensatory plan, which allows eligible employees to acquire shares of common stock through systematic payroll deductions. The plan consists of three-month subscription periods, beginning July 1 of each year. The purchase price is 85% of the fair market value of the common stock on either the first or last day of that subscription period, whichever is lower. Purchases may range from 2% to 15% of an employee's base salary each pay period, subject to certain limitations. Currently, there are no shares of Hercules common stock registered for offer and sale under the plan. Shares issued at December 31, 2001 and 2000, were 1,758,081 and 1,597,861, respectively. The Company applies APB Opinion 25 and related interpretations in accounting for its Employee Stock Purchase Plan. Accordingly, no compensation cost has been recognized for the Employee Stock Purchase Plan.

Had compensation cost for Hercules' Stock-Based Incentive Plans and Employee Stock Purchase Plan been determined on the basis of fair value according to SFAS No. 123, the fair value of each option granted or share purchased would be estimated on the grant date using the Black-Scholes option pricing model.

The following weighted-average assumptions would be used in estimating fair value for 2001, 2000 and 1999:

Assumption	Regular Plan	Performance Accelerated Plan	Employee Stock Purchase Plan
Dividend yield	0.96%	3.83%	0.0%
Risk-free interest rate	5.80%	5.57%	4.86%
Expected life	7.1 yrs.	5 yrs.	3 mos.
Expected volatility	33.36%	29.78%	49.11%

## Edgar Filing: HERCULES INC - Form 10-K/A

The Company's net income and earnings per share for 2001, 2000 and 1999 would approximate the pro forma amounts below:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Net income (loss)			
As reported	\$8,814	\$(23,377)	\$12,955
Pro forma	\$8,849	\$(23,402)	\$12,955

### 19. RELATED PARTY TRANSACTIONS

The Company has entered into certain agreements with affiliated entities. These agreements were developed in the context of parent/subsidiary relationship and therefore may not necessarily reflect the result of arm-length negotiations between independent parties. The terms of the agreements provide for the sale of product to the affiliated entities based on a cost-plus formula.

#### CORPORATE AND OTHER ALLOCATIONS

As discussed in Note 1, the financial statements of the Company reflect certain allocated support costs incurred by other entities in Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, safety, information management, health and environmental, investor relations and other corporate services. Allocations and charges included in the Company's financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities, or a percentage allocation for such services provided based on factors such as revenues, net assets, cost of sales and relative weighting of geographic activity. These allocations are reflected in the selling, general and administrative line item in our statements of operations. In addition, the Company allocates certain of its own costs to other companies in the FiberVision group of companies. Such allocations and corporate charges totaled \$226 thousand, \$426 thousand and \$1,747 thousand in 2001, 2000 and 1999, respectively.

#### SALES TO AFFILIATES

The Company sells fiber in the normal course of business to affiliated companies. The Company's revenues from sales to affiliated companies were \$43,243 thousand, \$49,885 thousand, and \$30,919 thousand in 2001, 2000, and 1999, respectively.

#### PURCHASES FROM HERCULES GROUP

The Company also purchases finished product for resale in the normal course of business from the Hercules Group. The Company's purchases from the Hercules Group were \$30 thousand, \$3,874 thousand, and \$9,994 thousand in 2001, 2000, and 1999, respectively. In addition, supplies are purchased in the normal course of business from the Hercules Group. The Company's purchases from Hercules Group were \$9 thousand, \$7 thousand, and \$8 thousand in 2001, 2000, and 1999, respectively.

### 20. SUBSEQUENT EVENTS

On April 29, 2002, Hercules completed the sale of its Water Treatment Business to GE Specialty Materials (GESM). Pursuant to the Stock and Asset



## Edgar Filing: HERCULES INC - Form 10-K/A

Agreement for the transaction, the sale included all of the stock of BetzDearborn Inc. Hercules used the proceeds from the sale to prepay borrowings under its Senior Credit Facility and ESOP Credit Facility. Pursuant to the prepayment, among other things, the stock pledges were released.

121

### REPORT OF INDEPENDENT ACCOUNTANTS

TO THE SHAREHOLDERS AND THE BOARD OF DIRECTORS OF

HERCULES INCORPORATED  
WILMINGTON, DELAWARE

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations and of cash flows present fairly, in all material respects, the financial position of FiberVisions, Inc., a subsidiary of Hercules Incorporated, and its subsidiaries at December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America that require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP  
Philadelphia, Pennsylvania

November 7, 2002

122

FIBERVISIONS INC.  
CONSOLIDATED STATEMENTS OF OPERATIONS

	(Dollars in thousands)		
	Year ended December 31,		
	2001	2000	1999
	-----	-----	-----
Sales to Hercules Group	\$ 82,101	\$ 105,724	\$ 92,35
Cost of sales	71,285	99,026	82,85
Selling, general, and administrative expenses	3,717	3,570	4,64
Research and development	2,772	3,458	3,39
Impairment of long lived assets (Note 9)	--	25,372	--
Goodwill and intangible amortization	\$ 4,704	\$ 4,698	\$ 4,74
Miscellaneous (income) expense, net	1,023	(247)	(
	-----	-----	-----
Loss from operations	(1,400)	(30,153)	(3,28
Equity in income of affiliated companies (Note 4)	3,090	2,463	12,71
Interest expense, net (Note 8)	4,221	5,209	3,79

Edgar Filing: HERCULES INC - Form 10-K/A

(Loss) income before income taxes	(2,531)	(32,899)	5,64
(Benefit) provision for income taxes (Note 10)	792	(9,808)	2,74
Net (loss) income	\$ (3,323)	\$ (23,091)	\$ 2,90

The accompanying notes are an integral part of the consolidated financial statements.

123

FIBERVISIONS INC.  
CONSOLIDATED BALANCE SHEET

	(Dollars in thousands)	
	December 31,	
	2001	2000
	-----	-----
ASSETS		
Current assets		
Cash and cash equivalents	\$ 4,803	\$ 1,148
Miscellaneous receivables	234	174
Inventories (Note 3)	9,022	11,850
	-----	-----
Total current assets	14,059	13,172
	-----	-----
Property, plant, and equipment, net (Notes 5 and 9)	24,667	26,936
Investment in affiliates (Note 4)	21,215	18,140
Goodwill and other intangible assets, net (Note 6)	96,934	101,638
Deferred charges and other assets	126	224
	-----	-----
Total assets	\$157,001	\$160,110
	=====	=====
LIABILITIES AND NET HERCULES GROUP INVESTMENT		
Current liabilities		
Accounts payable	\$ 6,724	\$ 8,478
Payables to affiliates (Note 7)	649	104
Accrued expenses (Note 5)	6,362	6,202
	-----	-----
Total current liabilities	13,735	14,784
Deferred income taxes (Note 10)	1,685	1,368
	-----	-----
Total liabilities	15,420	16,152
Commitments and contingencies (Note 12)	--	--
Net Hercules Group investment (Note 16)	141,581	143,958
	-----	-----
Total liabilities and net Hercules Group investment	\$157,001	\$160,110
	=====	=====

The accompanying notes are an integral part of the consolidated financial statements.

124

## Edgar Filing: HERCULES INC - Form 10-K/A

FIBERVISIONS INC.  
CONSOLIDATED STATEMENT OF CASH FLOWS

	(Dollars in thousands)		
	Year ended December 31,		
	2001	2000	1999
	-----	-----	-----
<b>CASH FLOW FROM OPERATING ACTIVITIES:</b>			
Net (loss) income	\$(3,323)	\$(23,091)	\$
Adjustments to reconcile net income to net cash provided from operations:			
Depreciation	2,522	5,604	
Impairment of long lived assets	--	25,372	
Amortization of goodwill and other intangible assets	4,704	4,698	
Loss on disposal of fixed assets	--	--	
Corporate and other cost allocations	650	(1,444)	
Deferred income taxes	318	(11,181)	
Goodwill adjustment	--	--	
Affiliates' earning in excess of dividends received	(3,075)	(2,463)	
Accruals and deferrals of cash receipts and payments:			
Miscellaneous receivable	(60)	1,405	
Inventories	2,828	2,616	
Transfers from Hercules Group	940	2,096	
Accounts payable and accrued expenses	(1,594)	(821)	
Payables to affiliates	545	104	
Noncurrent assets and liabilities	98	855	
	-----	-----	-----
Net cash provided by operations	4,553	3,750	
	-----	-----	-----
<b>CASH FLOW FROM INVESTING ACTIVITIES:</b>			
Capital expenditures	(253)	(1,779)	
	-----	-----	-----
Net cash used in investing activities	(253)	(1,779)	
	-----	-----	-----
<b>CASH FLOW FROM FINANCING ACTIVITIES:</b>			
Transfers to Hercules Group	(645)	(849)	
	-----	-----	-----
Net cash used in financing activities	(645)	(849)	
	-----	-----	-----
Net increase (decrease) in cash and cash equivalents	3,655	1,122	
Cash and cash equivalents at beginning of year	1,148	26	
	-----	-----	-----
Cash and cash equivalents at end of year	\$ 4,803	\$ 1,148	\$
	=====	=====	=====
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>			
Cash paid during the year for:			
Income taxes paid, net	\$ --	\$ 300	\$
Interest paid	1,878	2,253	
Noncash financing activities			
Corporate and other cost allocations	650	(1,444)	

The accompanying notes are an integral part of the consolidated financial statements.

FIBERVISIONS INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. DESCRIPTION OF BUSINESS

FiberVisions Inc. (the "Company") serves worldwide markets for polypropylene nonwoven fiber used to make disposable hygiene products. FiberVisions Inc. also produces olefin fiber and yarn for domestic textile and industrial markets for use in fabrics, residential upholstery, geotextiles, carpets and asphalt. The Company was formed on May 30, 1997 and is a wholly owned subsidiary of FiberVisions, L.L.C. ("FiberVisions"); itself a wholly owned subsidiary of Hercules Incorporated ("Hercules").

Historically, separate company stand-alone financial statements were not prepared for the Company. In November 2000, Hercules amended its senior credit facility and ESOP credit facility (the "Facilities"). The Facilities, as amended, are secured by liens on Hercules' property and assets (and those of Hercules' Canadian Subsidiaries), a pledge of the stock of substantially all of Hercules' domestic subsidiaries (including FiberVisions Inc.) and 65% of the stock of foreign subsidiaries directly owned by Hercules, and a pledge of Hercules' domestic intercompany indebtedness. These financial statements present the financial information on the Company, a collateral party to the Hercules debt, based on the Hercules' understanding of Securities and Exchange Commission's interpretation and application of Rule 3-16 under the Securities and Exchange Commission's Regulation S-X. These statements were derived from historical accounting records.

On April 29, 2002, in connection with Hercules' sale of its Water Treatment Business (see Note 17) and the repayment of the Facilities, the stock pledges were released. As a result, based on Hercules' current debt structure, these separate company stand-alone financial statements will not be required for the fiscal year ending December 31, 2002.

The Company participates in Hercules' centralized cash management system. Accordingly, cash received from the Company's operations is transferred to Hercules on a periodic basis, and Hercules funds all operational and capital requirements.

The financial statements of the Company reflect certain allocated support costs incurred by other entities in the Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations and charges included in the Company's financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on factors such as sales, net assets, or cost of sales; or a relative weighting of geographic activity. Management believes that the allocation methods are reasonable.

During 1998, Hercules acquired FiberVisions, making the Company a wholly owned subsidiary. These financial statements include the push-down of fair value adjustments to assets and liabilities, including goodwill, other intangible assets and property, plant, and equipment and their related amortization and depreciation adjustments.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

PRINCIPLES OF CONSOLIDATION

## Edgar Filing: HERCULES INC - Form 10-K/A

The consolidated financial statements include the accounts of the FiberVisions Inc. and its majority-owned subsidiaries where control exists. Investments in affiliated companies with a greater than 20% and less than 50% ownership interest are accounted for using the equity method of accounting and, accordingly, consolidated income includes FiberVisions Inc. share of their income. All intercompany transactions and profits have been eliminated.

### USE OF ESTIMATES

Preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

### REVENUE RECOGNITION

The Company recognizes revenue when the earnings process is complete. This generally occurs when products are shipped to the customer or services are performed in accordance with the terms of the agreement, title and risk of loss have been transferred, collectibility is probable, and pricing is fixed and determinable. Accruals are made for sales returns and other allowances based on the Company's experience. The corresponding shipping and handling costs are included in cost of sales.

126

### FIBERVISIONS INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### CASH AND CASH EQUIVALENTS

Cash equivalents include commercial paper and other securities with original maturities of 90 days or less. Book value approximates fair value because of the short maturity of those instruments.

#### INVENTORIES

Inventories are stated at the lower of cost or market using the average cost method.

#### PROPERTY AND DEPRECIATION

Property, plant, and equipment are stated at cost. The Company uses the straight-line method of depreciation to depreciate assets over their useful lives. The estimated useful lives of depreciable assets are as follows: buildings - 30 years; plant, machinery and equipment - 15 years; other machinery and equipment - 3 to 15 years.

Maintenance, repairs, and minor renewals are charged to income; major renewals and betterments are capitalized. Upon normal retirement or replacement, the net book value of property (less proceeds of sale or salvage) is charged to income.

#### GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill and other intangible assets are amortized on a straight-line basis over the estimated future periods to be benefited, generally 40 years for goodwill and 10 years for other intangible assets.

## Edgar Filing: HERCULES INC - Form 10-K/A

Pursuant to Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (SFAS 142), beginning January 1, 2002, goodwill will not be amortized but will be tested for impairment annually and any necessary adjustment charged to expense. Intangible assets with finite lives will be amortized over their useful lives.

### LONG-LIVED ASSETS

The Company reviews its long-lived assets, including goodwill and other intangibles, for impairment on an exception basis whenever events or changes in circumstances indicate carrying amounts of the assets may not be recoverable through undiscounted future cash flows. If an impairment loss has occurred based on expected future cash flows (undiscounted), the loss is recognized in the income statement. The amount of the impairment loss is the excess of the carrying amount of the impaired asset over the fair value of the asset. The fair value represents expected future cash flows from the use of the assets, discounted at the rate used to evaluate potential investments. During 2000 the Company had long-lived asset impairments of \$25,372 thousand (see Note 9).

### CONCENTRATIONS OF CREDIT RISK

Financial instruments that potentially subject the Company to concentration of credit risk consist principally of trade receivables with FiberVisions LP.

### STOCK-BASED COMPENSATION

Compensation costs attributable to stock option and similar plans are recognized based on any excess of the quoted market price of the stock on the date of grant over the amount the employee is required to pay to acquire the stock (the intrinsic-value method under Accounting Principles Board Opinion 25 (APB 25)). Such amount, if any, is accrued over the related vesting period, as appropriate. Statement of Financial Accounting Standard No. 123, "Accounting for Stock-based Compensation," requires companies electing to continue to use the intrinsic-value method to make pro forma disclosures of net income as if the fair-value-based method of accounting had been applied.

### NET HERCULES GROUP INVESTMENT

The net Hercules Group investment account reflects the balance of the Company's historical earnings, intercompany amounts, post employment liabilities, and other transactions between the Company and the Hercules Group.

### INCOME TAXES

The provisions for income taxes has been determined using the asset and liability approach of accounting for income taxes. Under this approach, deferred taxes represent the future tax consequences expected to occur when the reported amounts of assets and liabilities are recovered or paid. The provision for income taxes represents income taxes paid or payable for the current year plus the change in deferred taxes during the year. Deferred taxes result from

## Edgar Filing: HERCULES INC - Form 10-K/A

are enacted. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized.

### NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 141, "Business Combinations" ("SFAS 141"), and Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"). SFAS 141 supersedes Accounting Principles Board Opinion ("APB") No. 16, Business Combinations. The provisions of SFAS 141 (1) require that the purchase method of accounting be used for all business combinations initiated after June 30, 2001, (2) provide specific criteria for the initial recognition and measurement of intangible assets apart from goodwill and (3) require that unamortized negative goodwill be written off immediately as extraordinary gain instead of being deferred and amortized. SFAS 141 also requires that upon adoption of SFAS 142 the Company reclassify the carrying amounts of certain intangible assets into or out of goodwill, based on certain criteria. SFAS 142 supersedes APB No. 17, Intangible Assets, and is effective for fiscal years beginning after December 15, 2001. SFAS 142 primarily addresses the accounting for goodwill and intangible assets subsequent to their initial recognition. The provisions of SFAS 142 (1) prohibit the amortization of goodwill and indefinite-lived intangible assets, (2) require that goodwill and indefinite-lived intangible assets be tested annually for impairment (and in interim periods if certain events occur indicating that the carrying value of goodwill and/or indefinite-lived intangible assets maybe impaired), based on fair value (as opposed to cost recovery using future undiscounted cash flows), (3) require that reporting units be identified for the purpose of assessing potential future impairments of goodwill and (4) remove the forty-year limitation on the amortization period of intangible assets that have finite lives.

Effective January 1, 2002 Hercules adopted the provisions of SFAS 142. Hercules identified the following reporting units: BetzDearborn, Pulp and Paper, Aqualon, FiberVisions and Resins. In connection with Hercules' transitional review recorded goodwill was determined to be impaired in the BetzDearborn and FiberVisions reporting units. In the first quarter 2002, Hercules completed its transitional impairment review of the identified reporting units and recognized an after-tax impairment loss of \$368 million as a cumulative effect of a change in accounting principle, of which \$87 million related to the FiberVisions reporting unit. As a result of Hercules' adoption of SFAS 142, the Company will no longer record \$4.7 million of annual amortization relating to existing goodwill and intangibles, as adjusted for the reclassifications just mentioned.

Goodwill was evaluated for impairment at December 31, 2001 under Statement of Financial Accounting Standards No. 121 "Accounting for the Impairment of Long-Fixed Assets and for Long-Lived Assets to Be Disposed of". Such evaluations indicated that goodwill associated with the business was recoverable from anticipated future undiscounted cash flows. Accordingly, no impairment loss was recorded in the December 31, 2001 financial statements.

In June 2001, the Financial Accounting Standards Board ("FASB") approved the issuance of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143"). SFAS 143 establishes accounting standards for the recognition and measurement of legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 will become effective for the Company on January 1, 2003 and requires recognition of a liability for an asset retirement obligation in the period in which it is incurred. The Company does not believe it will have a material effect on its financial statements.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of

## Edgar Filing: HERCULES INC - Form 10-K/A

Long-Lived Assets" ("SFAS 144"). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company does not believe it will have a material effect on its financial statements.

128

### FIBERVISIONS INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment to FASB Statement No. 13, and Technical Corrections." The Company elected to early adopt the provisions of SFAS 145 related to the rescission of SFAS 4, "Reporting Gains and Losses from the Extinguishment of Debt" ("SFAS 4"). The early adoption had no effect on the Company's financial statements.

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146"). SFAS 146 addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs in a Restructuring)". SFAS 146 defines the timing of the recognition of costs associated with exit or disposal activities, the types of costs that may be recognized and the methodology for calculating the fair value of such costs. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. The Company does not believe this statement will have a material effect on its financial statements.

### RECLASSIFICATIONS

Certain amounts in the 2000 and 1999 consolidated financial statements and notes have been reclassified to conform to the 2001 presentation.

129

### FIBERVISIONS INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### 3. INVENTORIES

The components of inventories are:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Finished products	\$2,897	\$ 4,813
Raw materials	6,100	7,013
Work in process	25	24
	-----	-----
Total	\$9,022	\$11,850
	=====	=====



## Edgar Filing: HERCULES INC - Form 10-K/A

### 4. INVESTMENT

In 1998, the Company entered into a 50% joint venture with FiberVisions Products, Inc. Both parties manufacture products for the joint venture, FiberVisions LP, under a manufacturing agreement. FiberVisions Inc.'s share of the net income was \$3,090 thousand, \$2,463 thousand, and \$12,716 thousand in 2001, 2000, and 1999, respectively.

Summarized financial information for the equity affiliate at December 31, and the years then ended is as follows:

	(Dollars in thousands)		
	2001	2000	
	-----	-----	
Current assets	\$21,589	\$27,805	
Non Current assets	20,841	8,475	
			1999
			-----
Net sales	\$114,969	\$149,007	\$150,450
Gross profit	5,526	5,898	27,730
Net earnings	6,180	4,927	25,432

The investment is a partnership which require the associated tax benefit or expense to be recorded by the partners.

130

### FIBERVISIONS INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 5. ADDITIONAL BALANCE SHEET DETAIL

	(Dollars in thousands)	
	2001	2000
	-----	-----
Property, plant, and equipment		
Land	\$ 654	\$ 654
Buildings and equipment	172,977	173,599
Construction in progress	10,579	11,075
	-----	-----
Total	184,210	185,328
Accumulated depreciation and amortization	(159,543)	(158,392)
	-----	-----
Net property, plant, and equipment	\$ 24,667	\$ 26,936
	=====	=====
Accrued expenses		
Income taxes payable	\$ 719	\$ 245
Miscellaneous	5,643	5,957
	-----	-----
	\$ 6,362	\$ 6,202
	=====	=====

Edgar Filing: HERCULES INC - Form 10-K/A

6. GOODWILL AND OTHER INTANGIBLES ASSETS

At December 31, 2001 and 2000, the goodwill and other intangible assets were:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Goodwill	\$ 83,640	\$ 83,640
Other intangible assets	29,752	29,752
Less accumulated amortization	(16,458)	(11,754)
	-----	-----
Net goodwill and other intangible assets	\$ 96,934	\$ 101,638
	=====	=====

In July 1998, Hercules Inc. completed the acquisition of 49% share of FiberVisions L.L.C. owned by its joint venture partner, Jacob Holm & Son A/S, for approximately \$230 million in cash, plus assumed debt of \$188 million. The allocation of the purchase price resulted in \$188,051 thousand of goodwill for the FiberVisions group, which is being amortized over its estimated useful life of 40 years. \$83,640 thousand of the goodwill was assigned to FiberVisions Inc. Other intangibles assets, related to the acquisition, amounted to \$29,752 thousand.

7. PAYABLES TO AFFILIATES

Trade payables to affiliates, consists of \$649 thousand and \$104 thousand due to ES FiberVisions in 2001 and 2000, respectively.

131

FIBERVISIONS INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

8. INTEREST EXPENSE, NET

Interest costs are summarized as follows:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Interest expense	\$4,221	\$5,209	\$ 3,915
Amount capitalized	--	--	(119)
	-----	-----	-----
Interest expense, net	4,221	5,209	3,796
	=====	=====	=====

9. IMPAIRMENT OF LONG LIVED ASSETS

In 2000, an impairment of \$25,372 was recorded to write off the

## Edgar Filing: HERCULES INC - Form 10-K/A

remaining net book value of the textiles plant in Covington, GA. The textiles business fundamentals had been deteriorating during the previous few years. In 2000, the cost for the major raw material, polypropylene, had risen above historical price levels. The combination of the above factors has resulted in an irreversible loss of profitability for the textiles business. Estimated future cash flows related to this facility indicated full impairment had occurred.

### 10. INCOME TAXES

The domestic and foreign components of income before taxes and effect of change in accounting principle are presented below:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Domestic	\$ (2,532)	\$ (32,901)	\$ 5,650
Foreign	--	2	(10)
	-----	-----	-----
	\$ (2,532)	\$ (32,899)	\$ 5,640
	=====	=====	=====

A summary of the components of the tax provision follows:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Current			
Domestic	\$474	\$ 1,373	\$ 3,545
Foreign	--	1	--
Deferred			
Domestic	318	(11,182)	(805)
	-----	-----	-----
(Benefit) provision for income taxes	\$792	\$ (9,808)	\$ 2,740
	=====	=====	=====

132

FIBERVISIONS INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Deferred tax liabilities (assets) at December 31 consist of:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Depreciation	\$ 13,041	\$ 14,105
	-----	-----
Gross deferred tax liabilities	13,041	14,105
	-----	-----

## Edgar Filing: HERCULES INC - Form 10-K/A

Amortization	\$ (531)	\$ (413)
Bad Debts/ Other Accrueds	(1,069)	(791)
Impairment of assets	(8,938)	(8,938)
Inventory	(817)	(2,595)
	-----	-----
Gross deferred tax assets	(11,355)	(12,737)
	-----	-----
Valuation allowance	--	--
	-----	-----
Total deferred income taxes	\$ 1,686	\$ 1,368
	=====	=====

A reconciliation of the statutory income tax rate to the effective rate follows:

	2001	2000	1999
	-----	-----	-----
Statutory income tax rate	35.00%	35.00%	35.00%
State Taxes	(0.87)	0.85	(12.77)
Provision to return true-up		2.32	8.60
Goodwill	(65.02)	(5.00)	12.85
Reserves	--	(3.31)	4.20
Other	(0.40)	(0.04)	0.64
	-----	-----	-----
Effective tax rate	(31.29)	29.81%	48.53%
	=====	=====	=====

### 11. LONG TERM DEBT AND OTHER FINANCING ARRANGEMENTS

Hercules manages the Company's cash and indebtedness. The majority of the cash provided by or used by the Company is provided through this consolidated cash and debt management system. As a result, the amount of domestic cash or debt historically related to the Company is not determinable. For the purposes of the Company's historical financial statements all of its positive or negative cash flows have been treated as cash transferred to or from its parent.

The Company has intercompany loans with Hercules Group in the amount of \$61,467 thousand and \$61,532 thousand which is included in the net Hercules Group investment balance at December 31, 2001 and 2000, respectively. The weighted average rate on long term intercompany borrowing was 7.6%, 7.4%, and 6.4% as of December 31, 2001, 2000, and 1999, respectively. Interest expense was \$4,221 thousand, \$5,209 thousand, and \$3,606 thousand in 2001, 2000, and 1999, respectively. Repayment terms of the loan are included as part of the Hercules cash management system as described in the previous paragraph.

### 12. COMMITMENTS AND CONTINGENCIES

The Company has operating leases (including office space, storage space, and data processing equipment) expiring at various dates. Rental expense was \$359 thousand, \$540 thousand, and \$434 thousand in 2001, 2000, and 1999, respectively.

The net minimum future payments at December 31, 2001 are as follows:

## Edgar Filing: HERCULES INC - Form 10-K/A

FIBERVISIONS INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

	(Dollars in thousands)
2002	\$ 186
2003	81
2004	19
thereafter	-
	-----
Total	\$ 286
	=====

The Company currently and from time to time is involved in litigation incidental to the conduct of its business. In the opinion of the Company's management, none of such litigation as of December 31, 2001 is likely to have a material adverse effect on the financial position, results of operations, or cash flows of the Company.

### 13. PENSION, OTHER POSTRETIREMENT BENEFITS AND OTHER BENEFITS

The Company participates in a defined benefit pension plan sponsored by Hercules, which covers substantially all employees of Hercules in the U.S. Benefits under this plan are based on the average final pay and years of service. Hercules also provides postretirement health care and life insurance benefits to eligible retired employees and their dependents.

Information on the actuarial present value of the benefit obligation and fair value of the plan assets is not presented as Hercules manages its U.S. employee benefit plans on a consolidated basis and such information is not maintained separately for the U.S. employees of the Company. The Company's statement of operation includes an allocation of the costs of the U.S. benefits plans. The pension costs were allocated based on percentage of pensionable wages, for each of the years presented, postretirement benefit costs were allocated using factors derived from the relative net assets and revenues. Net pension expense (income) of Hercules allocated to the Company was (\$612) thousand and (\$670) thousand for the year ended December 31, 2001 and 2000 respectively, and there was no allocation for 1999.

The Company maintains a 401(k) savings plan for its full-time U.S. employees. Each participant in the plan may elect to contribute 1% to 15% of his or her annual salary to the plan subject to statutory limitations. The Company matches employee contributions to the plan at the rate of 50% of the first 6% of salary contributed. The Company's matching contribution was \$268 thousand, \$313 thousand, and \$334 thousand for 2001, 2000, and 1999, respectively.

### 14. LONG-TERM INCENTIVE COMPENSATION PLAN

The Company participates in long-term incentive compensation plans sponsored by Hercules. These plans provide for the grant of stock options and the award of common stock and other market-based units to certain key employees and non-employee directors.

In 1995, Hercules changed the structure of the long-term incentive compensation plans to place a greater emphasis on shareholder value creation

## Edgar Filing: HERCULES INC - Form 10-K/A

through grants of regular stock options, performance-accelerated stock options, and Cash Value Awards (performance-based awards denominated in cash and payable in shares of common or restricted stock, subject to the same restrictions as restricted stock). Restricted stock and other market-based units are awarded with respect to certain programs. The number of awarded shares outstanding was 189,704 at December 31, 2001, and 491,488 and 926,689 at December 31, 2000 and 1999, respectively.

At December 31, 2001, under Hercules' incentive compensation plans, 1,265,493 shares of common stock were available for grant as stock awards or stock option awards. Stock awards are limited to approximately 15% of the total authorizations. Regular stock options are granted at the market price on the date of grant and are exercisable at various periods from one to five years after date of grant. Performance-accelerated stock options are also granted at the market price on the date of grant and are normally exercisable at nine and one-half years. Exercisability may be accelerated based upon the achievement of predetermined performance goals. Both regular and performance-accelerated stock options expire 10 years after the date of grant.

Restricted shares, options and performance-accelerated stock options are forfeited and revert to Hercules in the event of employment termination, except in the case of death, disability, retirement, or other specified events.

The Company applies APB Opinion 25 in accounting for its plans. Accordingly, no compensation cost has been recognized for the stock option plans. There were no charges to income for the cost of stock awards over the restriction or performance period for 2001, 2000 and 1999, respectively.

134

### FIBERVISIONS INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Below is a summary of outstanding stock option grants under the incentive compensation plans during 1999, 2000 and 2001:

	Regular		Performance-Accelerated	
	Number of Shares	Weighted-average price	Number of Shares	Weighted-average price
December 31, 1998	--	\$ --	--	--
Granted	69,000	\$37.56	55,700	\$ --
Exercised	--	--	--	--
Forfeited	--	--	--	--
December 31, 1999	69,000	\$37.56	55,700	\$ --
Granted	97,800	\$17.25	--	--
Exercised	--	--	--	--
Forfeited	--	--	--	--
December 31, 2000	166,800	\$25.65	55,700	\$ --
Granted	86,550	\$11.28	--	--
Exercised	--	--	--	--
Forfeited	--	--	--	--
December 31, 2001	253,350	\$20.74	55,700	\$ --

## Edgar Filing: HERCULES INC - Form 10-K/A

The weighted-average fair value of regular stock options granted during 1999, 2000 and 2001 was \$8.08, \$8.85 and \$5.69, respectively. The weighted-average fair value of performance-accelerated stock options granted during 1999, 2000 and 2001 was \$8.01, \$0 and \$0, respectively.

Following is a summary of regular stock options exercisable at December 31, 1999, 2000, and 2001, and their respective weighted-average share prices:

Options Exercisable	Number of Shares	Weighted-average exercise price
December 31, 2000	37,850	\$31.53
December 31, 2001	102,470	\$28.47

There were no performance-accelerated stock options exercisable at December 31, 1999, 2000 and 2001.

Following is a summary of stock options outstanding at December 31, 2001:

Exercise Price Range	Outstanding Options			Exer 12
	Number Outstanding at 12/31/2001	Weighted-average Remaining Contractual Life	Weighted- average exercise price	
Regular Stock Options				
\$11 - \$20	184,350	8.84	\$14.45	
\$30 - \$40	69,000	7.34	\$37.56	
	----- 253,350 -----			----- 1 -----
Performance-Accelerated Stock Options				
\$14 - \$40	55,700	7.34	\$37.56	
	----- 55,700 -----			-----  -----

The Company currently expects that 100% of performance-accelerated stock options will eventually vest.

The Company's employees may also participate in the Hercules Employee Stock Purchase Plan ("ESSP"). The ESSP is a qualified non-compensatory plan, which allows eligible employees to acquire shares of common stock through systematic payroll deductions. The plan consists of three-month subscription periods, beginning July 1 of each year. The purchase price is 85% of the fair market value of the common stock on either the first or last day of that subscription period, whichever is lower. Purchases may range from 2% to 15% of an employee's base salary each pay period, subject to certain limitations. Currently, there are no shares of Hercules common stock registered for offer and sale under the plan. Shares issued at December 31, 2001 and 2000, were 1,758,081 and 1,597,861, respectively. The Company applies APB Opinion 25 and related interpretations in accounting for its Employee Stock Purchase Plan.

## Edgar Filing: HERCULES INC - Form 10-K/A

Accordingly, no compensation cost has been recognized for the Employee Stock Purchase Plan.

Had compensation cost for Hercules' Stock-Based Incentive Plans and Employee Stock Purchase Plan been determined on the basis of fair value according to SFAS No. 123, the fair value of each option granted or share purchased would be estimated on the grant date using the Black-Scholes option pricing model.

The following weighted-average assumptions would be used in estimating fair value for 2001, 2000 and 1999:

135

FIBERVISIONS INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Assumption -----	Regular Plan -----	Performance Accelerated Plan -----	Employee Stock Purchase Plan -----
Dividend yield	0.96%	3.83%	0.0%
Risk-free interest rate	5.80%	5.57%	4.86%
Expected life	7.1 yrs.	5 yrs.	3 mos.
Expected volatility	33.36%	29.78%	49.11%

The Company's net income and earnings per share for 2001, 2000 and 1999 would approximate the pro forma amounts below:

	(Dollars in thousands)		
	2001 -----	2000 -----	1999 -----
Net income			
As reported	\$(3,323)	\$(23,091)	\$2,900
Pro forma	\$(3,793)	\$(23,521)	\$2,745

### 15. RELATED PARTY TRANSACTIONS

The Company has entered into certain agreements with affiliated entities. These agreements were developed in the context of parent/subsidiary relationship and therefore may not necessarily reflect the result of arm-length negotiations between independent parties. The terms of the agreements provide for the sale of product to the affiliated entities based on a cost-plus formula.

#### CORPORATE AND OTHER ALLOCATIONS

As discussed in Note 1, the financial statements of the Company reflect certain allocated support costs incurred by other entities in Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, safety, information management, health and environmental, investor relations and other corporate services. Allocations and charges included in the Company's financial statements were based on either a direct cost pass-through for items directly identified as related to the



## Edgar Filing: HERCULES INC - Form 10-K/A

Company's activities; or a percentage allocation for such services provided based on factors such as revenues, net assets, cost of sales and relative weighting of geographic activity. In addition, the Company allocates certain of its own costs to other companies in the FiberVisions group of companies. These allocations are reflected in the selling, general and administrative line item in our statement of operations. Such allocations and corporate charges totaled \$650 thousand, (\$1,444) thousand and (\$2,865) thousand in 2001, 2000, and 1999, respectively.

### SALES TO HERCULES GROUP

The Company sells fiber in the normal course of business to affiliated companies. Company's revenues from sales to affiliated companies were \$82,101 thousand, \$105,724 thousand, and \$92,352 thousand in 2001, 2000 and 1999, respectively.

### PURCHASES FROM HERCULES GROUP

The Company purchases supplies in the normal course of business from the Hercules Group. The Company's purchases from Hercules Group were \$35 thousand, \$69 thousand, and \$80 thousand in 2001, 2000, and 1999, respectively.

### 16. NET HERCULES GROUP INVESTMENT

Changes in net Hercules Group investment were as follows:

136

### FIBERVISIONS INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

Balance at January 1, 1999	\$ 151,138
Net income	2,900
Intercompany transactions, net	13,208
	-----
Balance at December 31, 1999	167,246
Net income	(23,091)
Intercompany transactions, net	(197)
	-----
Balance at December 31, 2000	143,958
Net (loss)	(3,323)
Intercompany transactions, net	946
	-----
Balance at December 31, 2001	\$ 141,581
	=====

### 17. SUBSEQUENT EVENTS

On April 29, 2002, Hercules completed the sale of its Water Treatment Business to GE Specialty Materials (GSM). Pursuant to the Stock and Asset Agreement for the transaction, the sale included all of the stock of BetzDearborn Inc. Hercules used the proceeds from the sale to prepay borrowings under its Senior Credit Facility and ESOP Credit Facility. Pursuant to the prepayment, among other things, the stock pledges were released.

REPORT OF INDEPENDENT ACCOUNTANTS

TO THE SHAREHOLDERS AND THE BOARD OF DIRECTORS OF  
HERCULES INCORPORATED  
WILMINGTON, DELAWARE

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations and comprehensive income (loss) and of cash flows present fairly, in all material respects, the financial position of FiberVisions L.L.C., a subsidiary of Hercules Incorporated, and its subsidiaries at December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America that require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 20, the Company has restated its December 31, 2000 and 1999 financial statements to reflect income tax provisions for its subsidiaries whose income is subject to corporate income taxes at the subsidiary level.

PricewaterhouseCoopers LLP  
Philadelphia, Pennsylvania  
November 21, 2002

FIBERVISIONS, L.L.C.  
CONSOLIDATED STATEMENT OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousand)	
	YEAR ENDED DECEMBER	
	2001	Restated 2000
	-----	-----
Sales to third parties	\$201,780	\$236,856
Sales to affiliates	16,586	15,003
	-----	-----
	218,366	251,859
Cost of sales	184,393	223,133
Selling, general, and administrative expenses	5,509	9,521
Research and development	3,681	4,475
Impairment of long lived assets (Note 11)	--	53,541
Goodwill and intangible amortization	7,348	7,394
Other operating expenses (income), net (Note 12)	1,363	(146)
	-----	-----
Profit (loss) from operations	16,072	(46,059)
Equity in income of affiliated companies (Note 6)	1,319	153
Interest expense, net (Note 10)	5,790	6,940
	-----	-----
Income (loss) before income taxes	11,601	(52,846)
Provision (benefit) for income taxes (Note 19)	6,110	(6,378)
	-----	-----
Net income (loss)	5,491	(46,468)
Translation gain, net of tax	1,274	1,299
	-----	-----
Comprehensive income (loss)	\$ 6,765	\$ (45,169)
	=====	=====

The accompanying notes are an integral part of the consolidated financial statements.

FIBERVISIONS, L.L.C.  
CONSOLIDATED BALANCE SHEET

(Dollars in thousands)	
DECEMBER 31,	
2001	Restated 2000
-----	-----

Edgar Filing: HERCULES INC - Form 10-K/A

ASSETS

Current assets

Cash and cash equivalents	\$ 10,303	\$ 4,777
Accounts receivable, net (Note 3)	34,205	42,809
Affiliate receivables (Note 5)	1,873	2,711
Inventories (Note 4)	14,851	17,993

Total current assets	61,232	68,290
----------------------	--------	--------

Property, plant, and equipment, net (Note 8)	109,149	121,966
Goodwill and other intangible assets, net (Note 9)	192,241	199,696
Deferred charges and other assets	502	423

Total assets	\$363,124	\$390,375
--------------	-----------	-----------

LIABILITIES AND NET MEMBERS' (HERCULES GROUP) INVESTMENT

Current liabilities

Accounts payable	\$ 15,485	\$ 21,405
Short-term debt (Note 7)	7,532	11,588
Accrued expenses (Note 8)	17,413	12,787

Total current liabilities	40,430	45,780
---------------------------	--------	--------

Long-term debt - third parties (Note 7)	44,489	53,919
Deferred income taxes (Note 19)	24,316	20,105

Total liabilities	109,235	119,804
-------------------	---------	---------

Commitments and contingencies (Note 14)

-- --

Net members' (Hercules Group) investment (Note 18)

Accumulated other comprehensive income	3,625	2,351
Intercompany balances	250,264	268,220

Net members' (Hercules Group) investment	253,889	270,571
--	---------	---------

Total liabilities and net members' (Hercules Group) investment	\$363,124	\$390,375
--	-----------	-----------

The accompanying notes are an integral part of the consolidated financial statements.

FIBERVISIONS, L.L.C.  
CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars  
YEAR ENDED)

2001

## Edgar Filing: HERCULES INC - Form 10-K/A

CASH FLOW FROM OPERATING ACTIVITIES:		
Net income (loss)	\$	5,491
Adjustments to reconcile net income (loss) to net cash provided from operations:		
Depreciation		11,229
Provision for impairment of long-lived assets		--
Amortization of goodwill and other intangible assets		7,348
Bad debt expense		--
Loss on disposal of fixed assets		18
Corporate and other cost allocations		876
Deferred income taxes		(714)
Other items, net		--
Affiliates earnings in excess of dividends received		(282)
Accruals and deferrals of cash receipts and payments:		
Accounts receivable		7,946
Affiliate receivables (payables)		957
Transfers from Hercules Group		1,210
Inventories		2,976
Accounts payable and accrued expenses		(201)
Noncurrent assets and liabilities		(20)
Net cash provided by operations		36,834
CASH FLOW FROM INVESTING ACTIVITIES:		
Capital expenditures		(609)
Acquisitions, net of cash acquired		--
Other, net		95
Net cash used in investing activities		(514)
CASH FLOW FROM FINANCING ACTIVITIES:		
Long-term debt repayments, third parties		(11,279)
Transfers to Hercules Group		(19,404)
Change in short-term debt		--
Net cash used in financing activities		(30,683)
Effect of exchange rate changes on cash		(111)
Net increase (decrease) in cash and cash equivalents		5,526
Cash and cash equivalents at beginning of year		4,777
Cash and cash equivalents at end of year	\$	10,303
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the year for:		
Interest	\$	5,807
Income taxes, net		2,728
Noncash financing activities		
Corporate and other cost allocations		876

The accompanying notes are an integral part of the consolidated financial statements.

## Edgar Filing: HERCULES INC - Form 10-K/A

FIBERVISIONS, L.L.C.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

### 1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

FiberVisions LLC. ("FiberVisions" or the "Company") serves worldwide markets for polypropylene nonwoven fiber used to make disposable hygiene products. The Company also produces olefin fiber and yarn for domestic textile and industrial markets for use in fabrics, residential upholstery, geotextiles, carpets and asphalt. The company is a wholly owned subsidiary of Hercules Incorporated ("Hercules").

Historically, separate company stand-alone financial statements were not prepared for the Company. In November 2000, Hercules amended its senior credit facility and ESOP credit facility (the "Facilities"). The Facilities, as amended, are secured by liens on Hercules' property and assets (and those of Hercules' Canadian Subsidiaries), a pledge of the stock of substantially all of Hercules' domestic subsidiaries (including FiberVisions LLC) and 65% of the stock of foreign subsidiaries directly owned by Hercules, and a pledge of Hercules' domestic intercompany indebtedness. These financial statements present the financial information on the Company, a collateral party to the Hercules debt, based on the Hercules' understanding of Securities and Exchange Commission's interpretation and application of Rule 3-16 under the Securities and Exchange Commission's Regulation S-X. These statements were derived from historical accounting records.

On April 29, 2002, in connection with Hercules' sale of its Water Treatment Business (see Note 21) and the repayment of the Facilities, the stock pledges were released. As a result, based on Hercules' current debt structure, these separate company stand-alone financial statements will not be required for the fiscal year ending December 31, 2002.

The Company participates in Hercules' centralized cash management system. Accordingly, cash received from the Company's operations is transferred to Hercules on a periodic basis, and Hercules funds all operational and capital requirements.

The financial statements of the Company reflect certain allocated support costs incurred by other entities in the Hercules group. These costs include legal, accounting, tax, purchasing, safety, information management and other corporate services. Allocations and charges included in the Company's financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on factors such as sales, net assets, or cost of sales; or a relative weighting of geographic activity. Management believes that the allocation methods are reasonable.

During 1998, Hercules acquired the remaining 49% of the Company to make this a wholly owned subsidiary. These financial statements include the push-down of fair value adjustments to assets and liabilities, including goodwill, other intangible assets and property, plant, and equipment and their related amortization and depreciation adjustments.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the FiberVisions, L.L.C. and its majority-owned subsidiaries where control exists. Investments in affiliated companies with a greater than 20% and less than 50% ownership interest are accounted for using the equity method of accounting and,

## Edgar Filing: HERCULES INC - Form 10-K/A

accordingly, consolidated income includes FiberVisions L.L.C.'s share of their income. All intercompany transactions and profits have been eliminated.

### USE OF ESTIMATES

Preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

### REVENUE RECOGNITION

The company recognizes revenue when the earnings process is complete. This generally occurs when products are shipped to the customer or services are performed in accordance with the terms of the agreement, title and risk of loss have been transferred, collectibility is probable, and pricing is fixed and determinable. Accruals are made for sales returns and other allowances based on the Company's experience. The corresponding shipping and handling costs are included in cost of sales.

142

FIBERVISIONS, L.L.C.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

### CASH AND CASH EQUIVALENTS

Cash equivalents include commercial paper and other securities with original maturities of 90 days or less. Book value approximates fair value because of the short maturity of those instruments.

### INVENTORIES

Inventories are stated at the lower of cost or market using the average cost method.

### PROPERTY AND DEPRECIATION

Property, plant, and equipment are stated at historical cost. The company uses the straight-line method of depreciation. The company believes straight-line depreciation provides a better matching of costs and revenues over the lives of the assets. The estimated useful lives of depreciable assets are as follows: buildings - 30 years; plant, machinery and equipment - 15 years; other machinery and equipment - 3 to 15 years.

Maintenance, repairs, and minor renewals are charged to income; major renewals and betterments are capitalized. Upon normal retirement or replacement, the net book value of property (less proceeds of sale or salvage) is charged to income.

### GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill and other intangible assets are amortized on a straight-line basis over the estimated future periods to be benefited, generally 40 years for goodwill and 10 years for other intangible assets. Goodwill arises in connection with acquisitions. The purchase price is allocated to the fair value of the assets acquired and liabilities assumed with the excess recorded as goodwill.

## Edgar Filing: HERCULES INC - Form 10-K/A

Pursuant to Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (SFAS 142), beginning January 1, 2002, goodwill will not be amortized but will be tested for impairment annually and any necessary adjustment charged to expense. Intangible assets with finite lives will be amortized over their useful lives.

### INCOME TAXES

U.S. Federal income taxes on net earnings of the company are payable directly by the members. In jurisdictions where partnership status is not recognized or foreign corporate subsidiaries exist, the company provides for income taxes currently payable as well as for those deferred because of temporary differences between the financial and tax basis of assets and liabilities. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized.

The company provides taxes on undistributed earnings of subsidiaries and affiliates included in consolidated retained earnings to the extent such earnings are planned to be remitted and not re-invested permanently. The undistributed earnings of subsidiaries and affiliates on which no provision for foreign withholding or US income taxes has been made amounted to approximately \$63,270 thousand, \$62,410 thousand, and \$61,343 thousand at December 31 2001, 2000, and 1999, respectively. US and foreign income taxes that would be payable if such earnings were distributed may be lower than the amount computed at the US statutory rate because of the availability of tax credits.

### IMPAIRMENT OF LONG-LIVED ASSETS

The company reviews its long-lived assets, including goodwill and other intangibles, for impairment on an exception basis whenever events or changes in circumstances indicate carrying amounts of the assets may not be recoverable through undiscounted future cash flows. If an impairment loss has occurred based on expected future cash flows (undiscounted), the loss is recognized in the income statement. The amount of the impairment loss is the excess of the carrying amount of the impaired asset over the fair value of the asset. The fair value represents expected future cash flows from the use of the assets, discounted at the rate used to evaluate potential investments. During 2000 the company recorded long-lived asset impairments of \$53,541 thousand (see note 11).

### FOREIGN CURRENCY TRANSLATION AND TRANSACTIONS

The accompanying consolidated financial statements are reported in U.S. dollars. The US Dollar is the functional currency for FiberVisions L.L.C. and its domestic subsidiaries and associated companies. However, the Danish kroner, Chinese renmimbi, German mark, and the Swiss franc are the functional currencies for its foreign subsidiaries located in the Denmark, China, Germany, and Switzerland respectively. The translation of the functional currencies into U.S. dollars (reporting currency) is performed for assets and liabilities using the current exchange rates in effect at the balance sheet date, and for revenues, costs and expenses using average exchange rates prevailing during the reporting periods.



## Edgar Filing: HERCULES INC - Form 10-K/A

Adjustments resulting from the translation of functional currency financial statements to reporting currency are accumulated and reported as other comprehensive income (loss), a separate component of shareholders' equity.

Transactions in foreign currency are recorded at the exchange rate prevailing on the date of transaction. Monetary assets and liabilities denominated in foreign currencies are expressed in the functional currency at the exchange rates in effect at the balance sheet date. Revenues, costs and expenses are recorded using average exchange rates prevailing during the reporting periods. Gains or losses resulting from foreign currency transactions are included in the statement of operations.

### CONCENTRATIONS OF CREDIT RISK

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of trade receivables. However, the overall risk is limited to the large number of customers in different geographic areas and industries.

### STOCK-BASED COMPENSATION

Compensation costs attributable to stock option and similar plans are recognized based on any excess of the quoted market price of the stock on the date of grant over the amount the employee is required to pay to acquire the stock (the intrinsic-value method under Accounting Principles Board Opinion 25 (APB 25)). Such amount, if any, is accrued over the related vesting period, as appropriate. Statement of Financial Accounting Standard No. 123, "Accounting for Stock-based Compensation," requires companies electing to continue to use the intrinsic-value method to make pro forma disclosures of net income as if the fair-value-based method of accounting had been applied.

### NET MEMBERS' (HERCULES GROUP) INVESTMENT

The net Members' (Hercules Group) investment account reflects the balance of FiberVisions historical earnings, foreign currency translation, intercompany amounts, income tax, taxes accrued and deferred, post employment liabilities, and other transactions between the Company and the Members/Hercules Group.

### NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 141, "Business Combinations" ("SFAS 141"), and Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"). SFAS 141 supersedes Accounting Principles Board Opinion ("APB") No. 16, Business Combinations. The provisions of SFAS 141 (1) require that the purchase method of accounting be used for all business combinations initiated after June 30, 2001, (2) provide specific criteria for the initial recognition and measurement of intangible assets apart from goodwill and (3) require that unamortized negative goodwill be written off immediately as extraordinary gain instead of being deferred and amortized. SFAS 141 also requires that upon adoption of SFAS 142 the Company reclassify the carrying amounts of certain intangible assets into or out of goodwill, based on certain criteria. SFAS 142 supersedes APB No. 17, Intangible Assets, and is effective for fiscal years beginning after December 15, 2001. SFAS 142 primarily addresses the accounting for goodwill and intangible assets subsequent to their initial recognition. The provisions of SFAS 142 (1) prohibit the amortization of goodwill and indefinite-lived intangible assets, (2) require that goodwill and indefinite-lived intangible assets be tested annually for impairment (and in interim periods if certain events occur indicating that the carrying value of goodwill and/or indefinite-lived intangible assets may be impaired), based on fair value (as opposed to cost recovery using future undiscounted cash flows),

## Edgar Filing: HERCULES INC - Form 10-K/A

(3) require that reporting units be identified for the purpose of assessing potential future impairments of goodwill and (4) remove the forty-year limitation on the amortization period of intangible assets that have finite lives.

Effective January 1, 2002, Hercules adopted the provisions of SFAS 142. Hercules identified the following reporting units: Betz Dearborn, Pulp and Paper, Aqualon, FiberVisions, and Resins. In connection with Hercules' transitional review, recorded goodwill was determined to be impaired in the Betz Dearborn and FiberVisions reporting units. In the first quarter 2002, Hercules completed its transitional impairment review of the identified units and recognized an after tax impairment loss of \$368 million as a cumulative effect of a change in accounting principle of which \$87 million related to the FiberVisions reporting unit. As a result of Hercules' adoption of SFAS 142, the Company will no longer record \$7.3 million of annual amortization relating to existing goodwill and intangibles.

Goodwill was evaluated for impairment at December 31, 2001 under Statement of Financial Accounting Standards No. 121 "Accounting for the Impairment of Long-Fixed Assets and for Long-Lived Assets to Be Disposed of". Such evaluations indicated that goodwill associated with the business was recoverable from anticipated future

144

FIBERVISIONS, L.L.C.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

undiscounted cash flows. Accordingly, no impairment loss was recorded in the December 31, 2001 financial statements.

In June 2001, the Financial Accounting Standards Board ("FASB") approved the issuance of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143"). SFAS 143 establishes accounting standards for the recognition and measurement of legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 will become effective for the Company on January 1, 2003 and requires recognition of a liability for an asset retirement obligation in the period in which it is incurred. The Company does not believe it will have a material effect on its financial statements.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company does not believe it will have a material effect on its financial statements.

In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment to FASB Statement No. 13, and Technical Corrections." The Company elected to early adopt the provisions of SFAS 145 related to the rescission of SFAS 4, "Reporting Gains and Losses from the Extinguishment of Debt" ("SFAS 4"). The early adoption had no effect on the Company's financial statements.

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146"). SFAS 146 addresses financial accounting and reporting for costs

## Edgar Filing: HERCULES INC - Form 10-K/A

associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs in a Restructuring)". SFAS 146 defines the timing of the recognition of costs associated with exit or disposal activities, the types of costs that may be recognized and the methodology for calculating the fair value of such costs. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. The Company does not believe this statement will have a material effect on its financial statements.

### RECLASSIFICATIONS

Certain amounts in the 2000 and 1999 consolidated financial statements and notes have been reclassified to conform to the 2001 presentation.

#### 3. ACCOUNTS RECEIVABLE, NET

Accounts receivable, net, consists of:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Trade	\$ 30,609	\$ 39,834
Rebates from suppliers	3,856	2,857
Other	154	748
	-----	-----
	34,619	43,439
Less allowance for doubtful accounts	(414)	(630)
	-----	-----
Total	\$ 34,205	\$ 42,809
	=====	=====

#### 4. INVENTORIES

The components of inventories are:

145

FIBERVISIONS, L.L.C.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

	(Dollars in thousands)	
	2001	2000
	-----	-----
Finished products	\$ 5,227	\$ 7,461
Materials and work in process	3,643	4,596
Supplies	5,981	5,936
	-----	-----
Total	\$14,851	\$17,993
	=====	=====

## Edgar Filing: HERCULES INC - Form 10-K/A

### 5. AFFILIATE RECEIVABLES (PAYABLES), NET

Trade receivables from affiliates, consists of \$3,813 thousand and \$4,926 thousand due from ES FiberVisions for years ended December 31, 2001 and 2000, respectively, net of \$1,940 and \$2,215 of accumulated losses of unconsolidated companies in excess of investment for years 2001 and 2000, respectively (see Note 6). The company agrees to fund the accumulated losses of such unconsolidated companies.

### 6. INVESTMENTS

On January 1, 2000 the Company and Chisso Polypro Fiber Co., Ltd formed a 50/50 joint venture, ES FiberVisions, combining their bicomponent fibers businesses outside of Japan. While the Company has a 50% equity interest, it's share of joint venture operations is 67%. Both parent companies supply fiber to the joint venture under manufacturing agreements. The Company manufactures bicomponent fibers for the joint venture at the Varde, Denmark and Athens, Georgia locations. The annual sales of the venture were approximately \$55 million and \$48 million in fiscal 2001 and 2000, respectively. The Company's share of net income was \$1,319 thousand and \$153 thousand in 2001 and 2000, respectively.

Summarized financial information for the equity affiliates at December 31, and the years then ended is as follows:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Current assets	\$10,413	\$10,809
Noncurrent assets	1,865	1,450
Current liabilities	9,389	10,803
Noncurrent liabilities	94	
Net sales	\$54,509	\$48,410
Gross profit	9,888	7,520
Net earnings	1,969	228

### 7. LONG-TERM DEBT

Long-term debt at December 31, 2001 and 2000 is summarized as follows:

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousand)		
	2001		
	BOOK VALUE	MARKET VALUE	BOOK VALUE
Revolving credit facility due in varying amounts through 2005 with an average interest rate of 4.15%	\$ 18,533	\$ 18,533	\$ 19,000
Finansierings Instituttet for Industri og Handvoerk A/S (FIH)	10,455	10,610	15,000
term notes at various rates from 6.94% to 9.60% and due in varying amounts through 2006			
Danmark Finansiering Institut A/S (DFI)	18,704	19,266	23,000
term notes at various rates from 6.48% to 8.56% and due in varying amounts through 2006			
Mortgage at a fixed rate of 7.16% and due in varying amounts through 2014	4,079	4,304	4,000
Industrialization Fund for Developing Countries (IFU) at a fixed rate of 5.23% and due in 2001	--	--	2,000
Lease purchase obligation	250	250	
	-----	-----	-----
	52,021	52,963	65,000
Less current maturities	(7,532)	(7,765)	(11,000)
	-----	-----	-----
Total	\$ 44,489	\$ 45,198	\$ 53,000
	=====	=====	=====

As of December 31, 2001 FIH term notes are collateralized by land, buildings, and plant and machinery of approximately \$27,598 thousand. The DFI loan is collateralized by a letter of indemnification regarding land, buildings and plant and machinery of approximately \$17,843 thousand. The mortgage is collateralized by land and buildings of approximately \$4,079 thousand.

In December 1996 the Company entered into a long-term lease purchase obligation with The Athens-Clark County Industrial Development Authority to purchase land. The interest rate is fixed at 1% per annum and the due date of the obligation is December 2020. The balance of the obligation was \$250 thousand at December 31, 2001 and 2000.

Scheduled annual maturities of long-term debt outstanding at December 31, 2001 in the successive five-year period are summarized as follows:

(Dollars in thousands)	
-----	
2002	\$ 7,532
2003	12,270
2004	12,243
2005	12,692
2006	4,222
Thereafter	3,062
	-----
Total	\$52,021
	=====

FIBERVISIONS, L.L.C.  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

8. ADDITIONAL BALANCE SHEET DETAIL

	(Dollars in thousands)	
	2001	2000
	-----	-----
Property, plant, and equipment		
Land	\$ 1,273	\$ 1,282
Buildings and equipment	360,315	365,539
Construction in progress	15,531	16,054
	-----	-----
Total	377,119	382,875
Accumulated depreciation and amortization	(267,970)	(260,909)
	-----	-----
Net property, plant, and equipment	\$ 109,149	\$ 121,966
	=====	=====
Accrued expenses		
Payroll and employee benefits	\$ 2,069	\$ 2,168
Accrued interest payable	275	365
Current taxes payable	3,616	245
Accrued MICP	945	--
Miscellaneous	10,508	10,009
	-----	-----
	\$ 17,413	\$ 12,787
	=====	=====

9. GOODWILL AND OTHER INTANGIBLES ASSETS

At December 31, 2001 and 2000, the goodwill and other intangible assets were:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Goodwill from Hercules acquisition	\$ 188,051	\$ 188,051
Other intangibles	31,219	31,350
	-----	-----
Total	219,270	219,401
Less accumulated amortization	(27,029)	(19,705)
	-----	-----
Net goodwill and other intangible assets	\$ 192,241	\$ 199,696
	=====	=====

In July 1998, Hercules Inc. completed the acquisition of 49% share of FiberVisions L.L.C. owned by its joint venture partner, Jacob Holm & Son A/S, for approximately \$230 million in cash, plus assumed debt of \$188 million. The

## Edgar Filing: HERCULES INC - Form 10-K/A

allocation of the purchase price resulted in \$188,051 thousand of goodwill for the FiberVisions group, which is being amortized over its estimated useful life of 40 years. Other intangibles assets, related to the acquisition, amounted to \$29,752 thousand, the remaining other intangible assets relate to capitalization of certain patent costs.

### 10. INTEREST EXPENSE , NET

Interest costs are summarized as follows:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Interest expense	\$ 6,945	\$ 7,459	\$ 8,738
Interest income	(1,155)	(519)	(187)
	-----	-----	-----
Interest expense, net	\$ 5,790	\$ 6,940	\$ 8,551
	=====	=====	=====

148

FIBERVISIONS, L.L.C.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 11. IMPAIRMENT OF LONG LIVED ASSETS

In the third quarter of 2000, FiberVisions recorded assets impairments of the China facility of \$28,169 thousand. Management determined that revised growth projections for the China hygiene non-woven market would indefinitely delay the feasibility of expanding the production capability of the facility. Estimated future cash flows related to this facility without the planned expansion indicated that an impairment had occurred. The impairment charge was required to write off approximately 90% of the net book value of the existing Suzhou, China facility as well as the investment in the new fiber line.

In addition, impairment of \$25,372 thousand was required to write off the remaining net book value of the textiles plant in Covington, GA. The textiles business fundamentals have been deteriorating for the past few years. In 2000, the cost for the major raw material, polypropylene, has risen above historical price levels. The combination of the above factors has resulted in an irreversible loss of profitability for the textiles business. Estimated future cash flows related to this facility indicated full impairment had occurred.

### 12. OTHER OPERATING EXPENSES (INCOME), NET

Other operating expenses, net, consists of the following:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----

## Edgar Filing: HERCULES INC - Form 10-K/A

Miscellaneous expense (income), net	\$ 1,355	\$ (252)	\$ 14
Loss (gain) on foreign currency transactions	8	106	(327)
	-----	-----	-----
	\$ 1,363	\$ (146)	\$ (313)
	=====	=====	=====

### 13. OTHER FINANCING ARRANGEMENTS

Hercules manages the Company's cash and indebtedness. The majority of the cash provided by or used by the Company is provided through this consolidated cash and debt management system. As a result, the amount of domestic cash or debt historically related to the Company is not determinable. For the purposes of the Company's historical financial statements all of its positive or negative cash flows have been treated as cash transferred to or from its parent.

The Company has an intercompany loan with the Hercules Group in the amount of \$21,705 thousand and \$36,799 thousand which is included in the net members' investment balance at December 31, 2001 and 2000, respectively. At December 31, 2001 and 2000 the weighted average interest rate on the intercompany borrowings was 7.6% and 7.4%, respectively. Interest expense was \$3,009 thousand, \$2,865 thousand and \$2,721 thousand in 2001, 2000 and 1999, respectively. Repayment terms of the loan are included as part of the Hercules cash management system as described in the previous paragraph.

### 14. COMMITMENTS AND CONTINGENCIES

The Company has operating leases (including office space, storage space, and data processing equipment) expiring at various dates. Rental expense was \$437 thousand, \$574 thousand, and \$484 thousand in 2001, 2000, and 1999, respectively.

The net minimum future payments at December 31, 2001 are as follows:

149

FIBERVISIONS, L.L.C.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands)

2002	\$273
2003	150
2004	52
2005	8
2006	8
	-----
Total	\$491
	=====

The Danish tax authorities have increased FiberVisions A/S' taxable income for the tax year 1997. The tax value of the declared increase amounts to



## Edgar Filing: HERCULES INC - Form 10-K/A

approximately \$1,400 thousand. Management does not agree with the assessment of the tax authorities, and the case has been appealed. Consequently, the final outcome of the case uncertain.

The Company currently and from time to time is involved in litigation incidental to the conduct of its business. In the opinion of the Company's management, none of such litigation as of December 31, 2001 is likely to have a material adverse effect on the financial position, results of operations, or cash flows of the Company.

### 15. PENSION, OTHER POSTRETIREMENT BENEFITS AND OTHER BENEFITS

The Company participates in a defined benefit pension plan sponsored by Hercules, which covers substantially all employees of Hercules in the U.S. Benefits under this plan are based on the average final pay and years of service. Hercules also provides postretirement health care and life insurance benefits to eligible retired employees and their dependents.

Information on the actuarial present value of the benefit obligation and fair value of the plan assets is not presented as Hercules manages its U.S. employee benefit plans on a consolidated basis and such information is not maintained separately for the U.S. employees of the Company. The Company's statement of operation includes an allocation of the costs of the U.S. benefits plans. The pension costs were allocated based on percentage of pensionable wages, for each of the years presented, postretirement benefit costs were allocated using factors derived from the relative net assets and revenues. Net pension expense (income) of Hercules allocated to the Company was (\$724) thousand (\$799) thousand for the year ended December 31, 2001 and 2000 respectively. There was no allocation in 1999.

The company maintains a 401(k) savings plan for its US full-time employees. Each participant in the plan may elect to contribute 1% to 15% of his or her annual salary to the plan subject to statutory limitations. The company matches employee contributions to the plan at the rate of 50% of the first 6% of salary contributed. The Company's matching contribution was \$327 thousand, \$382 thousand, and \$413 thousand for 2001, 2000, and 1999, respectively.

FiberVisions A/S maintains a contributory pension plan. FiberVisions A/S matching contribution was \$940 thousand, \$964 thousand, and \$977 thousand for 2001, 2000, and 1999, respectively. FiberVisions (China) Textiles Products, Ltd. provides a housing allowance for their employees. FiberVisions (China) Textiles Products, Ltd. contribution was \$141 thousand, \$160 thousand, and \$137 thousand in 2001, 2000, and 1999, respectively.

### 16. LONG TERM INCENTIVE COMPENSATION PLAN

The company participates in long-term incentive compensation plans sponsored by Hercules. These plans provide for the grant of stock options and the award of common stock and other market-based units to certain key employees and non-employee directors.

In 1995, Hercules changed the structure of the long-term incentive compensation plans to place a greater emphasis on shareholder value creation through grants of regular stock options, performance-accelerated stock options, and Cash Value Awards (performance-based awards denominated in cash and payable in shares of common or restricted stock, subject to the same restrictions as restricted stock). Restricted stock and other market-based units are awarded with respect to certain programs. The number of awarded shares outstanding was 189,704 at December 31, 2001, and 491,488 and 926,689 at December 31, 2000 and 1999, respectively.

FIBERVISIONS, L.L.C.  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

At December 31, 2001, under Hercules' incentive compensation plans 1,265,493 shares of common stock were available for grant as stock awards or stock option awards. Stock awards are limited to approximately 15% of the total authorizations. Regular stock options are granted at the market price on the date of grant and are exercisable at various periods from one to five years after date of grant. Performance-accelerated stock options are also granted at the market price on the date of grant and are normally exercisable at nine and one-half years. Exercisability may be accelerated based upon the achievement of predetermined performance goals. Both regular and performance-accelerated stock options expire 10 years after the date of grant.

Restricted shares, options and performance-accelerated stock options are forfeited and revert to Hercules in the event of employment termination, except in the case of death, disability, retirement, or other specified events.

The Company applies APB Opinion 25 in accounting for its plans. Accordingly, no compensation cost has been recognized for the stock option plans. There were no charges to income for the cost of stock awards over the restriction or performance period for 2001, 2000 and 1999, respectively.

Below is a summary of outstanding stock option grants under the incentive compensation plans during 1999, 2000 and 2001:

	REGULAR		PERFORMANCE-ACCELERATED	
	NUMBER OF SHARES	WEIGHTED-AVERAGE PRICE	NUMBER OF SHARES	WEIGHTED-AVERAGE PRICE
December 31, 1998	--	\$ --	--	--
Granted	69,000	\$ 37.56	55,700	\$ 37.56
Exercised	--	--	--	--
Forfeited	--	--	--	--
December 31, 1999	69,000	\$ 37.56	55,700	\$ 37.56
Granted	104,675	\$ 17.25	--	--
Exercised	--	--	--	--
Forfeited	--	--	--	--
December 31, 2000	173,675	\$ 25.32	55,700	\$ 37.56
Granted	93,425	\$ 11.28	--	--
Exercised	--	--	--	--
Forfeited	--	--	--	--
December 31, 2001	267,100	\$ 20.41	55,700	\$ 37.56

The weighted-average fair value of regular stock options granted during 1999, 2000 and 2001 was \$8.08, \$8.85 and \$5.69, respectively. The weighted-average fair value of performance-accelerated stock options granted during 1999, 2000 and 2001 was \$8.01, \$0 and \$0, respectively.

## Edgar Filing: HERCULES INC - Form 10-K/A

Following is a summary of regular stock options exercisable at December 31, 2001, 2000, and 1999, and their respective weighted-average share prices:

OPTIONS EXERCISABLE	NUMBER OF SHARES	WEIGHTED-AVERAGE EXERCISE PRICE
December 31, 2000	37,850	\$31.53
December 31, 2001	105,220	\$28.18

There were no performance-accelerated stock options exercisable at December 31, 2001, 2000 and 1999.

Following is a summary of stock options outstanding at December 31, 2001:

EXERCISE PRICE RANGE	OUTSTANDING OPTIONS			N EXERC 12/
	NUMBER OUTSTANDING AT 12/31/2001	WEIGHTED-AVERAGE REMAINING CONTRACTUAL LIFE	WEIGHTED- AVERAGE EXERCISE PRICE	
Regular Stock Options				
\$11 - \$20	198,100	8.85	\$14.43	4
\$30 - \$40	69,000	7.34	\$37.56	5
	267,100			10
Performance-Accelerated Stock Options				
\$14 - \$40	55,700	7.34	\$37.56	
	55,700			

The Company currently expects that 100% of performance-accelerated stock options will eventually vest.

FIBERVISIONS, L.L.C.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

FiberVisions LLC employees may also participate in the Hercules Employee Stock Purchase Plan ("ESSP"). The ESSP is a qualified non-compensatory plan, which allows eligible employees to acquire shares of common stock through systematic payroll deductions. The plan consists of three-month subscription periods, beginning July 1 of each year. The purchase price is 85% of the fair market value of the common stock on either the first or last day of that subscription period, whichever is lower. Purchases may range from 2% to 15% of an employee's base salary each pay period, subject to certain limitations. Currently, three are no shares of Hercules common stock are registered for offer

## Edgar Filing: HERCULES INC - Form 10-K/A

and sale under the plan. Shares issued at December 31, 2001 and 2000, were 1,758,081 and 1,597,861, respectively. The company applies APB Opinion 25 and related interpretations in accounting for its Employee Stock Purchase Plan. Accordingly, no compensation cost has been recognized for the Employee Stock Purchase Plan.

Had compensation cost for Hercules' Stock-Based Incentive Plans and Employee Stock Purchase Plan been determined on the basis of fair value according to SFAS No. 123, the fair value of each option granted or share purchased would be estimated on the grant date using the Black-Scholes option pricing model.

The following weighted-average assumptions would be used in estimating fair value for 2001, 2000 and 1999:

ASSUMPTION -----	REGULAR PLAN -----	PERFORMANCE ACCELERATED PLAN -----	EMPLOYEE STOCK PURCHASE PLAN -----
Dividend yield	0.96%	3.83%	0.0%
Risk-free interest rate	5.80%	5.57%	4.86%
Expected life	7.1 yrs.	5 yrs.	3 mos.
Expected volatility	33.36%	29.78%	49.11%

The Company's net income and earnings per share for 2001, 2000 and 1999 would approximate the pro forma amounts below:

	(Dollars in thousands)		
	2001 -----	2000 -----	1999 -----
Net income			
As reported	\$5,491	\$(46,468)	\$15,855
Pro forma	\$5,001	\$(46,912)	\$15,700

### 17. RELATED PARTY TRANSACTIONS

The Company has entered into certain agreements with affiliated entities. These agreements were developed in the context of parent/subsidiary relationship and therefore may not necessarily reflect the result of arm-length negotiations between independent parties. The terms of the agreements provide for the sale of product to the affiliated entities based on a cost-plus formula.

#### CORPORATE AND OTHER ALLOCATIONS

As discussed in Note 1, the financial statements of the Company reflect certain allocated support costs incurred by other entities in Hercules group. These costs include legal, accounting, tax, purchasing, safety, information management, and other corporate services. Allocations and charges included in the Company's financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; or a percentage allocation for such services provided based on factors such as revenues, net assets, cost of sales and relative weighting of geographic activity. These allocations are reflected in the selling, general and

## Edgar Filing: HERCULES INC - Form 10-K/A

administrative line item in our statement of operations. Such allocations and corporate charges totaled \$876 thousand, \$457 thousand and \$1,180 thousand in 2001, 2000 and 1999, respectively.

### SALES TO AFFILIATES

The Company sells fiber in the normal course of business to affiliated companies. Company's revenues from sales to affiliated companies were \$16,586 thousand, \$15,003 thousand in 2001 and 2000, respectively. Total amounts due from affiliated companies related to those sales were \$3,813 thousand and \$4,926 thousand at December 31, 2001 and 2000, respectively.

152

FIBERVISIONS, L.L.C.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

### PURCHASES FROM HERCULES GROUP

The Company purchases supplies in the normal course of business from the Hercules Group. The Company's purchases from Hercules Group were \$44 thousand, \$76 thousand and \$88 thousand in 2001, 2000 and 1999, respectively.

#### 18. NET MEMBERS' (HERCULES GROUP) INVESTMENT

Changes in net Members' (Hercules Group) investment were as follows:

	(Dollars in thousands)
	-----
Balance at January 1, 1999	\$ 309,777
Comprehensive income for the year ended December 31, 1999	16,752
Intercompany transactions, net	(11,831)
	-----
Balance at December 31, 1999	314,698
Comprehensive income for the year ended December 31, 2000	(45,169)
Intercompany transactions, net	1,042
	-----
Balance at December 31, 2000	270,571
Comprehensive income for the year ended December 31, 2001	6,765
Intercompany transactions, net	(23,447)
	-----
Balance at December 31, 2001	\$ 253,889
	=====

The Company includes accumulated other comprehensive income in net Members' Hercules Group investment. At December 31, 2001 and 2000 accumulated other comprehensive income included \$3,625 thousand and \$2,351 thousand, respectively, of foreign currency translation adjustments.

#### 19. INCOME TAXES

## Edgar Filing: HERCULES INC - Form 10-K/A

The domestic and foreign components of income before taxes and effect of change in accounting principle are presented below:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Domestic	\$ (1,016)	\$ (32,803)	\$ 15,495
Foreign	12,617	(20,043)	11,155
	-----	-----	-----
	\$ 11,601	\$ (52,846)	\$ 26,650
	=====	=====	=====

A summary of the components of the tax provision follows:

153

FIBERVISIONS, L.L.C.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Currently payable			
Domestic	\$ 474	\$ 935	\$ 3,376
Foreign	6,350	2,226	3,042
Deferred			
Domestic	1,262	(10,173)	3,413
Foreign	(1,976)	634	964
	-----	-----	-----
Provision (benefit) for income taxes	\$ 6,110	\$ (6,378)	\$ 10,795
	=====	=====	=====

Deferred tax liabilities (assets) at December 31 consist of:

	2001	2000
	-----	-----
Depreciation	\$ 28,120	\$ 34,196
Accrued expenses	--	1,093
Other	9,881	
	-----	-----
Gross deferred tax liabilities	38,001	35,289
	-----	-----
Amortization	\$ (531)	\$ (1,758)

Edgar Filing: HERCULES INC - Form 10-K/A

Inventory	(818)	(2,703)
Bad debts/other accrued	(1,069)	(791)
Impairment of assets	(12,642)	(12,642)
Loss carryforwards	(6,293)	(5,273)
Other comprehensive income	--	1,005
Other	--	(691)
	-----	-----
Gross deferred tax assets	(21,353)	(22,853)
	-----	-----
Valuation allowance	7,668	7,669
	-----	-----
Total deferred income tax	\$ 24,316	\$ 20,105
	=====	=====

A reconciliation of the statutory income tax rate to the effective rate follows:

Statutory income tax rate	35.00%	35.00%	35.00%
Foreign rate differential	(4.87)	(9.39)	1.42
Valuation allowance	0.51	(10.86)	--
Reserves	--	(2.78)	(0.25)
Goodwill	21.49	(4.30)	4.76
Other	0.10	2.44	0.45
State taxes	0.42	0.53	(2.70)
Provision to return true-up		1.44	1.82
	-----	-----	-----
Effective tax rate	52.65%	12.08%	40.50%
	=====	=====	=====

20. RESTATEMENT

The Company has restated it's December 31, 2000 and 1999 financial statements to reflect income tax provisions for both years. During 2002, the Company discovered that it's prior financial statements did not include income tax provisions for its subsidiaries whose income is subject to corporate income taxes at the subsidiary level. Accordingly, the financial statements for December 31, 2000 and 1999 have been restated. The effect of these adjustments on the Company's December 31, 2000 and 1999 financial statements is as follows:

154

FIBERVISIONS, L.L.C.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

-----

	(Dollars in thousands)		
	DECEMBER 31, 2000		DECEMBER 31
	-----		-----
	AS PREVIOUSLY	AS RESTATED	AS PREVIOUSLY
	REPORTED	REPORTED	REPORTED
	-----	-----	-----

BALANCE SHEET

## Edgar Filing: HERCULES INC - Form 10-K/A

Accrued Expenses	\$ 12,542	\$ 12,787	\$ 13,524
Deferred income taxes	--	20,105	--
Net members' investment	290,921	253,889	343,137
Opening net members' investment	343,137	314,698	340,102
 INCOME STATEMENT			
Income before taxes	(52,846)	(52,846)	26,650
Income taxes	--	(6,378)	--
Net income	(52,846)	(46,468)	26,650
 CASHFLOW STATEMENT			
Net income	(52,846)	(46,468)	26,650
Deferred income taxes	--	(9,539)	--
Transfers to/from Hercules Group	(1,683)	2,822	(26,076)
Accounts payable and accrued expenses	(1,792)	(3,084)	4,216

### 21. SUBSEQUENT EVENTS

On April 29, 2002, Hercules completed the sale of its Water Treatment Business to GE Specialty Materials (GESM). Pursuant to the Stock and Asset Agreement for the transaction, the sale included all of the stock of BetzDearborn Inc.. Hercules used the proceeds from the sale to prepay borrowings under its Senior Credit Facility and ESOP Credit Facility. Pursuant to the prepayment, among other things, the stock pledges were released.

155

### REPORT OF INDEPENDENT ACCOUNTANTS

TO THE SHAREHOLDERS AND THE BOARD OF DIRECTORS OF  
HERCULES INCORPORATED  
WILMINGTON, DELAWARE

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income and of cash flows present fairly, in all material respects, the financial position of FiberVisions Products, Inc., a subsidiary of Hercules Incorporated, and its subsidiaries at December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America that require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.



Edgar Filing: HERCULES INC - Form 10-K/A

PricewaterhouseCoopers LLP  
Philadelphia, Pennsylvania  
November 7, 2002

156

FIBERVISIONS PRODUCTS, INC.  
CONSOLIDATED STATEMENTS OF INCOME

	(Dollars in thousands)		
	Year ended December 31		
	2001	2000	1999
Sales to Hercules Group	\$ 25,426	\$ 33,695	\$ 31,013
Cost of sales	24,883	32,108	28,856
Selling, general, and administrative expenses	434	1,037	922
Other operating expenses, net (Note 10)	1,124	1,112	1,125
(Loss) income from operations	(1,015)	(562)	110
Equity income of affiliated companies	3,562	2,057	12,716
Interest expense (income), net (Note 9)	1,032	(143)	1,426
Income before income taxes	1,515	1,638	11,400
Provision for income taxes (Note 12)	944	571	4,049
Net income	\$ 571	\$ 1,067	\$ 7,351

The accompanying notes are an integral part of the consolidated financial statements.

157

FIBERVISIONS PRODUCTS, INC.  
CONSOLIDATED BALANCE SHEET

	(Dollars in thousands)	
	December 31	
	2001	2000
ASSETS		
Current assets		
Cash and cash equivalents	\$ 17	\$ 13
Miscellaneous accounts receivable	1,138	1,703
Receivables from affiliates (Note 3)	1,672	476

Edgar Filing: HERCULES INC - Form 10-K/A

Inventories (Note 4)	1,640	2,053
	-----	-----
Total current assets	4,467	4,245
Property, plant, and equipment, net (Note 7)	34,483	37,640
Investments (Note 5)	21,215	18,140
Goodwill (Note 8)	39,430	40,534
Deferred charges and other assets	11	6
	-----	-----
Total assets	\$ 99,606	\$100,565
	=====	=====
LIABILITIES AND NET HERCULES GROUP INVESTMENT		
Current liabilities		
Accounts payable	\$ 2,707	\$ 3,278
Accrued expenses	--	54
	-----	-----
Total current liabilities	2,707	3,332
Long-term debt - third parties (Note 6)	250	250
Deferred income taxes (Note 12)	6,160	6,920
	-----	-----
Total liabilities	9,117	10,502
Commitments and contingencies (Note 14)	--	--
Net Hercules Group investment (Note 13)	90,489	90,063
	-----	-----
Total liabilities and net Hercules Group investment	\$ 99,606	\$100,565
	=====	=====

The accompanying notes are an integral part of the consolidated financial statements.

158

FIBERVISIONS PRODUCTS, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS

	(Dollars in thousands)		
	Year ended December 31		
	2001	2000	1999
	-----	-----	-----
CASH FLOW FROM OPERATING ACTIVITIES:			
Net income	\$ 571	\$ 1,067	\$ 7,351
Adjustments to reconcile net income to net cash provided from operations:			
Depreciation	3,261	3,128	2,949
Amortization of goodwill	1,104	1,104	1,104
Nonoperating gain on disposals	--	--	53
Corporate and other cost allocations	--	(346)	129
Deferred income taxes	(760)	1,009	4,218
Affiliates' earnings in excess of dividends received	(2,849)	(1,006)	(12,716)
Accruals and deferrals of cash receipts and payments:			
Accounts receivable	565	(516)	702
Receivables from affiliates	(1,422)	(1,933)	--
Transfers to/from Hercules Group	--	(243)	3,504
Inventories	413	(429)	(145)
Accounts payable and accrued expenses	(625)	(783)	2,568

**Edgar Filing: HERCULES INC - Form 10-K/A**

Noncurrent assets and liabilities	(5)	(6)	312
	-----	-----	-----
Net cash provided by operations	253	1,046	10,029
	-----	-----	-----
CASH FLOW FROM INVESTING ACTIVITIES:			
Capital expenditures	(104)	(2,133)	(1,934)
	-----	-----	-----
Net cash used in investing activities	(104)	(2,133)	(1,934)
	-----	-----	-----
CASH FLOW FROM FINANCING ACTIVITIES:			
Transfers to/from Hercules Group	(145)	1,094	(8,095)
	-----	-----	-----
Net cash provided by (used in) financing activities	(145)	1,094	(8,095)
	-----	-----	-----
Net increase in cash and cash equivalents	4	7	--
Cash and cash equivalents at beginning of year	13	6	6
	-----	-----	-----
Cash and cash equivalents at end of year	\$ 17	\$ 13	\$ 6
	=====	=====	=====
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:			
Cash paid during the year for:			
Income taxes, net	\$ 348	\$ --	\$ 353
Noncash financing activities			
Corporate and other cost allocations	--	(346)	129

The accompanying notes are an integral part of the consolidated financial statements.

159

FIBERVISIONS PRODUCTS, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

1. DESCRIPTION OF BUSINESS

FiberVisions Products, Inc. ("Products" or the "Company"), a wholly owned subsidiary of Hercules Incorporated ("Hercules"), serves worldwide markets for polypropylene nonwoven fiber used to make disposable hygiene products. The company was formed on September 26, 1994.

Historically, separate company stand-alone financial statements were not prepared for the Company. In November 2000, Hercules amended its senior credit facility and ESOP credit facility (the "Facilities"). The Facilities, as amended, are secured by liens on Hercules' property and assets (and those of Hercules' Canadian Subsidiaries), a pledge of the stock of substantially all of Hercules' domestic subsidiaries (including FiberVisions Products) and 65% of the stock of foreign subsidiaries directly owned by Hercules, and a pledge of Hercules' domestic intercompany indebtedness. These financial statements present the financial information on the Company, a collateral party to the Hercules debt, based on the Hercules' understanding of Securities and Exchange Commission's interpretation and application of Rule 3-16 under the Securities and Exchange Commission's Regulation S-X. These statements were derived from historical accounting records.

On April 29, 2002, in connection with Hercules' sale of its Water Treatment Business (see Note 17) and the repayment of the Facilities, the stock pledges

## Edgar Filing: HERCULES INC - Form 10-K/A

were released. As a result, based on Hercules' current debt structure, these separate company stand-alone financial statements will not be required for the fiscal year ending December 31, 2002.

The Company participates in Hercules' centralized cash management system. Accordingly, cash received from the Company's operations is transferred to Hercules on a periodic basis, and Hercules funds all operational and capital requirements.

The financial statements of the Company reflect certain allocated support costs incurred by other entities in the Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations and charges included in the Company's financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on factors such as sales, net assets, or cost of sales; or a relative weighting of geographic activity. Management believes that the allocation methods are reasonable.

During 1998, Hercules acquired the Company to make it a wholly owned subsidiary. These financial statements include the push-down of fair value adjustments to assets and liabilities, including goodwill, other intangible assets and property, plant, and equipment and their related amortization and depreciation adjustments.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its majority-owned subsidiaries where control exists. Investments in affiliated companies with a greater than 20% and 50% or less ownership interest are accounted for using the equity method of accounting and, accordingly, consolidated income includes the Company's share of income. All intercompany transactions and profits have been eliminated.

### USE OF ESTIMATES

Preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

### REVENUE RECOGNITION

The company recognizes revenue when the earnings process is complete. This generally occurs when products are shipped to the customer or services are performed in accordance with the terms of the agreement, title and risk of loss have been transferred, collectibility is probable, and pricing is fixed and determinable. Accruals are made for sales returns and other allowances based on the Company's experience. The corresponding shipping and handling costs are included in cost of sales.

## Edgar Filing: HERCULES INC - Form 10-K/A

FIBERVISIONS PRODUCTS, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

### CASH AND CASH EQUIVALENTS

Cash equivalents include commercial paper and other securities with original maturities of 90 days or less. Book value approximates fair value because of the short maturity of those instruments.

### INVENTORIES

Inventories are stated at the lower of cost or market using the average cost method.

### PROPERTY AND DEPRECIATION

Property, plant, and equipment are stated at cost. The company uses the straight-line method of depreciation to depreciate assets over their useful lives. The estimated useful lives of depreciable assets are as follows: buildings - 30 years; plant, machinery and equipment - 15 years; other machinery and equipment - 3 to 15 years.

Maintenance, repairs, and minor renewals are charged to income; major renewals and betterments are capitalized. Upon normal retirement or replacement, the net book value of property (less proceeds of sale or salvage) is charged to income.

### GOODWILL

Goodwill is amortized on a straight-line basis over the estimated future periods to be benefited, generally 40 years.

Pursuant to Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (SFAS 142), beginning January 1, 2002, goodwill will not be amortized but will be tested for impairment annually and any necessary adjustment charged to expense. Intangible assets with finite lives will be amortized over their useful lives.

### IMPAIRMENT OF LONG LIVED ASSETS

The company reviews its long-lived assets, including goodwill and other intangibles, for impairment on an exception basis whenever events or changes in circumstances indicate carrying amounts of the assets may not be recoverable through undiscounted future cash flows. If an impairment loss has occurred based on expected future cash flows (undiscounted), the loss is recognized in the income statement. The amount of the impairment loss is the excess of the carrying amount of the impaired asset over the fair value of the asset. The fair value represents expected future cash flows from the use of the assets, discounted at the rate used to evaluate potential investments.

### CONCENTRATIONS OF CREDIT RISK

Financial instruments that potentially subject the Company to concentration of credit risk consist principally of trade receivables from FiberVisions LP.

### FINANCIAL INSTRUMENTS

The Company uses various non-derivative financial instruments, including letters of credit, and generally does not require collateral to support its financial instruments.

## Edgar Filing: HERCULES INC - Form 10-K/A

### NET HERCULES GROUP INVESTMENT

The net Hercules Group investment account reflects the balance of the Company's historical earnings, intercompany amounts, income tax, and other transactions between FiberVisions Products, Inc. and the Hercules Group.

### INCOME TAXES

The provisions for income taxes has been determined using the asset and liability approach of accounting for income taxes. Under this approach, deferred taxes represent the future tax consequences expected to occur when the reported amounts of assets and liabilities are recovered or paid. The provision for income taxes represents income taxes paid or payable for the current year plus the change in deferred taxes during the year. Deferred taxes result from differences between the financial and tax basis of the Company's assets and liabilities and are adjusted for changes in tax rates and tax laws when changes are enacted. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized.

161

FIBERVISIONS PRODUCTS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

### NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 141, "Business Combinations" ("SFAS 141"), and Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"). SFAS 141 supersedes Accounting Principles Board Opinion ("APB") No. 16, Business Combinations. The provisions of SFAS 141 (1) require that the purchase method of accounting be used for all business combinations initiated after June 30, 2001, (2) provide specific criteria for the initial recognition and measurement of intangible assets apart from goodwill and (3) require that unamortized negative goodwill be written off immediately as extraordinary gain instead of being deferred and amortized. SFAS 141 also requires that upon adoption of SFAS 142 the Company reclassify the carrying amounts of certain intangible assets into or out of goodwill, based on certain criteria. SFAS 142 supersedes APB No. 17, Intangible Assets, and is effective for fiscal years beginning after December 15, 2001. SFAS 142 primarily addresses the accounting for goodwill and intangible assets subsequent to their initial recognition. The provisions of SFAS 142 (1) prohibit the amortization of goodwill and indefinite-lived intangible assets, (2) require that goodwill and indefinite-lived intangible assets be tested annually for impairment (and in interim periods if certain events occur indicating that the carrying value of goodwill and/or indefinite-lived intangible assets may be impaired), based on fair value (as opposed to cost recovery using future undiscounted cash flows), (3) require that reporting units be identified for the purpose of assessing potential future impairments of goodwill and (4) remove the forty-year limitation on the amortization period of intangible assets that have finite lives.

Effective January 1, 2002, Hercules adopted the provisions of SFAS 142. Hercules identified the following reporting units: BetzDearborn, Pulp and Paper, Aqualon, FiberVisions and Resins. In connection with Hercules' transitional review recorded goodwill was determined to be impaired in the BetzDearborn and FiberVisions reporting units. In the first quarter 2002, Hercules completed its transitional impairment review of the identified reporting units and recognized an after-tax impairment loss of \$368 million as a cumulative effect of a change in accounting principle, of which \$87 million related to the FiberVisions

## Edgar Filing: HERCULES INC - Form 10-K/A

reporting unit. As a result of Hercules' adoption of SFAS 142, the Company will no longer record \$1.1 of annual amortization relating to existing goodwill and intangibles, as adjusted for the reclassifications just mentioned.

Goodwill was evaluated for impairment at December 31, 2001 under Statement of Financial Accounting Standards No. 121 "Accounting for the Impairment of Long-Fixed Assets and for Long-Lived Assets to Be Disposed of". Such evaluations indicated that goodwill associated with the business was recoverable from anticipated future undiscounted cash flows. Accordingly, no impairment loss was recorded in the December 31, 2001 financial statements.

In June 2001, the Financial Accounting Standards Board ("FASB") approved the issuance of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143"). SFAS 143 establishes accounting standards for the recognition and measurement of legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 will become effective for the Company on January 1, 2003 and requires recognition of a liability for an asset retirement obligation in the period in which it is incurred. The Company does not believe it will have a material effect on its financial statements.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company does not believe it will have a material effect on its financial statements.

162

FIBERVISIONS PRODUCTS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

-----  
In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment to FASB Statement No. 13, and Technical Corrections." The Company elected to early adopt the provisions of SFAS 145 related to the rescission of SFAS 4, "Reporting Gains and Losses from the Extinguishment of Debt" ("SFAS 4"). The early adoption had no effect on the Company's financial statements.

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146"). SFAS 146 addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs in a Restructuring)". SFAS 146 defines the timing of the recognition of costs associated with exit or disposal activities, the types of costs that may be recognized and the methodology for calculating the fair value of such costs. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. The Company does not believe this statement will have a material effect on its financial statements.

### RECLASSIFICATIONS

Certain amounts in the 2000 and 1999 consolidated financial statements and notes have been reclassified to conform to the 2001 presentation.

FIBERVISIONS PRODUCTS, INC.  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

3. RECEIVABLES FROM AFFILIATES

Trade receivables from affiliates, consists of \$3,355 thousand and \$1,933 thousand due from ES FiberVisions for years then ended December 31, 2001 and 2000, respectively, and net of \$1,683 and \$1,457 of accumulated losses of unconsolidated companies in excess of investment for years 2001 and 2000, respectively (see Note 5).

4. INVENTORIES

The components of inventories are:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Finished products	\$ 420	\$ 766
Raw materials	1,220	1,254
Work in process	--	33
	-----	-----
Total	\$1,640	\$2,053
	=====	=====

5. INVESTMENTS

The equity investments in affiliated companies consist of:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Investment in FiberVisions, LP	\$21,215	\$18,140
	=====	=====

In 1998, Products entered into a 50% joint venture with Fibervisions Inc. Products and FiberVisions Inc. manufacture products for the joint venture, FiberVisions LP, under a manufacturing agreement. Products' share of the net income was \$3,090 thousand, \$2,463 thousand and \$12,716 thousand in 2001, 2000, and 1999, respectively.

On January 1, 2000 Products and Chisso Polypro Fiber Co., Ltd formed a 50/50 joint venture, ES FiberVisions, combining their bicomponent fibers businesses outside of Japan. While Products has a 50% equity interest, it's share of joint venture operations is 67%. Both parent companies supply fiber to the joint venture under manufacturing agreements. Products manufactures bicomponent fibers for the joint venture at its Varde, Denmark and Athens, Georgia locations. The annual sales of the venture were approximately \$55 million and \$48 million in fiscal 2001 and 2000, respectively. Products share of net income (loss) was \$472



## Edgar Filing: HERCULES INC - Form 10-K/A

thousand and (\$406) thousand in 2001 and 2000, respectively.

Summarized financial information for the equity affiliates at December 31, and the years then ended is as follows:

164

FIBERVISIONS PRODUCTS, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

	(Dollars in thousands)		
	2001	2000	
	----	----	
Current assets	\$ 26,566	\$ 33,023	
Non Current assets	22,133	9,335	
Current liabilities	6,206	6,476	
			1999
			----
Net sales	\$136,703	\$164,714	\$150,450
Gross profit	9,309	8,397	27,730
Net earnings	6,885	4,305	25,432

The investments are partnerships which require the associated tax benefit or expense to be recorded by the Company.

### 6. LONG TERM DEBT - THIRD PARTY

In December 1996 the Company entered into a long-term lease purchase obligation with The Athens-Clark County Industrial Development Authority to purchase land. The interest rate is fixed at 1% per annum and the due date of the obligation is December 2020. The balance of the obligation was \$250 thousand at December 31, 2001 and 2000.

### 7. ADDITIONAL BALANCE SHEET DETAIL

	(Dollars in thousands)	
	2001	2000
	-----	-----
Property, plant, and equipment		
Land	\$ 430	\$ 430
Buildings and equipment	45,704	45,703
Construction in progress	4,785	4,682
	-----	-----
Total	50,919	50,815
Accumulated depreciation and amortization	(16,436)	(13,175)
	-----	-----
Net property, plant, and equipment	\$ 34,483	\$ 37,640
	=====	=====

### 8. GOODWILL

At December 31, 2001 and 2000, the goodwill was:

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousands)	
	2001	2000
	-----	-----
Goodwill	\$ 43,290	\$ 43,290
Less accumulated amortization	(3,860)	(2,756)
	-----	-----
Net goodwill and other intangible assets	\$ 39,430	\$ 40,534
	=====	=====

In July 1998, Hercules Inc. completed the acquisition of 49% share of FiberVisions L.L.C. owned by its joint venture partner, Jacob Holm & Son A/S, for approximately \$230 million in cash, plus assumed debt of \$188 million. The allocation of the purchase price resulted in \$188,051 thousands of goodwill for the FiberVisions group, which is being amortized over its estimated useful life of 40 years. \$43,290 thousands of the goodwill was assigned to FiberVisions Products, Inc.

165

FIBERVISIONS PRODUCTS, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

9. INTEREST (INCOME) EXPENSE

Interest costs are summarized as follows:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Interest expense	\$ 2,265	\$ 2,201	\$ 2,311
Interest income	(1,233)	(2,344)	(885)
	-----	-----	-----
Interest (income) expense, net	\$ 1,032	\$ (143)	\$ 1,426
	=====	=====	=====

10. OTHER OPERATING EXPENSES (INCOME), NET

Other operating expenses (income), net, consists of the following:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Goodwill and intangible amortization	\$1,104	\$1,104	\$1,104
Miscellaneous expense, net	20	8	21
	-----	-----	-----
	\$1,124	\$1,112	\$1,125
	=====	=====	=====

## Edgar Filing: HERCULES INC - Form 10-K/A

### 11. LONG TERM DEBT AND OTHER FINANCING ARRANGEMENTS

Hercules manages the Company's cash and indebtedness. The majority of the cash provided by or used by the Company is provided through this consolidated cash and debt management system. As a result, the amount of domestic cash or debt historically related to the Company is not determinable. For the purposes of the Company's historical financial statements all of its positive or negative cash flows have been treated as cash transferred to or from its parent.

The Company has an intercompany loan with the Hercules Group in the amount of \$37,720 thousand and \$34,280 thousand which is included in the net Hercules Group investment balance at December 31, 2001 and 2000, respectively. In 2001 and 2000 interest was charged on the intercompany loans based on the stated rate of 6.5%. The loan is payable upon demand.

The Company also has an intercompany receivable with the Hercules Group in the amount of \$18,926 thousand and \$16,258 thousand which is included in the net Hercules Group investment balance at December 31, 2001 and 2000, respectively. At December 31, 2001 and 2000 the weighted average interest rate on the intercompany borrowings was 7.6% and 7.4%, respectively.

166

FIBERVISIONS PRODUCTS, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

### 12. INCOME TAXES

A summary of the components of the tax provision follows:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Current (Domestic)	\$ --	\$ (438)	\$ (169)
Deferred (Domestic)	944	1,009	4,218
	-----	-----	-----
Provision for income taxes	\$ 944	\$ 571	\$ 4,049
	=====	=====	=====

Deferred tax liabilities (assets) at December 31 consist of:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Depreciation	\$ 9,302	\$ 9,369
Gross deferred tax liabilities	9,302	9,369
	-----	-----
Inventory	\$ --	\$ (154)
Accrued expenses	(226)	(152)
Loss carryforwards	(2,329)	(1,309)

Edgar Filing: HERCULES INC - Form 10-K/A

Amortization	(472)	(412)
Other	(115)	(422)
	-----	-----
Gross deferred tax assets	(3,142)	(2,449)
	-----	-----
Total deferred income taxes	\$ 6,160	\$ 6,920
	=====	=====

A reconciliation of the statutory income tax rate to the effective rate follows:

	2001	2000	1999
	-----	-----	-----
Statutory income tax rate	35.00%	35.00%	35.00%
Rate differential adjustment	--	--	2.46
Goodwill	25.50	30.00	3.39
State taxes	1.73	2.30	0.69
Reserves	--	(30.71)	--
Other	0.07	(1.72)	(6.03)
	-----	-----	-----
Effective tax rate	62.30%	34.87%	35.51%
	-----	-----	-----

167

FIBERVISIONS PRODUCTS, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

13. NET HERCULES GROUP INVESTMENT

Changes in net Hercules Group investment were as follows:

	(Dollars in thousands)
	-----
Balance at January 1, 1999	\$ 85,603
Net loss for the year ended December 31, 1999	7,351
Intercompany transactions, net	(4,463)
	-----
Balance at January 1, 2000	\$ 88,491
Net loss for the year ended December 31, 2000	1,067
Intercompany transactions, net	505
	-----
Balance at December 31, 2000	90,063
Net loss for the year ended December 31, 2001	571
Intercompany transactions, net	(145)
	-----
Balance at December 31, 2001	\$ 90,489
	=====

## Edgar Filing: HERCULES INC - Form 10-K/A

### 14. COMMITMENTS AND CONTINGENCIES

The Company has operating leases (storage space and data processing equipment) expiring at various dates. Rental expense was \$22 thousand, \$14 thousand, and \$10 thousand in 2001, 2000, and 1999, respectively.

The net minimum future payments at December 31, 2001 are as follows:

	(Dollars in thousands)	
	-----	
2002	\$	7
2003		2
		-----
Total	\$	9
		=====

2004 and thereafter the net minimum future payments are zero.

The Company currently and from time to time is involved in litigation incidental to the conduct of its business. In the opinion of the Company's management, none of such litigation as of December 31, 2001 is likely to have a material adverse effect on the financial position, results of operations, or cash flows of the Company.

### 15. PENSION, OTHER POSTRETIREMENT BENEFITS AND OTHER BENEFITS

The Company participates in a defined benefit pension plan sponsored by Hercules, Inc. ("Hercules") which covers substantially all employees of Hercules in the U.S. Benefits under this plan are based on the average final pay and years of service. Hercules also provides postretirement health care and life insurance benefits to eligible retired employees and their dependents.

Information on the actuarial present value of the benefit obligation and fair value of the plan assets is not presented as Hercules manages its U.S. employee benefit plans on a consolidated basis and such information is not maintained separately for the U.S. employees of the Company. The Company's statement of operation includes an allocation of the costs of the U.S. benefits plans. The pension costs were allocated based on percentage of pensionable wages, for each of the years presented, postretirement benefit costs were allocated using factors derived from the relative net assets and revenues. Net pension expense (income) of Hercules allocated to the Company was (\$112) thousand, (\$129) thousand, and \$0 for the years ended December 31, 2001, 2000, and 1999, respectively.

168

FIBERVISIONS PRODUCTS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

-----

FiberVisions Products, Inc. maintains a 401(k) savings plan for its full-time employees in North America. Each participant in the plan may elect to contribute 1 % to 15 % of his or her annual salary to the plan subject to statutory limitations. The company matches employee contributions to the plan at the rate of 50% of the first 6% of salary contributed. The Company's matching contribution was \$59 thousand, \$69 thousand, and \$79 thousand for 2001, 2000, and 1999, respectively.

16. RELATED PARTY TRANSACTIONS

The Company has entered into certain agreements with affiliated entities. These agreements were developed in the context of parent/subsidiary relationship and therefore may not necessarily reflect the result of arm-length negotiations between independent parties. The terms of the agreements provide for the sale of product to the affiliated entities based on a cost-plus formula.

CORPORATE AND OTHER ALLOCATIONS

As discussed in Note 1, the financial statements of the Company reflect certain allocated support costs incurred by other entities in Hercules group. These costs include executive, legal, accounting, human resources, tax, auditing, cash management, purchasing, safety, information management, health and environmental, investor relations and other corporate services. Allocations and charges included in the Company's financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; or a percentage allocation for such services provided based on factors such as revenues, net assets, cost of sales and relative weighting of geographic activity. These allocations are reflected in the selling, general and administrative line item in our statement of operations. In addition, the company allocates certain of it's own costs to other companies in the FiberVisions group of companies. Such allocations and corporate charges totaled (\$346) thousand, and \$129 thousand in 2000 and 1999, respectively.

SALES TO HERCULES GROUP

The Company sells fiber in the normal course of business to the Hercules Group. Company's revenues from sales to the Hercules Group were \$25,426 thousand, \$33,695 thousand, and \$31,013 thousand in 2001, 2000, and 1999, respectively.

PURCHASES FROM HERCULES GROUP

The Company purchases supplies in the normal course of business from the Hercules Group. The Company's purchases from Hercules Group were \$9 thousand, \$7 thousand, and \$8 thousand in 2001, 2000, and 1999, respectively.

17. SUBSEQUENT EVENTS

On April 29, 2002, Hercules completed the sale of its Water Treatment Business to GE Specialty Materials (GSM). Pursuant to the Stock and Asset Agreement for the transaction, the sale included all of the stock of BetzDearborn Inc.. Hercules used the proceeds from the sale to prepay borrowings under its Senior Credit Facility and ESOP Credit Facility. Pursuant to the prepayment, among other things, the stock pledges were released.

## Edgar Filing: HERCULES INC - Form 10-K/A

TO THE SHAREHOLDERS AND THE BOARD OF DIRECTORS OF  
HERCULES INCORPORATED  
WILMINGTON, DELAWARE

In our opinion, the accompanying balance sheets and the related statements of operations and comprehensive (loss) income and of cash flows present fairly, in all material respects, the financial position of Hercules Canada, Inc., a subsidiary of Hercules Incorporated, at December 31, 2001 and 2000 and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP  
Mississauga, Ontario

January 25, 2002, except for note 2, New accounting pronouncements, and note 10, Subsequent event, which are as of November 8, 2002

170

HERCULES CANADA, INC.  
Statements of Operations and Comprehensive (Loss) Income

		(thousands of U	
		Year ended De	
		2001	
		-----	-----
Equity in income of affiliated company (note 3)	\$	1,726	\$
Interest and debt expense (note 9)		(993)	
Interest income (note 9)		34	
Other income (expense) - net		82	
		-----	-----
Income before income taxes		849	
Provision for income taxes (note 7)		1,753	
		-----	-----
Net (loss) income		(904)	
Translation adjustments		(408)	
		-----	-----
Comprehensive (loss) income	\$	(1,312)	\$
		=====	=====

Edgar Filing: HERCULES INC - Form 10-K/A

The accompanying accounting policies and notes are an integral part of the financial statements.

171

HERCULES CANADA, INC.  
Balance Sheets

-----		
		(t)
		-----
ASSETS		
Current assets		
Cash and cash equivalents	\$	
Income taxes receivable		-----
Total current assets		
Investment (note 3)		-----
Total assets	\$	=====
LIABILITIES AND NET HERCULES GROUP INVESTMENT		
Current liabilities		
Accrued expenses	\$	-----
Total current liabilities		-----
Deferred income taxes (note 7)		-----
Total liabilities		-----
Contingencies (note 8)		
Net Hercules Group investment (note 6)		
Accumulated other comprehensive loss		(1
Intercompany transactions (note 5)		1
Total net Hercules Group investment		-----
Total liabilities and net Hercules Group investment	\$	=====



## Edgar Filing: HERCULES INC - Form 10-K/A

The accompanying accounting policies and notes are an integral part of  
the financial statements.

172

HERCULES CANADA, INC.  
Statements of Cash Flows

		(thousands of U	
		Year ended De	
		2001	
		-----	-----
<b>CASH FLOW FROM OPERATING ACTIVITIES:</b>			
Net (loss) income	\$	(904)	\$
Adjustments to reconcile net income to net cash provided from operations			
Equity in income (loss) of affiliated company - net of withdrawals from partnership equity		4,798	
Deferred income taxes		(686)	
Accruals and deferrals of cash receipts and payments			
Income taxes receivable		438	
Accrued expenses		(339)	
Transfer to Hercules Group		83	
Net cash provided by (used in) operations		----- 3,390	-----
<b>CASH FLOW FROM FINANCING ACTIVITIES:</b>			
Transfers (to) from Hercules Group		(2,655)	
(Decrease) increase in bank overdraft		-	
Net cash (used in) provided by financing activities		----- (2,655)	-----
<b>CASH FLOW FROM INVESTING ACTIVITIES:</b>			
Withdrawals from equity in partnership in excess of earnings		-	
Effect of exchange rate changes on cash and cash equivalents		31	
Net increase in cash and cash equivalents		766	
Cash and cash equivalents - Beginning of year		33	
Cash and cash equivalents - End of year	\$	799	\$
		=====	=====
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>			
Cash paid during the year for:			
Interest	\$	2,396	\$
Income taxes		3,296	

## Edgar Filing: HERCULES INC - Form 10-K/A

The accompanying accounting policies and notes are an integral part of the financial statements.

173

HERCULES CANADA, INC.  
Notes to Financial Statements

---

### 1 DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

Hercules Canada, Inc. (HCI or the Company) is a holding company, which is a partner in Hercules Canada Partnership (HCP). The majority partner in HCP is BetzDearborn Canada, Inc. (BDCI), which is an affiliated company under common control of Hercules Incorporated (Hercules). HCI is owned 100% by Hercules.

Historically, separate company stand-alone financial statements were not prepared for HCI. In November 2000, Hercules amended its senior credit facility and ESOP credit facility (the Facilities). The Facilities, as amended, were secured by liens on Hercules' property and assets (and those of Hercules' Canadian subsidiaries, including HCI), a pledge of the stock and partnership and member interests of substantially all of Hercules' U.S. subsidiaries and 65% of the stock of non-U.S.A. subsidiaries directly owned by Hercules, including HCI, and a pledge of Hercules' U.S.A. intercompany indebtedness. These financial statements present the financial information on HCI, a collateral party to the Hercules debt, based on Hercules' understanding of the Securities and Exchange Commission's interpretation and application of Rule 3-16 under the Securities and Exchange Commission's Regulation S-X. These statements were derived from historical accounting records.

On April 29, 2002, in connection with Hercules' sale of its Water Treatment Business (note 10) and the repayment of the Facilities, the stock pledges were released. As a result, based on Hercules' current debt structure, these separate company stand-alone financial statements will not be required for the fiscal year ending December 31, 2002.

As a result of the global Hercules acquisition of BetzDearborn Inc. on October 15, 1998, Hercules initiated a global process of internal reorganization, for which the Company entered into an agreement with BDCI to transfer its business to a newly created partnership, Hercules Canada Partnership. The Company has a 28.09% share of future profits from the partnership. Since this reorganization is under the common control of Hercules, the transactions have been accounted for in a manner similar to a pooling of interest.

### 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### INVESTMENTS

Investments in affiliated companies with a 20% to 50% ownership interest are accounted for using the equity method of accounting and, accordingly, net income includes HCI's share of the income of HCP. All intercompany transactions and profits have been eliminated.

#### USE OF ESTIMATES

Preparation of financial statements in conformity with generally accepted

## Edgar Filing: HERCULES INC - Form 10-K/A

accounting principles in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

174

HERCULES CANADA, INC.  
Notes to Financial Statements

---

### CASH AND CASH EQUIVALENTS

Cash equivalents include commercial paper and other securities with original maturities of 90 days or less. Book value approximates fair value because of the short maturity of those instruments.

### FOREIGN CURRENCY TRANSLATION AND TRANSACTIONS

The accompanying financial statements are reported in U.S. dollars. The Canadian dollar is the functional currency for HCI. The translation of the functional currency into U.S. dollars (reporting currency) is performed for assets and liabilities using the current exchange rates in effect at the balance sheets dates, and for revenues, costs and expenses using average exchange rates prevailing during the reporting periods. Adjustments resulting from the translation of functional currency financial statements to reporting currency are accumulated and reported as other comprehensive (loss) income, a component of net Hercules Group investment.

Transactions in foreign currency are recorded at the exchange rate prevailing on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are expressed in the functional currency at the exchange rates in effect at the balance sheets dates. Revenues, costs and expenses are recorded using average exchange rates prevailing during the reporting periods. Gains or losses resulting from foreign currency transactions are included in the statements of operations.

### NET HERCULES GROUP INVESTMENT

The net Hercules Group investment account reflects the balance of HCI's historical earnings, intercompany amounts, foreign currency translation and other transactions between HCI and the Hercules Group.

### INCOME TAXES

The provisions for income taxes have been determined using the asset and liability approach of accounting for income taxes. Under this approach, deferred taxes represent the future tax consequences expected to occur when the reported amounts of assets and liabilities are recovered or paid. The provision for income taxes represents income taxes paid or payable for the current year, plus the change in deferred taxes during the year. Deferred taxes result from differences between the financial and tax basis of the Company's assets and liabilities and are adjusted for changes in tax rates and tax laws when changes are enacted. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized.

175

## Edgar Filing: HERCULES INC - Form 10-K/A

HERCULES CANADA, INC.  
Notes to Financial Statements

---

### NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, the FASB approved the issuance of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" (SFAS 143). SFAS 143 establishes accounting standards for the recognition and measurement of legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 will become effective for the Company on January 1, 2003 and requires recognition of a liability for an asset retirement obligation in the period in which it is incurred. The Company does not believe it will have a material effect on its financial statements.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" (SFAS 144). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company does not believe it will have a material effect on its financial statements.

### 3 INVESTMENT

The investment in HCP is accounted for on the equity basis. As this investment is a partnership, the associated tax benefit or expense is recorded by its parent companies. The amount of retained earnings in the Company that represents undistributed earnings of HCP is \$nil (2000 - \$nil). During 2001, the Company received a distribution of \$6,524 thousand (2000 - \$7,904 thousand).

Summarized financial information for this equity affiliate at December 31 and for the years then ended is as follows:

	(thousands of U.S. dollars)	
	2001	
Current assets	\$ 43,449	\$
Non-current assets	286,249	
	-----	-----
Total assets	\$ 329,698	\$
	=====	=====
Current liabilities	\$ 38,286	\$
	=====	=====
Net sales	\$ 149,824	\$
Gross profit	62,882	
Net earnings	6,151	

HERCULES CANADA, INC.  
Notes to Financial Statements

---

## Edgar Filing: HERCULES INC - Form 10-K/A

### 4 BANK OVERDRAFT

Bank borrowings represent primarily overdraft facilities and short-term lines of credit, which are generally payable on demand with interest at various rates. Book values of bank borrowings approximate market value because of their short maturity period.

At December 31, 2001, HCI had \$3,131 thousand (2000 - \$3,309 thousand) of unused lines of credit that may be drawn as needed, with interest at a negotiated spread over lenders' cost of funds. Weighted average interest rates on short-term borrowings at December 31, 2001 and 2000 were nil%. All lines of credit are payable in Canadian funds.

### 5 INTERCOMPANY NOTE PAYABLE AND OTHER FINANCING ARRANGEMENTS

HCI has an intercompany loan with the Hercules Group in the amount of \$12,522 thousand and \$15,882 thousand, which is included in the net Hercules Group investment balance as of December 31, 2001 and 2000, respectively. The loan is denominated in Canadian dollars, is due on demand and bears interest at 10%.

### 6 NET HERCULES GROUP INVESTMENT

Changes in net parent investment were as follows:

	(thousands of dollars)
Balance - January 1, 1999	\$ 1
Net income	
Other comprehensive income	
Intercompany transactions - net	
	-----
Balance - January 1, 2000	1
Net income	
Other comprehensive loss	
Intercompany transactions - net	
	-----
Balance - December 31, 2000	1
Net loss	
Other comprehensive loss	
Intercompany transactions - net	
	-----
Balance - December 31, 2001	\$
	=====

The Company includes accumulated comprehensive income or loss in net Hercules Group investment. At December 31, 2001 and 2000, accumulated other comprehensive loss included a cumulative loss of \$10,568 thousand and a cumulative loss of \$10,160 thousand, respectively, of foreign currency translation adjustments.

Edgar Filing: HERCULES INC - Form 10-K/A

7 INCOME TAXES

A summary of the components of the tax provision follows:

	(thousands of U.S. Dollars)	
	Year ended December 31, 2001	
	2001	
	-----	-----
Current	\$ 2,439	\$
Deferred	(686)	
	-----	-----
Provision for income taxes	\$ 1,753	\$
	=====	=====

The deferred tax liability at December 31 is comprised of:

	(thousands of U.S. Dollars)
	-----
Accrued expenses of HCP	\$
Gross deferred tax assets	
Depreciation of HCP	
Prepaid pension and post-retirement benefits of HCP	
Other	
	-----
Gross deferred tax liabilities	
	-----
Total deferred income tax liability	\$
	=====

A reconciliation of the statutory income tax rate to the effective rate is as follows:

	2001
	-----
Statutory income tax rate	40.62%
Goodwill amortization of HCP	105.41
Non-deductible expenses	6.51
Other	53.93
	-----
Effective tax rate	206.47%
	=====

## Edgar Filing: HERCULES INC - Form 10-K/A

### 8 CONTINGENCIES

The Company, currently and from time to time, is involved in litigation incidental to the conduct of its business. In the opinion of the Company's management, none of such litigation as of December 31, 2001 is likely to have a material adverse effect on the financial position, results of operations, or cash flows of the Company.

178

HERCULES CANADA, INC.  
Notes to Financial Statements

---

### 9 RELATED PARTY TRANSACTIONS

In the year 2001, HCI incurred interest expense of \$993 thousand (2000 - \$1,021 thousand; 1999 - \$311 thousand) on its intercompany loan with the Hercules Group. In 2001, HCI also earned interest income of \$34 thousand (2000 - \$136 thousand; 1999 - \$nil) on its note receivable with the Hercules Group.

### 10 SUBSEQUENT EVENT

On April 29, 2002, Hercules completed the sale of its Water Treatment Business to GE Specialty Materials. Pursuant to the Stock and Asset Agreement for the transaction, the sale included all of the stock of BetzDearborn and the partnership interest of the Company. Hercules used the proceeds from the sale to prepay borrowings under its Senior Credit Facility and ESOP Credit Facility. Pursuant to the prepayment, among other things, the stock pledges were released.

179

### REPORT OF INDEPENDENT ACCOUNTANTS

To the Shareholders and the Board of Directors of  
Hercules Incorporated  
Wilmington, Delaware

In our opinion, the accompanying balance sheets and the related statements of income and comprehensive income and cash flows present fairly, in all material respects, the financial position of Hercules Chemicals (Taiwan) Co., Limited, a subsidiary of Hercules Incorporated, at November 30, 2001 and 2000, and the results of its operations and its cash flows for each of the three years in the period ended November 30, 2001, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers

Edgar Filing: HERCULES INC - Form 10-K/A

Taipei, Taiwan, Republic of China  
November 13, 2002

180

HERCULES CHEMICALS (TAIWAN) CO., LIMITED  
STATEMENTS OF INCOME and COMPREHENSIVE INCOME

	(Dollars in thousands)	
	2001	2000
	-----	-----
SALES TO THIRD PARTIES	\$ 27,727	\$ 27,467
SALES TO HERCULES GROUP	2,402	2,373
	-----	-----
	30,129	29,840
COST OF SALES	(15,822)	(15,801)
SELLING, GENERAL, AND ADMINISTRATIVE EXPENSES	(7,468)	(8,235)
GOODWILL AMORTIZATION	(358)	(419)
ROYALTY EXPENSE	(1,886)	(1,852)
	-----	-----
PROFIT FROM OPERATIONS	4,595	3,533
OTHER EXPENSE, NET (NOTE 8)	(10)	(286)
	-----	-----
INCOME BEFORE INCOME TAXES	4,585	3,247
PROVISION FOR INCOME TAXES (NOTE 10)	(913)	(949)
	-----	-----
NET INCOME	3,672	2,298
TRANSLATION ADJUSTMENTS, NET OF TAX	(703)	(1,051)
	-----	-----
COMPREHENSIVE INCOME	\$ 2,969	\$ 1,247
	=====	=====

The accompanying notes are an integral part of the financial statements.

181

HERCULES CHEMICALS (TAIWAN) CO., LIMITED  
BALANCE SHEET

	(Dollars in thousand)	
	November 30,	
	2001	2000
	-----	-----
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 983	\$ 466
Notes receivable	532	1,038
Accounts receivable, net (Note 3)	5,987	5,400
Inventories (Note 4)	2,747	3,600
Deferred income taxes (Note 10)	702	448
Other current assets	439	451
	-----	-----



Edgar Filing: HERCULES INC - Form 10-K/A

Total current assets	11,390	11,403
Property, plant and equipment, net (Note 5)	5,717	3,088
Goodwill, net (Note 12)	13,720	14,926
Deferred income taxes (Note 10)	453	425
Deferred charges	286	2,733
Other assets	2,832	2,809
	-----	-----
TOTAL ASSETS	\$ 34,398	\$ 35,384
	=====	=====
LIABILITIES AND NET HERCULES GROUP INVESTMENT		
Current Liabilities		
Short term debt and borrowings (Note 6)	\$ --	\$ 2,923
Accounts payable	1,358	1,099
Accrued expenses (Note 7)	1,395	3,252
Other current liabilities	986	784
	-----	-----
Total current liabilities	3,739	8,058
	-----	-----
Total liabilities	3,739	8,058
	-----	-----
Commitment and contingencies (Note 13)	--	--
Net Hercules Group Investment (Note 16)		
Accumulated other comprehensive income	(1,517)	(814)
Intercompany transactions, net	32,176	28,140
	-----	-----
Net Hercules Group Investment	30,659	27,326
	-----	-----
TOTAL LIABILITIES AND NET HERCULES GROUP INVESTMENT	\$ 34,398	\$ 35,384
	=====	=====

The accompanying notes are an integral part of the financial statements.

182

HERCULES CHEMICALS (TAIWAN) CO., LIMITED.  
STATEMENTS OF CASH FLOWS

	(Dollars in thou Year Ended Novemb	
	2001	2000
	-----	-----
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 3,672	\$ 2,298
Adjustments to reconcile net income to net cash provided from operations		
Depreciation	624	536
Amortization	358	419
Provision for bad debts	53	118
(Gain)loss on disposal of fixed assets	(25)	(47)
Corporate and other cost allocations	1,303	941
Accruals and deferrals of cash receipts and payments:		
Notes receivable	464	7
Accounts receivable	(1,110)	112
Inventories	710	(925)
Prepaid pension expense	--	124

Edgar Filing: HERCULES INC - Form 10-K/A

Other current assets	(6)	82
Deferred tax assets	21	(200)
Accounts payable	(57)	--
Accrued expense	(1,693)	578
Other current liabilities	232	662
Other liabilities	--	--
Transfers to/from Hercules Group	(236)	(177)
	-----	-----
NET CASH PROVIDED BY OPERATING ACTIVITIES	4,310	4,528
	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditure	(976)	(397)
Proceeds from disposal of fixed assets	87	165
Deposit	(273)	(6)
Goodwill Adjustment	270	--
Deferred charges	26	(2,408)
	-----	-----
NET CASH USED IN INVESTING ACTIVITIES	(866)	(2,646)
	-----	-----
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of short-term notes	--	704
Repayment of short-term notes loan	(638)	(4,060)
Increase in commercial paper payable	(2,166)	1,280
Transfers to/from Hercules Group	--	--
	-----	-----
NET CASH USED IN FINANCING ACTIVITIES	(2,804)	(2,076)
	-----	-----
EFFECT OF EXCHANGE RATE CHANGES ON CASH	(123)	364
	-----	-----
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	517	170
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	466	296
	-----	-----
CASH AND CASH EQUIVALENTS AT END OF YEAR	\$ 983	\$ 466
	=====	=====
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
CASH PAID DURING THE YEAR FOR:		
Interests	\$ 78	\$ 238
Income tax, net	1,272	266
NON CASH INVESTING AND FINANCING ACTIVITIES		
Corporate and other cost allocations	\$ 1,303	\$ 941
Reversal of restructuring reserve, net of tax	270	--

The accompanying notes are an integral part of the financial statements.

183

HERCULES CHEMICALS (TAIWAN) CO., LIMITED  
NOTES TO FINANCIAL STATEMENTS

1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

The Company

Hercules Chemicals (Taiwan) Co., Limited (the "Company"), a wholly-owned

## Edgar Filing: HERCULES INC - Form 10-K/A

subsidiary of Hercules Incorporated ("Hercules"), was incorporated in the Republic of China (ROC) on March 16, 1984. The Company is primarily engaged in the manufacturing and distribution of chemicals, including specialty chemicals and equipment for industrial and waste water treatments, and the provision of related engineering services in ROC.

Historically, separate company stand-alone financial statements were not prepared for the Company. In November 2000, Hercules amended its senior credit facility and ESOP credit facility (the "Facilities"). The Facilities, as amended, are secured by liens on Hercules' property and assets (and those of Hercules' Canadian Subsidiaries), a pledge of the stock and partnership and member interests of substantially all of Hercules' domestic subsidiaries and 65% of the stock of foreign subsidiaries including the companies directly owned by Hercules, and a pledge of Hercules' domestic intercompany indebtedness. These financial statements present the financial information on the Company, a collateral party to the Hercules' debt, based on the Hercules's understanding of Securities and Exchange Commission's interpretation and application of Rule 3-16 under the Securities and Exchange Commission's Regulation S-X. These statements were derived from historical accounting records.

On April 29, 2002, in connection with Hercules' sale of its Water Treatment Business (see Note 17) and the repayment of the Facilities, the stock pledges were released. As a result, based on Hercules' current debt structure, these separate company stand-alone financial statements will not be required for the fiscal year ending November 30, 2002.

When Hercules acquired all of the outstanding shares of BetzDearborn Inc on October 15, 1998, it paid \$2,235 million in cash and \$186 million in common stock in exchange for the shares held by the BetzDearborn ESOP Trust. As a result of this acquisition, the Company, as a part of an effort by Hercules, entered into an internal reorganization transaction during 1999 and 2000. The transaction included merging BetzDearborn Taiwan Ltd. into the Company. As this reorganization is under the common control of Hercules, this transaction has been accounted for in a manner similar to pooling of interest.

184

### HERCULES CHEMICALS (TAIWAN) CO., LIMITED NOTES TO FINANCIAL STATEMENTS

The purchase price allocated to the Company was approximately \$20 million. During 1999, Hercules completed the purchase price allocation and the final determination of goodwill was \$2,170 million of which the amount attributable to the Company was approximately \$16 million. These financial statements include the push down of fair value adjustments to assets and liabilities, including goodwill, other intangible assets and property, plant and equipment and their related amortization and depreciation adjustments.

The Company participates in Hercules' centralized cash management system. Accordingly, cash received from the Company operations is transferred to Hercules on a periodic basis, and Hercules funds all operational and capital requirements.

The financial statements of the Company reflect certain allocated support costs incurred by other entities in the Hercules Group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations

## Edgar Filing: HERCULES INC - Form 10-K/A

and charges included in the Company's financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on factors such as sales, net assets, or cost of sales; or a relative weighting of geographic activity. Management believes that the allocation methods are reasonable.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### Use of Estimates

The preparation of financial statements in accordance with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that effect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

#### Cash and Cash Equivalents

Cash equivalents include cash in banks and certificates of deposit with original maturities of 90 days or less. Book value approximates fair value because of the short maturity of those instruments.

185

### HERCULES CHEMICALS (TAIWAN) CO., LIMITED NOTES TO FINANCIAL STATEMENTS

#### Foreign currency translation and transactions

The accompanying financial statements are reported in U.S. dollars. The New Taiwan dollar is the functional currency for the Company. The translation of the functional currencies into U.S. dollars (reporting currency) is performed for assets and liabilities using the current exchange rates in effect at the balance sheet date, and for revenues, costs and expenses using average exchange rates prevailing during the reporting periods. Adjustments resulting from the translation of functional currency financial statements to reporting currency are accumulated and reported as other comprehensive income, a separate component of Net Hercules Group Investment.

Transactions in foreign currency are recorded at the exchange rate prevailing on the date of transaction. Monetary assets and liabilities denominated in foreign currencies are expressed in the functional currency at the exchange rates in effect at the balance sheet date. Gains or losses resulting from foreign currency transactions are included in the statement of income.

#### Financial instruments

The Company uses various non-derivative financial instruments, including letters of credit, and generally does not require collateral to support its financial instruments.

#### Inventories

Inventories are stated at the lower of cost or market value. Inventories are valued at standard cost which approximates the average cost.

HERCULES CHEMICALS (TAIWAN) CO., LIMITED  
NOTES TO FINANCIAL STATEMENTS

Property and depreciation

Property, plant and equipment are stated at cost and depreciated using straight-line method. The estimated useful lives of depreciable assets are as follows: building and improvement - 5 to 30 years; machinery and equipment - 5 to 15 years; other equipment - 3 to 15 years.

Maintenance, repairs and minor renewals are charged to income; major renewals and betterments are capitalized. Upon normal retirement or replacement, the net book value of property (less proceeds of sale or salvage) is expensed.

Goodwill

Goodwill is amortized on a straight-line basis over 40 years, the estimated future period to be benefited. Pursuant to Statement of Financial Accounting Standards No. 142 "Goodwill and Other Intangible Asset," ("SFAS 142"), beginning January 1, 2002, goodwill will not be amortized but will be tested for impairment annually and any necessary adjustment will be charged to expense. Intangible assets with finite lives will be amortized over their useful lives.

Long-Lived assets

The company reviews its long-lived assets, including goodwill for impairment on an exception basis whenever events or changes in circumstances indicate the carrying amounts of the assets may not be recoverable through undiscounted future cash flows. If an impairment loss has occurred based on expected future cash flows (undiscounted), the loss is recognized in the income statement. The amount of the impairment loss is the excess of the carrying amount of the impaired asset over the fair value of the asset. The fair value represents expected future cash flows from the use of the assets, discounted at the rate used to evaluate potential investments.

Deferred Charges

Deferred charges include construction-in-progress costs primarily consisting of fixed assets not yet placed in use. Once the projects are completed, the assets are reclassified to property, plant and equipment and are depreciated there in accordance with the Company's policy. Generally, these assets are held in deferred charges for no longer than one year.

Revenue recognition

The Company recognizes revenue when the earning process is complete. This generally occurs when products are shipped to the customer or services are performed in accordance with the terms of the agreement, title and risk of loss have been transferred, collectibility is probable, and pricing is

## Edgar Filing: HERCULES INC - Form 10-K/A

fixed and determinable. Accruals are made for sales returns and other allowances based on the Company's experience. The corresponding shipping and handling costs are included in cost of sales.

### Environmental expenditures

Environmental expenditures that pertain to current operations or future revenues are expensed or capitalized according to the Company's capitalization policy.

### Income Taxes

Income tax expense in the accompanying financial statements has been computed assuming the Company filed separate income tax returns.

The provisions for income taxes have been determined using the asset and liability approach of accounting for income taxes. Under this approach, deferred taxes represent the future tax consequences expected to occur when the reported amounts of assets and liabilities are recovered or paid. The provision for income taxes represents income taxes paid or payable for the current year plus the change in deferred taxes during the year. Deferred taxes result from differences between the financial and tax basis of the Company's assets and liabilities and are adjusted for changes in tax rates and tax laws when changes are enacted. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized.

### Stock-based Compensation

Compensation costs attributable to stock option and similar plans are recognized based on any excess of the quoted market price of the stock on the date of grant over the amount the employee is required to pay to acquire the stock (the intrinsic-value method under Accounting Principles Board Opinion 25 (APB 25)). Such amount, if any, is accrued over the related vesting period, as appropriate. Statement of Financial Accounting Standard No. 123, "Accounting for Stock-based Compensation," requires companies electing to continue to use the intrinsic-value method to make pro forma disclosures of net income as if the fair-value-based method of accounting had been applied.

### Concentrations of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist

188

## HERCULES CHEMICALS (TAIWAN) CO., LIMITED NOTES TO FINANCIAL STATEMENTS

principally of cash and cash equivalent, notes receivable and accounts receivable. The cash and cash equivalents are deposited with various well-known domestic and foreign financial institutions. Therefore, the concentration risk is limited. Concentrations of credit risk with respect to notes receivable and accounts receivable are limited due to the Company's large number of customers and their dispersion across many different industries and locations.

### Net Hercules Group Investment

The Net Hercules Group Investment account reflects the balance of the

## Edgar Filing: HERCULES INC - Form 10-K/A

Company's historical earnings, intercompany amounts, foreign currency translation and other transactions between the Company and the Hercules Group.

### New accounting Pronouncements

In June 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 141, "Business Combinations" ("SFAS 141"), and Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"). SFAS 141 supersedes Accounting Principles Board Opinion ("APB") No. 16, Business Combinations. The provisions of SFAS 141 (1) require that the purchase method of accounting be used for all business combinations initiated after June 30, 2001, (2) provide specific criteria for the initial recognition and measurement of intangible assets apart from goodwill and (3) require that unamortized negative goodwill be written off immediately as extraordinary gain instead of being deferred and amortized. SFAS 141 also requires that upon adoption of SFAS 142 the Company reclassify the carrying amounts of certain intangible assets into or out of goodwill, based on certain criteria. SFAS 142 supersedes APB No. 17, Intangible Assets, and is effective for fiscal years beginning after December 15, 2001. SFAS 142 primarily addresses the accounting for goodwill and intangible assets subsequent to their initial recognition. The provisions of SFAS 142 (1) prohibit the amortization of goodwill and indefinite-lived intangible assets, (2) require that goodwill and indefinite-lived intangible assets be tested annually for impairment (and in interim periods if certain events occur indicating that the carrying value of goodwill and/or indefinite-lived intangible assets may be impaired), based on fair value (as opposed to cost recovery using future undiscounted cash flows), (3) require that reporting units be identified for the purpose of assessing potential future impairments of goodwill and (4) remove the forty-year limitation on the amortization period of intangible assets that have finite lives.

189

### HERCULES CHEMICALS (TAIWAN) CO., LIMITED NOTES TO FINANCIAL STATEMENTS

Effective January 1, 2002 Hercules adopted the provisions of SFAS 142. Hercules identified the following reporting units: BetzDearborn, Pulp and Paper, Aqualon and FiberVisions. In connection with Hercules' transitional review, recorded goodwill was determined to be impaired in the BetzDearborn reporting unit. In the first quarter 2002, Hercules completed its transitional impairment review of the identified reporting units and recognized an after tax impairment loss of \$368 million as a cumulative effect of a change in accounting principle. As a result of Hercules' adoption of SFAS 142, the Company will no longer record \$358 thousand of annual amortization relating to existing goodwill and intangibles.

Goodwill related to the BetzDearborn business was evaluated for impairment at November 30, 2001 under Statement of Financial Accounting Standards No. 121 "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed of". Such evaluation indicated that goodwill associated with the business was recoverable from anticipated future undiscounted cash flows. Accordingly, no impairment loss was recorded in the November 30, 2001 financial statements.

In June 2001, the Financial Accounting Standards Board ("FASB") approved the issuance of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143"). SFAS 143

## Edgar Filing: HERCULES INC - Form 10-K/A

establishes accounting standards for the recognition and measurement of legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 will become effective for the Company on January 1, 2003 and requires recognition of a liability for an asset retirement obligation in the period in which it is incurred. The Company does not believe this statement will have a material effect on its financial statements.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company does not believe this statement will have a material effect on its financial statements.

In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment to FASB Statement No. 13, and Technical Corrections." The Company has elected to early adopt the provisions of SFAS 145 related to the rescission of SFAS 4, "Reporting Gains and Losses from the Extinguishment of Debt" ("SFAS 4"). The early adoption of SFAS 145 had no effect on the Company's financial statements.

190

### HERCULES CHEMICALS (TAIWAN) CO., LIMITED NOTES TO FINANCIAL STATEMENTS

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146"). SFAS 146 addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs in a Restructuring)". SFAS 146 defines the timing of the recognition of costs associated with exit or disposal activities, the types of costs that may be recognized and the methodology for calculating the fair value of such costs. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. The Company does not believe this statement will have a material effect on its financial statements.

#### Reclassifications

Certain accounts presented in the year ended November 30, 2000 financial statements have been reclassified to conform with presentation adopted for the year ended November 30, 2001.

191

### HERCULES CHEMICALS (TAIWAN) CO., LIMITED NOTES TO FINANCIAL STATEMENTS

#### 3. ACCOUNTS RECEIVABLE, NET

The accounts receivable, net, consists of:



Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousands)	
	2001	2000
	-----	-----
Trade	\$ 6,192	\$ 5,567
Less: Allowance for doubtful accounts	(205)	(167)
	-----	-----
Total	\$ 5,987	\$ 5,400
	=====	=====

4. INVENTORIES

The components of inventories are:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Finished goods	\$ 884	\$1,396
Raw materials and supplies	1,434	1,564
Goods in transit	429	640
	-----	-----
Total	\$2,747	\$3,600
	=====	=====

5. PROPERTY, PLANT, AND EQUIPMENT

	(Dollars in thousands)	
	2001	2000
	-----	-----
Buildings and improvements	\$ 2,714	\$ 1,271
Machinery and equipment	6,652	5,208
Other equipment	697	841
	-----	-----
	10,063	7,320
Less: Accumulated depreciation	(4,346)	(4,232)
	-----	-----
Total	\$ 5,717	\$ 3,088
	=====	=====

192

HERCULES CHEMICALS (TAIWAN) CO., LIMITED  
NOTES TO FINANCIAL STATEMENTS

Depreciation expense for the years ended November 30, 2001, 2000 and 1999 amounted to \$624 thousand, \$536 thousand and \$440 thousand, respectively.

6. SHORT TERM DEBT

At November 30, 2000, the Company has an outstanding balance of \$665 thousand on advances on the Company's \$6.5 million revolving bank

## Edgar Filing: HERCULES INC - Form 10-K/A

facility. The facility, guaranteed by Hercules, bears floating interest rates ranging from 6.61% to 12% during 2000.

Commercial papers-short term, which are guaranteed by CitiBank and Hong Kong Shanghai Bank bearing an interest rate of 5% at November 30, 2000, are as follows:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Commercial papers payable	\$ --	\$ 2,267
Less: unamortized discount	--	(9)
	-----	-----
Total	\$ --	\$ 2,258
	=====	=====

The Company paid off all of its short-term debt during 2001.

### 7. ACCRUED EXPENSES

	(Dollars in thousands)	
	2001	2000
	-----	-----
Other accrued expenses	\$ 493	\$1,010
Payroll and employee benefits	693	1,199
Restructuring reserves	195	593
Accrued royalty expenses	14	450
	-----	-----
Total	\$1,395	\$3,252
	=====	=====

### 8. OTHER EXPENSES, NET

Other income (expenses), net consist of the following:

193

## HERCULES CHEMICALS (TAIWAN) CO., LIMITED NOTES TO FINANCIAL STATEMENTS

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Interest expense	(\$ 75)	(\$256)	(\$202)
Foreign exchange gain	66	11	2
Interest income	3	9	10
Other (expenses) income	(4)	(50)	6
	-----	-----	-----
Total	(\$ 10)	(\$286)	(\$184)

Edgar Filing: HERCULES INC - Form 10-K/A

=====

194

HERCULES CHEMICALS (TAIWAN) CO., LIMITED  
NOTES TO FINANCIAL STATEMENTS

9. RETIREMENT BENEFITS

The Company has a non-contributory defined benefit plan covering all of its employees in ROC. The Company funds the plan through trust arrangements where the assets of the fund are held separately from the employer. The level of funding is in line with local practice and in accordance with the local tax and supervisory requirements. The following table lists benefit obligations, plan assets, and funded status of the plans:

	(Dollars in thousands)	
	2001	2000
	-----	-----
CHANGE IN BENEFIT OBLIGATION		
Benefit obligation at December 1	\$ 2,665	\$ 2,854
Service cost	298	289
Interest cost	148	157
Benefits paid	(621)	(489)
Actuarial loss	675	--
Translation adjustments	(115)	(146)
	-----	-----
Benefit obligation at November 30	\$ 3,050	\$ 2,665
	=====	=====
CHANGE IN PLAN ASSETS		
Fair value of plan assets at December 1	\$ 2,069	\$ 2,381
Actual return on plan assets	101	144
Company contributions	217	122
Benefits paid	(621)	(464)
Translation adjustments	(76)	(114)
	-----	-----
Fair value of plan assets at November 30	\$ 1,690	\$ 2,069
	=====	=====

195

HERCULES CHEMICALS (TAIWAN) CO., LIMITED  
NOTES TO FINANCIAL STATEMENTS

Funded status of the plan	(\$1,360)	(\$ 596)
Unrecognized net loss	667	540
Unrecognized net transition obligation	488	--
	-----	-----

Edgar Filing: HERCULES INC - Form 10-K/A

Accrued benefit cost	(\$ 205)	(\$ 55)
	=====	=====

ASSUMPTIONS AS OF NOVEMBER 30

Weighted-average discount rate	5%	6%
Expected return on plan assets	5%	6%
Rate of compensation increase	5%	6%

COMPONENTS OF NET PERIOD PENSION COST	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Service cost	\$ 298	\$ 289	\$ 24
Interest cost	148	157	14
Expected return on plan assets	(105)	(144)	(10)
Amortization of net loss	--	--	2
Amortization of transition obligation (asset)	31	34	(1)
	-----	-----	-----
Benefit cost	\$ 372	\$ 336	\$ 28
	=====	=====	=====

196

HERCULES CHEMICALS (TAIWAN) CO., LIMITED  
NOTES TO FINANCIAL STATEMENTS

10. INCOME TAXES

A summary of the components of the tax provision is as follows:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Current	\$ 980	\$ 807	\$ 11
Deferred	(67)	142	204
	-----	-----	-----
Provision for income taxes	\$ 913	\$ 949	\$ 215
	=====	=====	=====

Deferred tax assets consist of the following:

	(Dollars in thousands)	
	2001	2000
	----	----
Current items:		
Unrealized expenses	\$ 62	\$151
Unrealized foreign exchange loss	598	269
Allowance for doubtful accounts	42	28

Edgar Filing: HERCULES INC - Form 10-K/A

	-----	-----
	\$702	\$448
	=====	=====
Non-current items:		
Depreciation	\$388	\$333
Deferred pension cost	65	92
	-----	-----
	\$453	\$425
	=====	=====

A reconciliation of the ROC statutory income tax rate to the effective rate is as follows:

	2001	2000	1999
	-----	-----	-----
Statutory income tax rate	32%	32%	32%
Non-deductible amortization of goodwill	1%	1%	5%
Overaccrual for prior year's income tax	(2%)	--	--
Non-deductible meals and entertainment	--	1%	8%
Investment tax credit	(13%)	--	(5%)
Other	2%	(5%)	(6%)
	----	----	----
Effective tax rate	20%	29%	34%
	====	====	====

197

HERCULES CHEMICALS (TAIWAN) CO., LIMITED  
NOTES TO FINANCIAL STATEMENTS

11. RELATED PARTY TRANSACTIONS

The Company has entered into certain agreements with affiliated entities. These agreements were developed in the context of parent/subsidiary relationship and therefore may not necessarily reflect the result of arms-length negotiations between independent parties. The Company records sales with affiliates based on a cost-plus formula developed and agreed-upon by both parties.

CORPORATE AND OTHER ALLOCATIONS

As discussed in Note 1, the financial statements of the Company reflect certain allocated support costs incurred by other entities in the Hercules Group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, research and development overhead, investor relations and other corporate services. Allocations and charges included in the Company's financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on factors such as revenues, net assets, costs of sales or a relative weighting of geographic activity. These allocations are reflected in the selling, general and administrative line item in our statement of operations. Such allocations and corporate charges totaled \$1,303 thousand,

## Edgar Filing: HERCULES INC - Form 10-K/A

\$941 thousand, and \$1,241 thousand in 2001, 2000, and 1999, respectively.

### ROYALTY EXPENSES

The Company has an intellectual property license agreement with Hercules under which the Company agreed to pay royalties on a basis rested on certain percentages of the net sales of licensed products. The agreement expires in December 2004. Royalty expenses were \$1,886 thousand, \$1,852 thousand and \$1,286 thousand for the years ended November 30, 2001, 2000 and 1999,

198

### HERCULES CHEMICALS (TAIWAN) CO., LIMITED NOTES TO FINANCIAL STATEMENTS

respectively.

### SALES TO AFFILIATES

The Company sells paper and water treatment chemicals in the normal course of business to affiliated companies. Company's revenues from sales to affiliated companies were \$2,402 thousand, \$2,373 thousand and \$1,199 thousand in 2001, 2000 and 1999, respectively.

### PURCHASES FROM AFFILIATES

The Company purchases raw materials and resale products for paper and water treatment chemicals in the normal course of business to affiliated companies. Company's expenses from purchases from affiliated companies were \$6,407 thousand, \$8,338 thousand and \$5,557 thousand in 2001, 2000 and 1999, respectively.

## 12. GOODWILL

Goodwill relates to the Hercules' 1998 purchase of BDTL. At November 30, 2001 and 2000, goodwill was \$13,720 thousand and \$14,926 thousand, respectively, (net of accumulated amortization of \$1,206 thousand and \$890 thousand, respectively). The amortization period for goodwill is 40 years. A reconciliation of activities with related to goodwill is as follows:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Balance at beginning of year	\$ 14,926	\$ 16,167
Amortization	(358)	(419)
Reversal of restructuring reserve, net of tax	(270)	--
Translation adjustment	(578)	(822)
	-----	-----
Balance at end of year	\$ 13,720	\$ 14,926
	=====	=====

## 13. COMMITMENTS AND CONTINGENCIES

### LEASES

## Edgar Filing: HERCULES INC - Form 10-K/A

The Company has operating leases (including office space, transportation, and data processing equipment) expiring at various dates. Rental expense was \$486 thousand in 2001, \$307 thousand in 2000, and \$230 thousand in 1999.

199

### HERCULES CHEMICALS (TAIWAN) CO., LIMITED NOTES TO FINANCIAL STATEMENTS

At November 30, 2001, minimum rental payments under noncancelable leases aggregated \$146 thousand, which will be paid in 2002.

#### 14. RESTRUCTURING

Pursuant to the plans in place to merge the operations of BDTL with the Company and to rationalize the support infrastructure and other existing operations, 22 employees (21 related to the 1998 BDTL acquisition) were terminated and one facility was closed during 2000. Cash payments during 2000 amounted to \$375 thousands for severance benefits and \$15 thousands for other exit costs. In 1998, the Company incurred restructuring liabilities of \$1,347 thousands in connection with the acquisition of BDTL (see Note 1). These liabilities included charges of \$723 thousands for employee termination benefits and \$624 thousands for exit costs related to facility closures. The restructuring liability was charged to goodwill as part of the purchase price allocation related to the acquisition of BDTL. During the second and third quarter 2001, Hercules completed a global assessment of remaining expenditures for the 1998 BetzDearborn plan. As a result, the estimate for severance was lowered by \$344 thousand with an offsetting reduction to goodwill and deferred taxes assets of \$270 thousand and \$74 thousand, respectively.

Severance benefits payments are based on years of service and generally continue for 3 months to 24 months subsequent to termination. We expect to substantially complete remaining actions under the plans in 2001. A reconciliation of activity with respect to the liabilities established for these plans is as follows:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Balance at beginning of year	\$ 569	\$ 983
Cash payments	(30)	(390)
Reversal of restructuring reserve	(344)	--
	-----	-----
Balance at end of year	\$ 195	\$ 593
	=====	=====

200

### HERCULES CHEMICALS (TAIWAN) CO., LIMITED NOTES TO FINANCIAL STATEMENTS

#### 15. STOCK COMPENSATION

The Company participates in long-term incentive compensation plans sponsored by Hercules. These plans provide for the grant of stock options and the award of common stock and other market-based units to certain key employees and non-employee directors.

## Edgar Filing: HERCULES INC - Form 10-K/A

In 1995, Hercules changed the structure of the long-term incentive compensation plans to place a greater emphasis on shareholder value creation through grants of regular stock options, performance-accelerated stock options, and Cash Value Awards (performance-based awards denominated in cash and payable in shares of common or restricted stock, subject to the same restrictions as restricted stock). Restricted stock and other market-based units are awarded with respect to certain programs. The number of awarded shares outstanding was 189,704 at December 31, 2001, and 491,488 and 926,689 at December 31, 2000 and 1999, respectively.

At December 31, 2001, under Hercules' incentive compensation plans, 1,265,493 shares of common stock were available for grant as stock awards or stock option awards. Stock awards are limited to approximately 15% of the total authorizations. Regular stock options are granted at the market price on the date of grant and are exercisable at various periods from one to five years after date of grant. Performance-accelerated stock options are also granted at the market price on the date of grant and are normally exercisable at nine and one-half years. Exercisability may be accelerated based upon the achievement of predetermined performance goals. Both regular and performance-accelerated stock options expire 10 years after the date of grant.

Restricted shares, options and performance-accelerated stock options are forfeited and revert to Hercules in the event of employment termination, except in the case of death, disability, retirement, or other specified events.

The Company applies APB Opinion 25 in accounting for its plans. Accordingly, no compensation cost has been recognized for the stock option plans. There were no charges to income for the cost of stock awards over the restriction or performance period for 2001, 2000 and 1999, respectively.

201

### HERCULES CHEMICALS (TAIWAN) CO., LIMITED NOTES TO FINANCIAL STATEMENTS

Below is a summary of outstanding stock option grants under the incentive compensation plans during 1999, 2000 and 2001:

	Regular	
	Number of Shares	Weighted-average price
December 31, 1998	6,600	\$40.38
Granted	7,650	\$37.74
Exercised	--	--
Forfeited	--	--
December 31, 1999	14,250	\$38.96
Granted	--	--
Exercised	--	--
Forfeited	--	--
December 31, 2000	14,250	\$38.96
Granted	--	--
Exercised	--	--
Forfeited	--	--



Edgar Filing: HERCULES INC - Form 10-K/A

December 31, 2001	----- 14,250	\$38.96
-------------------	-----------------	---------

There were no performance-accelerated stock options granted or outstanding during 1999, 2000 and 2001.

The weighted-average fair value of regular stock options granted during 1999, 2000 and 2001 was \$8.26, \$0 and \$0, respectively.

Following is a summary of regular stock options exercisable at December 31, 1999, 2000, and 2001, and their respective weighted-average share prices:

Options Exercisable	Number of Shares	Weighted-average exercise price
-----		
December 31, 1999	5,000	\$39.97
December 31, 2000	9,520	\$39.42
December 31, 2001	12,720	\$39.11

Following is a summary of stock options outstanding at December 31, 2001:

Exercise Price Range	Outstanding Options			Number Exercisable 12/31/2001
	Number Outstanding at 12/31/2001	Weighted-average Remaining Contractual Life	Weighted- average exercise price	
-----				
Regular Stock Options				
\$30 - \$40	13,550	6.58	\$38.50	12,020
\$40 - \$50	700	6.35	\$47.81	700
	----- 14,250			----- 12,720
-----				

The Company employees may also participate in the Hercules Employee Stock Purchase Plan ("ESSP"). The ESSP is a qualified non-compensatory plan, which allows eligible employees to acquire shares of common stock through systematic payroll deductions. The plan consists of three-month subscription periods, beginning July 1 of each year. The purchase price is 85% of the fair market value of the common stock on either the first or last day of that subscription period, whichever is lower. Purchases

## Edgar Filing: HERCULES INC - Form 10-K/A

may range from 2% to 15% of an employee's base salary each pay period, subject to certain limitations. Currently, there are no shares of Hercules common stock registered for offer and sale under the plan. Shares issued at December 31, 2001 and 2000, were 1,758,081 and 1,597,861, respectively. The Company applies APB Opinion 25 and related interpretations in accounting for its Employee Stock Purchase Plan. Accordingly, no compensation cost has been recognized for the Employee Stock Purchase Plan.

Had compensation cost for Hercules' Stock-Based Incentive Plans and Employee Stock Purchase Plan been determined on the basis of fair value according to SFAS No. 123, the fair value of each option granted or share purchased would be estimated on the grant date using the Black-Scholes option pricing model.

The following weighted-average assumptions would be used in estimating fair value for 2001, 2000 and 1999:

Assumption -----	Regular Plan -----	Performance Accelerated Plan -----	Emplo Purch -----
Dividend yield	0.96%	3.83%	
Risk-free interest rate	5.80%	5.57%	
Expected life	7.1 yrs.	5 yrs.	
Expected volatility	33.36%	29.78%	

The Company's net income and earnings per share for 2001, 2000 and 1999 would approximate the pro forma amounts below:

	(Dollars in thousands)		
	2001 ----	2000 ----	1999 ----
Net income			
As reported	\$3,672	\$2,298	\$ 415
Pro forma	\$3,659	\$2,277	\$ 395

203

### HERCULES CHEMICALS (TAIWAN) CO., LIMITED NOTES TO FINANCIAL STATEMENTS

#### 16. NET HERCULES GROUP INVESTMENT

Changes in Net Hercules Group Investment were as follows:

	(Dollars in thousands)
Balance, December 1, 1998	27,027
Net income	415
Other comprehensive income, (net of tax of \$182)	547
Intercompany transaction, net	(2,723)

## Edgar Filing: HERCULES INC - Form 10-K/A

Balance, November 30, 1999	25,266
Net income	2,298
Other comprehensive income, (net of tax of \$334)	(1,002)
Intercompany transaction, net	764
	-----
Balance, November 30, 2000	27,326
Net income	2,969
Other comprehensive income, (net of tax of \$326)	(703)
Intercompany transaction, net	1,067
	-----
Balance, November 30, 2001	\$ 30,659
	=====

The Company includes accumulated other comprehensive income in net parent investment. At November 30, 2001 and 2000, accumulated other comprehensive income consisted of foreign currency translation adjustments only.

### 17. SUBSEQUENT EVENTS NOTE

On April 29, 2002, Hercules completed the sale of its Water Treatment Business to GE Specialty Materials (GESM). Pursuant to the Stock and Asset Agreement ("SAPA") for the transaction, the sale was executed using the stock of BetzDearborn, Inc and all of the assets, liabilities, and/or equity interests relating to the Water Treatment Business. Pursuant to the SAPA, the Company sold its Water Treatment Business assets to GESM. Hercules used the proceeds from the sale to repay borrowings under its Senior Credit Facility.

204

November 15, 2002

### REPORT OF INDEPENDENT ACCOUNTANTS

TO THE SHAREHOLDERS AND THE BOARD OF DIRECTORS OF  
HERCULES INCORPORATED  
WILMINGTON, DELAWARE

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income and of cash flows present fairly, in all material respects, the financial position of Hercules Credit, Inc., a subsidiary of Hercules Incorporated, and its subsidiaries at December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and

## Edgar Filing: HERCULES INC - Form 10-K/A

disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP  
Philadelphia, Pennsylvania  
November 13, 2002

205

HERCULES CREDIT, INC.  
CONSOLIDATED STATEMENTS OF INCOME

	(Dollars in thousands)		
	Year Ended December 31,		
	2001	2000	1999
	-----	-----	-----
Sales to third parties	\$ 255,285	\$ 274,775	\$ 295,473
Sales to Hercules Group	49,359	63,033	62,657
	-----	-----	-----
	304,644	337,808	358,130
Cost of sales third parties	204,127	227,272	250,066
Selling, general, and administrative expenses	51,529	50,599	57,745
Research and development	12,708	11,780	12,078
Goodwill and intangible asset amortization	1,014	1,014	1,014
Other operating (income) expenses, net (Note 12)	(2,129)	22,259	3,554
	-----	-----	-----
Profit from operations	37,395	24,884	33,673
Equity Income in affiliated companies	9,088	9,423	7,358
Interest and debt expense	(58)	(417)	(547)
Other income (expense), net	2,617	1,468	(903)
	-----	-----	-----
Income before income taxes and minority interest	\$ 49,042	\$ 35,358	\$ 39,581
Provision for income taxes (Note 13)	19,985	14,241	15,707
	-----	-----	-----
Income before minority interest	\$ 29,057	\$ 21,117	\$ 23,874
Minority interest	(243)	(164)	(215)
	-----	-----	-----
Net income	\$ 28,814	\$ 20,953	\$ 23,659
	=====	=====	=====

The accompanying accounting policies and notes are an integral part of the consolidated financial statements.

206

HERCULES CREDIT, INC.  
CONSOLIDATED BALANCE SHEETS

-----

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousands)	
	December 31,	
	2001	2000
	-----	-----
ASSETS		
Current assets		
Cash and cash equivalents	\$ 5,683	\$ 2,592
Accounts receivable, net (Note 3)	30,924	35,743
Notes receivable (Note 4)	--	3,600
Inventories (Note 5)	39,340	45,409
Other current assets	4,204	4,691
	-----	-----
Total current assets	80,151	92,035
	-----	-----
Property, plant, and equipment, net (Note 7)	94,722	92,229
Notes receivable (Note 4)	3,000	3,000
Investments (Note 8)	98,499	93,046
Goodwill and other intangible assets, net (Note 9)	27,536	28,550
Deferred charges and other assets	3,140	5,382
	-----	-----
Total assets	\$307,048	\$314,242
	=====	=====
LIABILITIES AND NET HERCULES GROUP INVESTMENT		
Current liabilities		
Accounts payable	\$ 14,354	\$ 17,724
Taxes Payable	39,824	33,660
Accrued expenses (Note 7)	26,844	25,590
	-----	-----
Total current liabilities	81,022	76,974
Deferred income taxes (Note 13)	8,957	7,720
Pension and other postretirement benefits (Note 11)	--	110
Environmental and other liabilities	26,661	32,863
	-----	-----
Total liabilities	116,640	117,667
Commitments and contingencies (Note 16)	--	--
Minority Interest	4,044	3,800
Net Hercules Group Investment (Note 14)		
Net Hercules Group Investment	186,364	192,775
	-----	-----
Total Net Hercules Group Investment	186,364	192,775
	-----	-----
Total liabilities and Net Hercules Group Investment	\$307,048	\$314,242
	=====	=====

The accompanying accounting policies and notes are an integral part of the consolidated financial statements.

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousands)		
	Year Ended December 31,		
	2001	2000	1999
	-----	-----	-----
<b>CASH FLOW FROM OPERATING ACTIVITIES:</b>			
Net Income	\$ 28,814	\$ 20,953	\$ 23,659
Adjustments to reconcile net income to net cash provided from operations:			
Depreciation	9,236	9,861	11,131
Amortization	1,014	1,014	1,014
Loss on disposal (Note 15)	--	6,854	6,500
Loss on impairment of fixed assets (Note 12)	--	--	2,000
Deferred Income Taxes	1,237	1,659	(7,906)
Minority Loss	243	164	215
Corporate and other cost allocations	19,296	17,569	25,148
Affiliates' earnings in excess of dividends received	(9,088)	(9,423)	(7,358)
Accruals and deferrals of cash receipts and payments:			
Accounts receivable and other assets	8,905	10,103	4,523
Inventories	6,069	7,084	5,112
Accounts payable and accrued expenses	7,661	(16,324)	258
Environmental and other assets and liabilities	(4,084)	(827)	2,410
Net cash provided by operations	69,303	48,687	66,706
	-----	-----	-----
<b>CASH FLOW FROM INVESTING ACTIVITIES:</b>			
Capital expenditures	(11,729)	(9,437)	(12,133)
Investment in affiliate	38	(179)	254
Net cash used in investing activities	(11,691)	(9,616)	(11,879)
	-----	-----	-----
<b>CASH FLOW FROM FINANCING ACTIVITIES:</b>			
Repayment of debt		(1,650)	--
Transfers to Hercules Group	(54,521)	(36,762)	(57,115)
Net cash used in financing activities	(54,521)	(38,412)	(57,115)
	-----	-----	-----
Net increase (decrease) in cash and cash equivalents	3,091	659	(2,288)
Cash and cash equivalents at beginning of year	2,592	1,933	4,221
Cash and cash equivalents at end of year	\$ 5,683	\$ 2,592	\$ 1,933
	=====	=====	=====
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>			
Cash paid during the year for:			
Interest paid	58	\$ 417	\$ 547
Income taxes paid	\$ 12,583	\$ 23,614	\$ 22,697
Noncash financing activities			
Issuance of note receivable	3,000	6,600	--
Corporate and other cost allocations	19,296	17,569	25,148

The accompanying accounting policies and notes are an integral part of the consolidated financial statements.

## Edgar Filing: HERCULES INC - Form 10-K/A

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

#### 1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

Hercules Credit, Inc., ("Credit" or the "Company") is a U.S. holding company which owns 99.4182% of Aqualon Company ("Aqualon") and 20% of Hercules Finance. Credit, Aqualon and Hercules Finance are wholly owned subsidiaries of Hercules Incorporated (Hercules).

Historically, separate company stand-alone financial statements were not prepared for Credit. In November 2000, Hercules amended its senior credit facility and ESOP credit facility (the "facilities"). The facilities, as amended, are secured by liens on Hercules' property and assets (and those of Hercules' Canadian Subsidiaries), a pledge of the stock of substantially all of Hercules' domestic subsidiaries (including Hercules Credit) and 65% of the stock of foreign subsidiaries directly owned by Hercules, and a pledge of Hercules' domestic intercompany indebtedness. These financial statements present the financial information on Credit, a collateral party to the Hercules debt, based on Hercules' understanding of Securities and Exchange Commission's interpretation and application of Rule 3-16 under the Securities and Exchange Commission's Regulation S-X. These statements were derived from historical accounting records.

On April 29, 2002, in connection with Hercules' sale of its Water Treatment Business (see Note 18) and the repayment of the Facilities, the stock pledges were released. As a result, based on Hercules' current debt structure, these separate company stand-alone financial statements will not be required for the fiscal year ending December 31, 2002.

As an operating division of Hercules, Credit participates in Hercules' centralized cash management system. Accordingly, cash received from Credit's operations is transferred to Hercules on a periodic basis, and Hercules funds all operational and capital requirements.

The financial statements of Credit reflect certain allocated support costs incurred by other entities in the Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations and charges included in Credit's financial statements were based on either a direct cost pass-through for items directly identified as related to Credit's activities; a percentage allocation for such services provided based on factors such as sales, net assets, or cost of sales; or a relative weighting of geographic activity. Management believes that the allocation methods are reasonable.

#### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

##### PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of Credit and its' subsidiary, Aqualon. All intercompany transactions and profits have been eliminated. Investments in affiliated companies with a greater than 20% and less than 50% ownership interest are accounted for using the equity method of accounting and, accordingly, consolidated income includes Hercules Credit's share of their income.

##### USE OF ESTIMATES

Preparation of financial statements in conformity with generally accepted

## Edgar Filing: HERCULES INC - Form 10-K/A

accounting principles in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

### REVENUE RECOGNITION

The Company recognizes revenue when the earnings process is complete. This generally occurs when products are shipped to the customer or services are performed in accordance with terms of the agreement, title and risk of loss have been transferred, collectibility is probable, and pricing is fixed and determinable. Accruals are made for sales returns and other allowances based on Credit's experience. The corresponding shipping and handling costs are included in cost of sales.

### ENVIRONMENTAL EXPENDITURES

Environmental expenditures that pertain to current operations or future revenues are expensed or capitalized according to Credit's capitalization policy, which is to charge repairs and maintenance to earnings and capitalize replacements or betterments. Expenditures for remediation of an existing condition caused by past operations that do not contribute to current or future revenues are expensed. Liabilities are recognized for remedial activities when the cleanup is probable and can be reasonably estimated.

209

HERCULES CREDIT, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

### CASH AND CASH EQUIVALENTS

Cash equivalents include commercial paper and other securities with original maturities of 90 days or less. Book value approximates fair value because of the short maturity of those instruments.

### INVENTORIES

Inventories are stated at the lower of cost or market. Inventories are valued at standard cost which approximates the average cost method.

### PROPERTY AND DEPRECIATION

Property, plant, and equipment are stated at cost and depreciated using the straight-line method. The estimated useful lives of depreciable assets are as follows: buildings - 30 years; plant, machinery and equipment - 15 years; other machinery and equipment - 3 to 15 years.

Maintenance, repairs, and minor renewals are charged to income; major renewals and betterments are capitalized. Upon normal retirement or replacement, the net book value of property (less proceeds of sale or salvage) is charged to income.

### GOODWILL

Goodwill and other intangible assets are amortized on a straight-line basis over the estimated future periods to be benefited, generally 40 years for goodwill, customer relationships, and trademarks and tradenames and 5 to 15 years for other intangible assets.



## Edgar Filing: HERCULES INC - Form 10-K/A

Pursuant to Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (SFAS 142), beginning January 1, 2002, goodwill will not be amortized but will be tested for impairment annually and any necessary adjustment charged to expense. Intangible assets with finite lives will be amortized over their useful lives.

### LONG-LIVED ASSETS

Credit reviews its long-lived assets, including goodwill and other intangibles, for impairment on an exception basis whenever events or changes in circumstances indicate carrying amounts of the assets may not be recoverable through undiscounted future cash flows. If an impairment loss has occurred based on expected future cash flows (undiscounted), the loss is recognized in the income statement. The amount of the impairment loss is the excess of the carrying amount of the impaired asset over the fair value of the asset. The fair value represents expected future cash flows from the use of the assets, discounted at the rate used to evaluate potential investments.

### CONCENTRATIONS OF CREDIT RISK

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of trade receivables. Concentrations of credit risk with respect to trade receivables are limited due to the Company's large number of customers and their dispersion across many different industries and locations.

### FINANCIAL INSTRUMENTS

The Company uses various non-derivative financial instruments, including letters of credit, and generally does not require collateral to support its financial instruments.

### STOCK-BASED COMPENSATION

Compensation costs attributable to stock option and similar plans are recognized based on any excess of the quoted market price of the stock on the date of grant over the amount the employee is required to pay to acquire the stock (the intrinsic-value method under Accounting Principles Board Opinion 25 (APB 25)). Such amount, if any, is accrued over the related vesting period, as appropriate. Statement of Financial Accounting Standard No. 123, "Accounting for Stock-based Compensation," requires companies electing to continue to use the intrinsic-value method to make pro forma disclosures of net income as if the fair-value-based method of accounting had been applied.

### COMPUTER SOFTWARE COSTS

Effective January 1, 1999, Credit adopted the American Institute of Certified Public Accountants Statement of Position 98-1, "Accounting for the Cost of Computer Software Developed or Obtained for Internal Use" (SOP 98-1). Our prior accounting was generally consistent with the requirements of SOP 98-1 and, accordingly, adoption of SOP 98-1 had no material effect. Computer software costs are being amortized over a period of 5 to 10 years.

210

HERCULES CREDIT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

-----  
INCOME TAXES

## Edgar Filing: HERCULES INC - Form 10-K/A

The Company's operations have historically been included in the consolidated tax returns filed by its parent. Income tax expense in the accompanying financial statements have been computed assuming the Company filed separate income tax returns. Differences between this calculation of income taxes currently payable and consolidated amounts reported in the consolidated financial statements of the parent have been reflected as net Hercules Group investment.

### NET HERCULES GROUP INVESTMENT

The Net Hercules Group investment account reflects the balance of Credit's historical earnings, intercompany amounts, income taxes, taxes accrued and deferred, post-employment liabilities and other transactions between Credit and the Hercules Group.

### NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, the FASB issued Statement of Financial Accounting Standards No. 141, "Business Combinations" ("SFAS 141") and Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"). SFAS 141 supersedes Accounting Principles Board Opinion ("SPB") No. 16, Business Combinations. The provisions of SFAS 141 (1) require that the purchase method of accounting be used for all business combinations initiated after June 30, 2001, (2) provide specific criteria for the initial recognition and measurement of intangible assets apart from goodwill and (3) require that unamortized negative goodwill be written off immediately as extraordinary gain instead of being deferred and amortized. SFAS 141 also requires that upon adoption of SFAS 142 the Company reclassify the carrying amounts of certain intangible assets into or out of goodwill, based on certain criteria. SFAS 142 supersedes APB No. 17, Intangible Assets, and is effective for fiscal years beginning after December 15, 2001. SFAS 142 primarily addresses the accounting for goodwill and intangible assets subsequent to their initial recognition. The provisions of SFAS 142 (1) prohibit the amortization of goodwill and indefinite-lived intangible assets, (2) require that goodwill and indefinite-lived intangible assets be tested annually for impairment (and in interim periods if certain events occur indicating that the carrying value of goodwill and/or indefinite-lived intangible assets may be impaired), based on fair value (as opposed to cost recovery using future undiscounted cash flows), (3) require that reporting units be identified for the purpose of assessing potential future impairments of goodwill and (4) remove the forty-year limitation on the amortization period of intangible assets that have finite lives.

Effective January 1, 2002 Hercules adopted the provisions of SFAS 142. Hercules identified the following reporting units: BetzDearborn, Pulp and Paper, Aqualon, FiberVisions and Resins. In connection with Hercules' transitional review recorded goodwill was determined to be impaired in the BetzDearborn and FiberVisions reporting units. In the first quarter 2002, Hercules completed its transitional impairment review of the identified reporting units and recognized an after-tax impairment loss of \$368 million as a cumulative effect of a change in accounting principle. As a result of Hercules' adoption of SFAS 142, the Company will no longer record \$1.0 million of annual amortization relating to existing goodwill and intangibles, as adjusted for the reclassifications just mentioned.

In June 2001, the FASB approved the issuance of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143"). SFAS 143 establishes accounting standards for the recognition and measurement of legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 will become effective for Aqualon in January 1, 2003 and requires recognition of a liability for an asset retirement obligation in the period in which it is incurred. The Company does not believe this statement

## Edgar Filing: HERCULES INC - Form 10-K/A

will have a material effect on its financial statements.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company does not believe this statement will have a material effect on its financial statements.

In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections." The Company has elected to early adopt the provisions of SFAS 145 related to the rescission of SFAS 4, "Reporting Gains and Losses for the Extinguishment of Debt" ("SFAS" 4"). The early adoption had no effect on the Company's financial statements.

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146"). SFAS 146 addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs in a Restructuring)". SFAS 146 defines the timing of the recognition of costs associated with exit or disposal activities, the types of costs that may be recognized and the methodology for calculating the fair value of such costs. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. The Company does not believe this statement will have a material effect on its financial statements.

211

HERCULES CREDIT, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

-----

### 3. ACCOUNTS RECEIVABLE, NET

Accounts receivable, net, consists of:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Trade	\$ 31,365	\$ 36,413
Less allowance for doubtful accounts	(441)	(670)
	-----	-----
Total	\$ 30,924	\$ 35,743
	=====	=====

### 4. NOTE RECEIVABLE

Notes receivable as of December 31, 2001, consists of an unsecured demand note to Greentree Chemical Technologies, Inc. (Greentree) for \$3,000 thousand, due June 30, 2005. The note carried an interest rate of 13.5% until May 1, 2001; thereafter, the interest rate is equal to Prime +7.5% for the remaining duration of the note. Notes receivable as of December 31, 2000, consist of a \$6,600 thousand 30-day demand note from Greentree, related to the divestiture of the Nitrocellulose business in June 2000. On January 8, 2001, Aqualon received \$3,600 thousand in cash from Greentree and issued the unsecured demand note to

## Edgar Filing: HERCULES INC - Form 10-K/A

Greentree for \$3,000 thousand, due June 30, 2005.

### 5. INVENTORIES

The components of inventories are:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Finished products	\$22,480	\$27,754
Raw material and supplies	14,280	15,613
Work in process	2,580	2,042
	-----	-----
Total	\$39,340	\$45,409
	=====	=====

### 6. LONG-TERM INCENTIVE COMPENSATION PLANS

The Company participates in long-term incentive compensation plans sponsored by Hercules. These plans provide for the grant of stock options and the award of common stock and other market-based units to certain key employees and non-employee directors.

In 1995, Hercules changed the structure of the long-term incentive compensation plans to place a greater emphasis on shareholder value creation through grants of regular stock options, performance-accelerated stock options, and Cash Value Awards (performance-based awards denominated in cash and payable in shares of common or restricted stock, subject to the same restrictions as restricted stock). Restricted stock and other market-based units are awarded with respect to certain programs. The number of awarded shares outstanding was 189,704 at December 31, 2001, and 491,488 and 926,689 at December 31, 2000 and 1999, respectively.

At December 31, 2001, under Hercules' incentive compensation plans, 1,265,493 shares of common stock were available for grant as stock awards or stock option awards. Stock awards are limited to approximately 15% of the total authorizations. Regular stock options are granted at the market price on the date of grant and are exercisable at various periods from one to five years after date of grant. Performance-accelerated stock options are also granted at the market price on the date of grant and are normally exercisable at nine and one-half years. Exercisability may be accelerated based upon the achievement of predetermined performance goals. Both regular and performance-accelerated stock options expire 10 years after the date of grant.

212

HERCULES CREDIT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

Restricted shares, options and performance-accelerated stock options are forfeited and revert to Hercules in the event of employment termination, except in the case of death, disability, retirement, or other specified events.

The Company applies APB Opinion 25 in accounting for its plans. Accordingly,

## Edgar Filing: HERCULES INC - Form 10-K/A

no compensation cost has been recognized for the stock option plans. There were no charges to income for the cost of stock awards over the restriction or performance period for 2001, 2000 and 1999, respectively.

Below is a summary of outstanding stock option grants under the incentive compensation plans during 1999, 2000 and 2001:

	Regular		Performance-Accelera	
	Number of Shares	Weighted-average price	Number of Shares	Weighted pr
December 31, 1998	337,405	\$ 39.48	136,645	\$
Granted	71,875	\$ 37.73	69,980	\$
Exercised	(1,050)	\$ 16.21	--	
Forfeited	(3,910)	\$ 39.50	--	
December 31, 1999	404,320	\$ 39.23	206,625	\$
Granted	129,800	\$ 17.20	--	
Exercised	--	--	--	
Forfeited	(39,250)	\$ 39.50	--	
December 31, 2000	494,870	\$ 33.43	206,625	\$
Granted	131,925	\$ 14.22	--	
Exercised	--	--	--	
Forfeited	(40,710)	\$ 39.56	--	
December 31, 2001	586,085	\$ 28.01	206,625	\$

The weighted-average fair value of regular stock options granted during 1999, 2000 and 2001 was \$8.26, \$8.85 and \$5.69, respectively. The weighted-average fair value of performance-accelerated stock options granted during 1999, 2000 and 2001 was \$8.01, \$0 and \$0, respectively.

Following is a summary of regular stock options exercisable at December 31, 1999, 2000, and 2001, and their respective weighted-average share prices:

Options Exercisable	Number of Shares	Weighted-average exercise price
1999	224,230	\$40.49
2000	293,370	\$39.20
2001	368,975	\$35.01

There were no performance-accelerated stock options exercisable at December 31, 1999, 2000 and 2001.

Following is a summary of stock options outstanding at December 31, 2001:

Outstanding Options		
Number	Weighted-average	Weighted-

Edgar Filing: HERCULES INC - Form 10-K/A

Exercise Price Range	Outstanding at 12/31/2001	Remaining Contractual Life	average exercise price	Ex
Regular Stock Options				
\$11 - \$20	261,725	8.90	\$ 14.22	
\$20-\$30	76,475	6.67	\$ 25.56	
\$30-\$40	135,515	6.33	\$ 38.68	
\$40-\$50	84,120	5.73	\$ 47.26	
\$50-\$60	28,250	4.56	\$ 54.01	
	-----			
	586,085			
	-----			
Performance-Accelerated Stock Options				
\$14-\$40	104,655	6.69	\$ 38.16	
\$40-\$50	81,270	5.70	\$ 47.40	
\$50-\$61	20,700	4.18	\$ 55.40	
	-----			
	206,625			
	-----			

The Company currently expects that 100% of performance-accelerated stock options will eventually vest.

The Company's employees may also participate in the Hercules Employee Stock Purchase Plan ("ESSP"). The ESSP is a qualified non-compensatory plan, which allows eligible employees to acquire shares of common stock through systematic payroll deductions. The plan consists of three-month subscription periods, beginning July 1 of each year.

213

HERCULES CREDIT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The purchase price is 85% of the fair market value of the common stock on either the first or last day of that subscription period, whichever is lower. Purchases may range from 2% to 15% of an employee's base salary each pay period, subject to certain limitations. Currently, there are no shares of Hercules common stock registered for offer and sale under the plan. Shares issued at December 31, 2001 and 2000, were 1,758,081 and 1,597,861, respectively. The Company applies APB Opinion 25 and related interpretations in accounting for its Employee Stock Purchase Plan. Accordingly, no compensation cost has been recognized for the Employee Stock Purchase Plan.

Had compensation cost for Hercules' Stock-Based Incentive Plans and Employee Stock Purchase Plan been determined on the basis of fair value according to SFAS No. 123, the fair value of each option granted or share purchased would be estimated on the grant date using the Black-Scholes option pricing model.

The following weighted-average assumptions would be used in estimating fair value for 1999, 2000 and 2001:

Assumption	Regular Plan	Performance Accelerated Plan	Employee Stock Purchase Plan
------------	-----------------	------------------------------------	------------------------------------

Edgar Filing: HERCULES INC - Form 10-K/A

-----	----	----	-----
Dividend yield	0.96%	3.83%	0.0%
Risk-free interest rate	5.80%	5.57%	4.86%
Expected life	7.1 yrs.	5 yrs.	3 mos.
Expected volatility	33.36%	29.78%	49.11%

The Company's net income and earnings per share for 2001, 2000 and 1999 would approximate the pro forma amounts below:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Net income			
As reported	\$28,814	\$20,953	\$23,659
Pro forma	\$28,043	\$19,328	\$22,110

7. ADDITIONAL BALANCE SHEET DETAIL

	(Dollars in thousands)	
	2001	2000
	-----	-----
Property, plant, and equipment		
Land	\$ 527	\$ 527
Buildings and equipment	371,173	365,202
Construction in progress	16,185	11,909
	-----	-----
Total	387,885	377,638
Accumulated depreciation and amortization	293,163	285,409
	-----	-----
Net property, plant, and equipment	\$ 94,722	\$ 92,229
	=====	=====
Accrued expenses		
Payroll and employee benefits	\$ 5,416	\$ 4,685
Nitrocellulose inventory disposal cost reserve	5,917	6,478
Current environmental reserve	5,222	4,686
Restructuring reserve (Note 10)	1,762	
Other	8,527	9,741
	-----	-----
Total	\$ 26,844	\$ 25,590
	=====	=====

8. INVESTMENTS

Summarized financial information for Hercules Finance Company, at December 31, 2001 and 2000 and the three years then ended is as follows:

## Edgar Filing: HERCULES INC - Form 10-K/A

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

	2001	2000	
	-----	-----	
Assets	--	\$ 55	
Net Hercules Group Investment	--	55	
	2001	2000	1999
	-----	-----	-----
Interest income	\$ 110	\$ 1,235	\$ 1,274
Interest income from Hercules Group	47,952	48,011	38,582
Corporate and other cost allocations	(2,621)	(2,132)	(3,067)
Other expense	--	--	--
Net income	45,441	47,114	36,789

#### 9. GOODWILL

Goodwill relates to Hercules' 1989 purchase of Henkel's portion of ownership in Aqualon. At December 31, 2001 and December 31, 2000, goodwill was \$27,536 thousand and \$28,550 thousand, respectively, (net of accumulated amortization of \$13,008 thousand and \$11,994 thousand respectively). Through December 31, 2001, the goodwill was being amortized over 40 years.

#### 10. RESTRUCTURING

In 2001 and 2000, Hercules Credit incurred \$6,000 thousand and \$1,662 thousand, respectively, in other operating expenses related to employee severance benefits for workforce reductions at Parlin, NJ, Louisiana, MO, and Hopewell, VA, manufacturing sites and Wilmington, DE headquarters in business support functions.

During 2001, management authorized and committed to a plan to reduce the workforce as part of the comprehensive cost reduction and work process redesign program. Under this plan, 97 employees have left or will leave Hercules Credit, of which 74 employees were terminated pursuant to this plan through December 31, 2001.

The 2000 restructuring costs are related to workforce reductions in the Hercules Credit manufacturing cost reduction plan. The total number of employee terminations relating to the 2000 plan is 35, and the actions under the 2000 plan are complete.

Severance benefits were paid in accordance with Hercules' standard severance pay plan. A reconciliation of activity with respect to the liabilities established for these plans is as follows:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Balance at beginning of year	\$ --	\$ --
Additional termination benefits and other exit costs	6,000	1,662



Edgar Filing: HERCULES INC - Form 10-K/A

Cash payments	(4,238)	(1,662)
	-----	-----
Balance at end of year	\$ 1,762	\$ --
	=====	=====

11. PENSION AND OTHER POSTRETIREMENT BENEFITS

Credit participates in a defined benefit pension plan sponsored by Hercules, which covers substantially all employees of Hercules in the U.S. Benefits under this plan are based on the average final pay and years of service. Hercules also provides post-retirement health care and life insurance benefits to eligible retired employees and their dependents.

Information on the actuarial present value of the benefit obligation and fair value of the plan assets is not presented as Hercules manages its U.S. employee benefit plans on a consolidated basis and such information is not maintained

215

HERCULES CREDIT, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

separately for the U.S. employees of the Company. The Company's statement of operations includes an allocation of the costs of the U.S. benefits plans. The pension costs were allocated based on percentage of pensionable wages, for each of the years presented, post-retirement benefit costs were allocated using factors derived from the relative net assets and revenues. Net pension income of Hercules allocated to the Company was \$1,719 thousand, \$3,367 thousand, and \$3,810 thousand for the years ended December 31, 2001, 2000 and 1999, respectively, and post-retirement benefit expense was \$2,125 thousand, \$2,462 thousand, and \$1,774 thousand for the years ended December 31, 2001, 2000 and 1999, respectively.

12. OTHER OPERATING EXPENSES, NET

Other operating expenses, net, consists of the following:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Loss on disposal of Nitrocellulose	\$ --	\$ 25,241	\$ 6,500
Asset impairments	--	--	2,000
Environmental charges	2,344	2,617	3,020
Restructuring charges	6,000	1,662	446
Royalties received	(10,473)	(7,613)	(8,474)
Other	--	352	62
	-----	-----	-----
Total	\$ (2,129)	\$ 22,259	\$ 3,554
	=====	=====	=====

In 1999, the remaining Nitrocellulose fixed assets at Parlin, NJ were deemed to be impaired.

Edgar Filing: HERCULES INC - Form 10-K/A

216

HERCULES CREDIT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

13. INCOME TAXES

The domestic components of income before taxes are presented below:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Domestic	\$49,042	\$35,358	\$39,581
	-----	-----	-----
	\$49,042	\$35,358	\$39,581
	=====	=====	=====

A summary of the components of the tax provision follows:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Currently Payable			
Domestic	\$ 18,747	\$ 12,583	\$ 23,612
Deferred			
Domestic	1,238	1,658	(7,905)
	-----	-----	-----
Provision for income taxes	\$ 19,985	\$ 14,241	\$ 15,707
	=====	=====	=====

Deferred tax liabilities (assets) at December 31 consists of:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Amortization	--	7
Partnership Interest	11,040	12,151
Other	--	704
	-----	-----
Gross deferred tax liabilities	\$ 11,040	\$ 12,862
	-----	-----
Depreciation	\$ (238)	\$ (217)
Deemed rent	--	(425)
Lease liability	(1,471)	(4,500)
Other	(374)	--
	-----	-----
Gross deferred tax assets	(2,083)	(5,142)
	-----	-----

Edgar Filing: HERCULES INC - Form 10-K/A

\$ 8,957                      \$ 7,720  
 =====                      =====

A reconciliation of the statutory tax rate to the effective tax rate follows:

	2000	1999	1998
	-----	-----	-----
Statutory income tax rate	35.00%	35.00%	35.00%
State Taxes	5.00%	5.00%	5.00%
	-----	-----	-----
	40%	40%	40%
	=====	=====	=====

217

HERCULES CREDIT, INC.  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

14. NET HERCULES GROUP INVESTMENT

Changes in net Hercules Group investment were as follows:

	(Dollars in thousands)
	-----
Balance, January 1, 1999	\$ 199,323
Net income	23,659
Intercompany transactions, net	(31,967)
	-----
Balance, December 31, 1999	191,015
Net income	20,953
Intercompany transactions, net	(19,193)
	-----
Balance, December 31, 2000	192,775
Net income	28,814
Intercompany transactions, net	(35,224)
	-----
Balance, December 31, 2001	\$ 186,364
	=====

15. DIVESTITURES

In June 2000, the Company divested its Nitrocellulose operation at Parlin, NJ to Greentree Chemical Technologies, Inc. As a result of the transaction, the Company received a \$6,600 thousand note (see note 4) and recorded a one-time pre-tax loss of \$25,241 thousand, primarily for employee termination benefits, inventory transfer and disposal, environmental liabilities, and other miscellaneous expenses, of which \$20,316 thousand has been expended. The Company terminated approximately 100 employees associated with the Nitrocellulose operation at Parlin, NJ, which resulted in severance payments of \$4 million. Nitrocellulose revenues were \$23,503 thousand and \$58,526 thousand, in 2000 and

## Edgar Filing: HERCULES INC - Form 10-K/A

1999, respectively.

### 16. COMMITMENTS AND CONTINGENCIES

#### Leases

The Company has operating leases (including office space, transportation, and data processing equipment) expiring at various dates. Rental expense was \$3,993 thousand in 2001, \$3,240 thousand in 2000, and \$3,446 thousand in 1999.

At December 31, 2001, minimum rental payments under noncancelable leases aggregated \$10,962 thousand. The net minimum payments over the next five years are \$2,448 thousand in 2002, \$2,287 thousand in 2003, \$2,106 thousand in 2004, \$2,067 thousand in 2005, and \$2,054 thousand in 2006.

#### Litigation

The Company currently and from time to time is involved in litigation incidental to the conduct of its business. In the opinion of Credit's management, none of such litigation as of December 31, 2001 is likely to have a material adverse effect on the financial position and results of operations of Credit.

#### Environmental

The Company has established accruals for the estimated cost of environmental remediation and/or cleanup at various sites. The estimated range of the reasonable possible share of costs for investigation and cleanup is between \$25 million and \$42 million. The actual costs will depend upon numerous factors, including the number of parties found to be responsible at each environmental site and their ability to pay; the actual methods of remediation required or agreed to; the outcomes of negotiations with regulatory authorities; outcomes of litigation; changes in environmental laws and regulations; technological developments; and the number of years of remedial activity required, which could range from 0 to 30 years. As of December 31, 2001, the accrued liability of \$25 million for environmental remediation represents management's best estimate of the probable and reasonably estimable costs related to environmental remediation. Credit estimates that these liabilities will be paid over the next five years. The extent of liability is evaluated quarterly. The measurement of the liability is evaluated based on currently available information, including the process of remedial investigations at each site and the current status of negotiations with regulatory authorities regarding the method and extent of apportionment of costs among other potentially responsible parties. The Company is unaware of any unasserted

218

HERCULES CREDIT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

claims and has not reflected them in the reserve. While it is not feasible to predict the outcome of all pending suits and claims, the ultimate resolution of these environmental matters could have a material effect upon the results of operations and the financial position of the Company.

#### Other

As of December 31, 2000, the Company had \$4.3 million in letters of credit outstanding with lenders.

### 17. RELATED PARTY TRANSACTIONS

## Edgar Filing: HERCULES INC - Form 10-K/A

The Company has entered into certain agreements with affiliated entities. These agreements were developed in the context of parent/subsidiary relationship and therefore may not necessarily reflect the result of arms-length negotiations between independent parties. The Company records sales with affiliates based on a cost-plus formula developed and agreed-upon by both parties.

**Corporate and other cost allocations:** As discussed in Note 1, the financial statements of The Company reflect certain allocated support costs incurred by other entities in Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, research & development overhead, investor relations and other corporate services. Allocations and charges included in Credit's financial statements were based on either a direct cost pass-through for items directly identified as related to Credit's activities; a percentage allocation for such services provided based on factors such as revenues, net assets, costs of sales or a relative weighting of geographic activity. These allocations are reflected in the selling, general and administrative line item in our statement of operations. . Such allocations and corporate charges totaled \$19,296 thousand, \$17,569 thousand, and \$25,148 thousand in 2001, 2000 and 1999, respectively.

**Royalties:** Credit entered into a license agreement in respect of the use of manufacturing formulations and specifications by affiliated companies which are developed and owned by the Company. The Company received royalties in respect of this agreement of \$10,473 thousand, \$7,613 thousand, and \$8,474 thousand in 2001, 2000 and 1999, respectively. The royalties are included as reductions to other operating expenses in the financial statements.

**Purchases from affiliates:** The Company purchases a broad range of products in the normal course of business from affiliated companies. Credit's purchases from affiliated companies were \$21,391 thousand, \$23,457 thousand, and \$23,598 thousand in 2001, 2000 and 1999, respectively.

### 18. SUBSEQUENT EVENTS

On April 29, 2002, Hercules completed the sales of its Water Treatment Business to GE Specialty Materials (GSM). Pursuant to the Stock and Asset Purchase Agreement for the transaction, the sale included the stock of BetzDearborn Inc. and certain specified assets and liabilities. Hercules used the proceeds from the sale to prepay borrowings under its Facilities. Pursuant to the prepayment, among other things, the Company's stock, which had been pledged as collateral to the Facilities, was released.

219

### REPORT OF INDEPENDENT ACCOUNTANTS

TO THE SHAREHOLDERS AND THE BOARD OF DIRECTORS OF  
HERCULES INCORPORATED  
WILMINGTON, DELAWARE

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations and comprehensive loss and of cash flows present fairly, in all material respects, the financial position of Hercules GB Holdings Limited, a subsidiary of Hercules Incorporated, and its subsidiaries at December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these

## Edgar Filing: HERCULES INC - Form 10-K/A

financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers Accountants N.V.  
Amsterdam, The Netherlands  
November 12, 2002

220

### HERCULES GB HOLDINGS LIMITED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS

	(Dollars in thousands)		
	Year Ended December 31,		
	2001	2000	1999
	-----	-----	-----
Sales to third parties	\$ 101,514	\$ 123,301	\$ 136,056
Sales to Hercules Group	18,932	23,072	22,334
	-----	-----	-----
	120,446	146,373	158,390
Cost of sales	69,811	85,980	92,200
Selling, general, and administrative expenses	31,982	35,332	38,493
Research and development	43	574	1,778
Goodwill and intangible asset amortization	4,099	4,608	4,875
Other operating expenses, net (Note 12)	15,603	6,248	5,361
	-----	-----	-----
(Loss) profit from operations	(1,092)	13,631	15,683
Interest and debt expense (Note 13)	(9,752)	(12,107)	(5,376)
Other income, net (Note 14)	560	97	565
	-----	-----	-----
(Loss) income before income taxes	(10,284)	1,621	10,872
Provision for income taxes (Note 16)	(781)	(1,960)	(4,817)
	-----	-----	-----
Net (loss) income	\$ (11,065)	\$ (339)	\$ 6,055
Additional minimum pension liability, net of tax of \$(6,327)	(14,762)	--	--
Foreign currency translation, net of tax of \$0 for each year	1,196	(2,534)	(8,724)
	-----	-----	-----
Comprehensive loss	\$ (24,631)	\$ (2,873)	\$ (2,669)
	=====	=====	=====

The accompanying accounting policies and notes are an integral part of the consolidated financial statements.

221

Edgar Filing: HERCULES INC - Form 10-K/A

HERCULES GB HOLDINGS LIMITED  
CONSOLIDATED BALANCE SHEETS

	(Dollars in thousands)	
	December 31,	
	2001	2000
	-----	-----
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 590	\$ 1,057
Accounts receivable, net (Note 3)	28,603	34,146
Inventories (Note 4)	5,334	8,312
Deferred income taxes (Note 16)	644	--
	-----	-----
Total current assets	35,171	43,515
Property, plant, and equipment, net (Note 8)	24,512	29,687
Goodwill and other intangible assets, net (Note 9)	121,252	139,157
Deferred income taxes (Note 16)	3,217	--
Prepaid pension (Note 11)	9,935	7,785
Deferred charges and other assets	3,037	1,723
	-----	-----
Total assets	\$ 197,124	\$ 221,867
	=====	=====
<b>LIABILITIES AND NET HERCULES GROUP INVESTMENT</b>		
Current liabilities		
Accounts payable	\$ 12,595	\$ 14,588
Short-term debt (Note 5)	--	4,469
Accrued expenses (Note 8)	9,323	7,266
	-----	-----
Total current liabilities	21,918	26,323
Deferred income taxes (Note 16)	--	4,831
Pension (Note 11)	22,139	--
	-----	-----
Total liabilities	44,057	31,154
	-----	-----
Commitments and contingencies (Note 17)	--	--
Net Hercules Group Investment (Note 15)		
Accumulated other comprehensive income	(19,954)	(6,388)
Intercompany transactions	173,021	197,101
	-----	-----
Net Hercules Group Investment	153,067	190,713
	-----	-----
Total liabilities and Net Hercules Group Investment	\$ 197,124	\$ 221,867
	=====	=====

The accompanying accounting policies and notes are an integral part of the consolidated financial statements.

HERCULES GB HOLDINGS LIMITED  
CONSOLIDATED STATEMENTS OF CASH FLOWS

Edgar Filing: HERCULES INC - Form 10-K/A

December 31  
(Dollars in thousands)

	2001 ----	2000 ----	1999 ----
<b>CASH FLOW FROM OPERATING ACTIVITIES:</b>			
Net (Loss) Income	\$ (11,065)	\$ (339)	\$ 6,055
Adjustments to reconcile net (loss) income to net cash provided from operations:			
Depreciation of property, plant and equipment	3,294	3,431	2,921
Amortization of goodwill and other intangible assets	4,099	4,608	4,875
Restructuring plans	1,919	319	(357)
Loss on disposals of property, plant and equipment	981	214	307
Nonoperating loss on sale of investment	7,194	--	--
Movement on deferred tax provision	(898)	410	1,615
Corporate cost allocations	1,802	1,917	3,593
Prepaid pension expense and other deferred charges	(3,602)	(1,753)	(888)
Accruals and deferrals of cash receipts and payments:			
Accounts receivable	5,182	(1,194)	1,235
Transfers from (to) Hercules Group	7,770	(11,064)	(4,665)
Inventories	2,384	3,861	(403)
Accounts payable and accrued expenses	3,958	(1,443)	(3,951)
	-----	-----	-----
Net cash provided by (used in) operations	23,018	(1,033)	10,337
	-----	-----	-----
<b>CASH FLOW FROM INVESTING ACTIVITIES:</b>			
Capital expenditures, net of proceeds from sale	(219)	(2,562)	(4,747)
	-----	-----	-----
Net cash used in investing activities	(219)	(2,562)	(4,747)
	-----	-----	-----
<b>CASH FLOW FROM FINANCING ACTIVITIES:</b>			
Transfers to Hercules Group	(18,795)	(1,067)	(8,855)
New loan proceeds	--	4,571	254
Loan repayments	(4,468)	(190)	--
	-----	-----	-----
Net cash (used in) provided by financing activities	(23,263)	3,314	(8,601)
	-----	-----	-----
Effect of exchange rate changes on cash	(3)	(107)	(159)
	-----	-----	-----
Net decrease in cash and cash equivalents	(467)	(388)	(3,170)
Cash and cash equivalents at beginning of year	1,057	1,445	4,615
	-----	-----	-----
Cash and cash equivalents at end of year	\$ 590	\$ 1,057	\$ 1,445
	-----	-----	-----
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION</b>			
Cash paid during year for:			
Income Taxes	\$ 1,136	\$ 1,550	\$ 6,911
Interest	\$ 3,127	\$ 4,982	\$ 7,830
<b>NON CASH FINANCING ACTIVITIES</b>			
Corporate cost allocations	\$ 1,802	\$ 1,917	\$ 3,593



HERCULES GB HOLDINGS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS-----  
1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

Hercules GB Holdings Limited (referred to singly or together with its subsidiaries as "the Company") is the intermediate United Kingdom holding company (directly or indirectly) of all entities in the United Kingdom in the ultimate ownership of Hercules Incorporated (Wilmington, Delaware, USA) ("Hercules"), with the sole exception of Citrus Colloids Limited which is not included in these consolidated statements. Hercules and its wholly owned subsidiaries comprise the Hercules Group. The two principle operating subsidiaries are Hercules Limited, engaged in the manufacture and merchandising of functional chemicals and food ingredients and BetzDearborn Limited engaged in the manufacture and marketing of water and process treatment chemicals and ancillary equipment.

BetzDearborn Limited became a subsidiary of the Company following the acquisition by Hercules on 15th October, 1998, of all of the outstanding shares of BetzDearborn Inc. (formerly the ultimate parent company of BetzDearborn Limited). Hercules paid \$2,235 million in cash and \$186 million in common stock exchanged for the shares held by the BetzDearborn ESOP Trust. The purchase price allocated to the Company and its subsidiaries was approximately \$123 million. During 1999, Hercules completed the purchase price allocation and the final determination of goodwill was \$2,170 million of which the amount attributable to the Company was approximately \$146 million. These financial statements include the push down of fair value adjustments to assets and liabilities, including goodwill, other intangible assets and property, plant and equipment and their related amortization and depreciation adjustments.

Hercules GB Holdings Limited was set up in June 1999 to be the principal holding company for Hercules entities based in UK. This was a result of several internal reorganization transactions during 1999 and 2000, that were initiated after the acquisition of BetzDearborn Inc. The reorganization included the Company acquiring nearly all of the existing UK based subsidiaries from other Hercules group of companies. As these reorganization transactions were under the common control of Hercules, they have been accounted for at book value and have been consolidated in a manner similar to a pooling of interests.

Prior to the 2000 fiscal year, separate company stand alone financial statements were not prepared for the Company. In November 2000, Hercules amended its senior credit facility and ESOP credit facility (the "Facilities"). The Facilities, as amended, are secured by liens on Hercules' property and assets (and those of Hercules' Canadian Subsidiaries), a pledge of the stock and partnership and member interests of substantially all of Hercules' domestic subsidiaries and 65% of the stock of foreign subsidiaries directly owned by Hercules, including the Company, and a pledge of Hercules' domestic intercompany indebtedness. These financial statements present the financial information on the Company, a collateral party to the Hercules debt, based on the Hercules' understanding of Securities and Exchange Commission's interpretation and application of Rule 3-16 under the Securities and Exchange Commission's Regulation S-X. These statements were derived from historical accounting records.

On April 29, 2002, in connection with Hercules' sale of its Water Treatment Business (see Note 19) and the repayment of the Facilities, the stock

## Edgar Filing: HERCULES INC - Form 10-K/A

pledges were released. As a result, based on Hercules' current debt structure, these separate company stand-alone financial statements will not be required for the fiscal year ending December 31, 2002.

The Company participates in Hercules' centralized cash management system. Accordingly, cash received from the Company's operations is transferred to Hercules on a periodic basis, and Hercules funds all operational and capital requirements.

The financial statements of the Company reflect certain allocated support costs incurred by other entities in the Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations and charges included in the Company's financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on factors such as sales, net assets, or cost of sales; or a relative weighting of geographic activity. Management believes that the allocation methods are reasonable.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of Hercules GB Holdings Limited and its wholly owned subsidiaries. Following the acquisition of BetzDearborn, the company continued BetzDearborn's practice of using a November 30 fiscal year-end for certain former BetzDearborn non-U.S. subsidiaries to expedite the year-end closing process. All intercompany transactions and profits have been eliminated.

#### USE OF ESTIMATES

Preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

224

#### HERCULES GB HOLDINGS LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

#### REVENUE RECOGNITION

The Company recognizes revenue when the earnings process is complete. This generally occurs when products are shipped to the customer or services are performed in accordance with terms of the agreement, title and risk of loss have been transferred, collectibility is probable, and pricing is fixed and determinable. Accruals are made for sales returns and other allowances based on the Company's experience. The corresponding shipping and handling costs are included in cost of sales.

#### RESEARCH AND DEVELOPMENT

Research and development expenditures are expensed as incurred.

#### ENVIRONMENTAL EXPENDITURES

## Edgar Filing: HERCULES INC - Form 10-K/A

Environmental expenditures that pertain to current operations or future revenues are expensed or capitalized according to the Company's capitalization policy. Expenditures for remediation of an existing condition caused by past operations that do not contribute to current or future revenues are expensed. Liabilities are recognized for remedial activities when the cleanup is probable and can be reasonably estimated.

### CASH AND CASH EQUIVALENTS

Cash in excess of operating requirements is invested in short-term, income-producing instruments and on interest bearing deposit with Hercules Europe NV, the Treasury Co-ordination Center. Cash equivalents include commercial paper and other securities with original maturities of 90 days or less. Book value approximates fair value because of the short maturity of those instruments.

### INVENTORIES

Inventories are stated at the lower of cost or market value. Cost is established on a moving average or standard cost basis both of which approximate to actual historic cost.

### PROPERTY AND DEPRECIATION

Property, plant, and equipment are stated at cost. Asset values are depreciated over estimated useful lives on the straight-line method of depreciation. The estimated useful lives of depreciable assets are as follows: buildings - 30 years; plant, machinery and equipment - 15 years; other machinery and equipment - 3 to 15 years; computer software - 10 years.

Maintenance, repairs, and minor renewals are charged to income; major renewals and improvements are capitalized. Upon normal retirement or replacement, the net book value of property (less proceeds of sale or salvage) is expensed.

### GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill and other intangible assets are amortized on a straight-line basis over the estimated future periods to be benefited, generally 40 years for goodwill, and 3 to 15 years for other intangible assets. Pursuant to Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (SFAS 142), beginning January 1, 2002, goodwill will not be amortized but will be tested for impairment annually and any necessary adjustment charged to expense. Intangible assets with finite lives will be amortized over their useful lives.

### LONG-LIVED ASSETS

The company reviews its long-lived assets, including goodwill and other intangibles, for impairment on an exception basis whenever events or changes in circumstances indicate carrying amounts of the assets may not be recoverable through undiscounted future cash flows. If an impairment loss has occurred based on expected future cash flows (undiscounted), the loss is recognized in the income statement. The amount of the impairment loss is the excess of the carrying amount of the impaired asset over the fair value of the asset. The fair value represents expected future cash flows from the use of the assets, discounted at the rate used to evaluate potential investments.

### COMPUTER SOFTWARE COSTS

Effective January 1, 1999, the Company adopted the American Institute of

## Edgar Filing: HERCULES INC - Form 10-K/A

Certified Public Accountants Statement of Position 98-1, "Accounting for the Cost of Computer Software Developed or Obtained for Internal Use" (SOP 98-1). The prior accounting was generally consistent with the requirements of SOP 98-1 and, accordingly, adoption of SOP 98-1 had no material effect. Computer software costs are being amortized over a period of 5 to 10 years.

225

HERCULES GB HOLDINGS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

### FOREIGN CURRENCY TRANSLATION AND TRANSACTIONS

The accompanying consolidated financial statements are reported in U.S. dollars. The pound sterling is the functional currency for the Company and its subsidiaries. The translation of the functional currencies into U.S. dollars (reporting currency) is performed for assets and liabilities using the current exchange rates in effect at the balance sheet date, and for revenues, costs and expenses using average exchange rates prevailing during the reporting periods. Adjustments resulting from the translation of functional currency financial statements to reporting currency are accumulated and reported as other comprehensive income (loss), a separate component of Net Hercules Group Investment.

Transactions in foreign currency are recorded at the exchange rate prevailing on the date of transaction. Monetary assets and liabilities denominated in foreign currencies are expressed in the functional currency at the exchange rates in effect at the balance sheet date. Revenues, costs and expenses are recorded using average exchange rates prevailing during the reporting periods. Gains or losses resulting from foreign currency transactions are included in the statement of income.

### CONCENTRATIONS OF CREDIT RISK

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of short-term cash investments and trade receivables. The Company places its short-term cash investments on the London money market via its commercial relationship banks. Concentrations of credit risk with respect to trade receivables are limited due to the Company's large number of customers and their dispersion across many different industries and locations.

### DERIVATIVE INSTRUMENTS AND HEDGING

On January 1, 2001, the Company adopted Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"). SFAS 133, as amended by Statement No. 137, "Accounting for Derivative Instruments and Hedging Activities-Deferral of the Effective Date of FASB Statement No. 133" and Statement No. 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities," requires that all derivative instruments be recorded on the balance sheet at their fair value. The Company has not designated any derivative as a hedge instrument and accordingly, changes in fair value of derivatives are recorded each period in earnings. The adoption of SFAS 133 did not result in a pre-tax or post-tax cumulative-effect-type adjustment to income and did not result in a change to other comprehensive income (loss).

Derivative financial instruments have been used to hedge risk caused by fluctuating currency. The Company enters into forward-exchange contracts to

## Edgar Filing: HERCULES INC - Form 10-K/A

hedge foreign currency exposure. Decisions regarding hedging are made on a case-by-case basis, taking into consideration the amount and duration of the exposure, market volatility, and economic trends. The Company uses the fair-value method of accounting, recording to other income (expense), net realized and unrealized gains and losses on these contracts monthly, except for gains and losses on contracts to hedge specific foreign currency commitments, which are deferred and accounted for as part of the transaction. Gains or losses on instruments which have been used to hedge the value of investments in certain non-U.S. subsidiaries have been accounted for under the deferral method and are included in the foreign currency translation adjustment. It is the Company's policy to match the term of financial instruments with the term of the underlying designated item. If the designated item is an anticipated transaction no longer likely to occur, gains or losses from the instrument designated as a hedge are recognized in current period earnings. The Company does not hold or issue financial instruments for trading purposes. In the consolidated statement of cash flow, the Company reports the cash flows resulting from its hedging activities in the same category as the related item that is being hedged.

### STOCK BASED COMPENSATION

Compensation costs attributable to stock option and similar plans are recognized based on any excess of the quoted market price of the stock on the date of grant over the amount the employee is required to pay to acquire the stock (the intrinsic-value method under Accounting Principles Board Opinion 25 (APB 25)). Such amount, if any, is accrued over the related vesting period, as appropriate. Statement of Financial Accounting Standard No. 123, "Accounting for Stock-Based Compensation," requires companies electing to continue to use the intrinsic-value method to make pro forma disclosures of net income as if the fair-value-based method of accounting had been applied.

### INCOME TAXES

Income tax expense in the accompanying financial statements has been computed assuming the Company filed separate income tax returns.

The provisions for income taxes has been determined using the asset and liability approach of accounting for income taxes. Under this approach, deferred taxes represent the future tax consequences expected to occur when the reported amounts of assets and liabilities are recovered or paid. The provision for income taxes represents income taxes paid or payable for the current year plus the change in deferred taxes during the year. Deferred taxes result from

226

### HERCULES GB HOLDINGS LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

differences between the financial and tax basis of the Company's assets and liabilities and are adjusted for changes in tax rates and tax laws when changes are enacted. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized.

### NET HERCULES GROUP INVESTMENT

The Net Hercules Group Investment reflects the balance of the Company's historical earnings, inter-company amounts, foreign currency translation and other transactions between the Company and the Hercules Group

### NEW ACCOUNTING PRONOUNCEMENTS

## Edgar Filing: HERCULES INC - Form 10-K/A

In June 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 141, "Business Combinations" ("SFAS 141"), and Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"). SFAS 141 supersedes Accounting Principles Board Opinion ("APB") No. 16, Business Combinations. The provisions of SFAS 141 (1) require that the purchase method of accounting be used for all business combinations initiated after June 30, 2001, (2) provide specific criteria for the initial recognition and measurement of intangible assets apart from goodwill and (3) require that unamortized negative goodwill be written off immediately as extraordinary gain instead of being deferred and amortized. SFAS 141 also requires that upon adoption of SFAS 142 the Company reclassify the carrying amounts of certain intangible assets into or out of goodwill, based on certain criteria. SFAS 142 supersedes APB No. 17, Intangible Assets, and is effective for fiscal years beginning after December 15, 2001. SFAS 142 primarily addresses the accounting for goodwill and intangible assets subsequent to their initial recognition. The provisions of SFAS 142 (1) prohibit the amortization of goodwill and indefinite-lived intangible assets, (2) require that goodwill and indefinite-lived intangible assets be tested annually for impairment (and in interim periods if certain events occur indicating that the carrying value of goodwill and/or indefinite-lived intangible assets may be impaired), based on fair value (as opposed to cost recovery using future undiscounted cash flows), (3) require that reporting units be identified for the purpose of assessing potential future impairments of goodwill and (4) remove the forty-year limitation on the amortization period of intangible assets that have finite lives.

Effective January 1, 2002 Hercules adopted the provisions of SFAS 142. Hercules identified the following reporting units: BetzDearborn and Pulp and Paper, Aqualon and FiberVisions. In connection with Hercules' transitional review, recorded goodwill was determined to be impaired in the BetzDearborn reporting unit. In the first quarter 2002, Hercules completed its transitional impairment review of the identified reporting units and recognized an after tax impairment loss of \$368 million as a cumulative effect of a change in accounting principle. As a result of Hercules' adoption of SFAS 142, the Company will no longer record approximately \$4 million of annual amortization relating to existing goodwill and intangibles.

Goodwill related to the BetzDearborn business was evaluated for impairment at December 31, 2001 under Statement of Financial Accounting Standards No. 121 "Accounting for the Impairment of Long-Fixed Assets and for Long-Lived Assets to Be Disposed of". Such evaluation indicated that goodwill associated with the business was recoverable from anticipated future undiscounted cash flows. Accordingly, no impairment loss was recorded in the December 31, 2001 financial statements.

In June 2001, the Financial Accounting Standards Board ("FASB") approved the issuance of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143"). SFAS 143 establishes accounting standards for the recognition and measurement of legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 will become effective for the Company on January 1, 2003 and requires recognition of a liability for an asset retirement obligation in the period in which it is incurred. The Company does not believe it will have a material effect on its financial statements.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company does not believe it will have a material effect on its financial statements.

HERCULES GB HOLDINGS LIMITED  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment to FASB Statement No. 13, and Technical Corrections." The Company elected to early adopt the provisions of SFAS 145 related to the rescission of SFAS 4, "Reporting Gains and Losses from the Extinguishment of Debt" ("SFAS 4"). The early adoption of SFAS 145 had no effect on the Company's financial statements.

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146"). SFAS 146 addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs in a Restructuring)". SFAS 146 defines the timing of the recognition of costs associated with exit or disposal activities, the types of costs that may be recognized and the methodology for calculating the fair value of such costs. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. The Company does not believe this statement will have a material effect on its financial statements.

RECLASSIFICATIONS

Certain amounts in the 2000 and 1999 consolidated financial statements and notes have been reclassified to conform to the 2001 presentation.

3. ACCOUNTS RECEIVABLE, NET

Accounts receivable, net, consists of:

	(Dollars in thousands)	
	2001	2000
	----	----
Trade	\$ 28,607	\$ 32,519
Other	2,204	3,863
	-----	-----
	30,811	36,382
Less allowance for doubtful accounts	\$ (2,208)	\$ (2,236)
	-----	-----
Total	\$ 28,603	\$ 34,146
	=====	=====

There are no single receivables which constitute more than 10% of the total.

4. INVENTORIES

The components of inventories are:

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousands)	
	2001	2000
	----	----
Finished products	\$ 3,027	\$ 4,904
Materials, supplies, and work in process	2,307	3,408
	-----	-----
Total	\$ 5,334	\$ 8,312
	=====	=====

5. SHORT-TERM DEBT

Short-term third party debt at December 31, 2000, consists of bank borrowings primarily representing overdraft facilities and short-term lines of credit, in the United Kingdom, which are generally payable on demand with interest at various rates. Book values of bank borrowings approximate market value because of their short maturity period. There was no third party debt outstanding at December 31, 2001.

At December 31, 2001, the Company and its subsidiaries had \$1,413 thousand of unused lines of credit that may be drawn as needed, with interest at a negotiated spread over lenders' cost of funds. Weighted-average interest rates on short-term borrowings at December 31, 2001 and 2000, were 7.5% and 6.5%, respectively.

228

HERCULES GB HOLDINGS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

6. LONG-TERM DEBT AND OTHER FINANCING ARRANGEMENTS

Hercules manages the Company's cash and indebtedness. The majority of the cash provided by or used by the Company is provided through this consolidated cash and debt management system. As a result, the amount of cash or debt historically related to the Company is not determinable. For purposes of the Company's historical financial statements all of the Company's positive or negative cash flows have been treated as cash transferred to or from the Hercules Group.

The Company has a number of intercompany loans with the Hercules Group in the amounts of \$126,330 thousand and \$145,393 thousand, which are included in the Net Hercules Group Investment balance as of December 31, 2001 and 2000, respectively.

Interest rates on these loans are detailed below:

	(Dollars in thousands)	
Interest rate	2001	2000
-----	----	----
Variable LIBOR plus 0.55%	\$ 90,075	\$ 92,519
Variable LIBOR plus 0.75%	36,255	47,666
Variable LIBOR plus 1.00%		5,138



## Edgar Filing: HERCULES INC - Form 10-K/A

Fixed 10%	--	70
	-----	-----
	\$126,330	\$145,393
	=====	=====

LIBOR is the London Inter-Bank Offer Rate.

All long-term debt with the Hercules Group has maturity dates after 2005.

The basis of valuation of long-term debt is the present value of expected cash flows related to existing borrowings discounted at rates currently available to the company for long-term borrowings with similar terms and remaining maturities.

### Fair Values

The following table presents the carrying amounts and fair values of the company's financial instruments at December 31, 2001 and 2000:

	(Dollars in thousands)			
	2001		2000	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
	-----	-----	-----	-----
Long-term debt	\$126,330	\$126,330	\$145,393	\$145,393

### 7. LONG-TERM INCENTIVE COMPENSATION PLANS

The Company participates in long-term incentive compensation plans sponsored by Hercules. These plans provide for the grant of stock options and the award of common stock and other market-based units to certain key employees and non-employee directors.

In 1995, Hercules changed the structure of the long-term incentive compensation plans to place a greater emphasis on shareholder value creation through grants of regular stock options, performance-accelerated stock options, and Cash Value Awards (performance-based awards denominated in cash and payable in shares of common or restricted stock, subject to the same restrictions as restricted stock). Restricted stock and other market-based units are awarded with respect to certain programs. The number of awarded shares outstanding was 189,704 at December 31, 2001, and 491,488 and 926,689 at December 31, 2000 and 1999, respectively.

At December 31, 2001, under Hercules' incentive compensation plans, 1,265,493 shares of common stock were available for grant as stock awards or stock option awards. Stock awards are limited to approximately 15% of the total authorizations. Regular stock options are granted at the market price on the date of grant and are exercisable at various periods from one to five years after date of grant. Performance-accelerated stock options are also granted at the market price on the date of grant and are normally exercisable at nine and one-half years. Exercisability may be accelerated

## Edgar Filing: HERCULES INC - Form 10-K/A

HERCULES GB HOLDINGS LIMITED  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

based upon the achievement of predetermined performance goals. Both regular and performance-accelerated stock options expire 10 years after the date of grant.

Restricted shares, options and performance-accelerated stock options are forfeited and revert to Hercules in the event of employment termination, except in the case of death, disability, retirement, or other specified events.

The Company applies APB Opinion 25 in accounting for its plans. Accordingly, no compensation cost has been recognized for the stock option plans. There were no charges to income for the cost of stock awards over the restriction or performance period for 2001, 2000 and 1999, respectively.

Below is a summary of outstanding stock option grants under the incentive compensation plans during 1999, 2000 and 2001:

	Regular	
	Number of Shares	Weighted-average price
December 31, 1998	17,750	\$ 40.27
Granted	22,550	\$ 37.75
Exercised	--	--
Forfeited	--	--
December 31, 1999	40,300	\$ 38.86
Granted	--	--
Exercised	--	--
Forfeited	--	--
December 31, 2000	40,300	\$ 38.86
Granted	--	--
Exercised	--	--
Forfeited	(3,800)	\$ 37.80
December 31, 2001	36,500	\$ 38.97

There were no performance-accelerated stock options granted or outstanding during 1999, 2000 and 2001.

The weighted-average fair value of regular stock options granted during 1999, 2000 and 2001 was \$8.26, \$0 and \$0, respectively.

Following is a summary of regular stock options exercisable at December 31, 1999, 2000 and 2001, and their respective weighted-average share prices:

	Number of Shares	Weighted-average price
Options Exercisable		

Edgar Filing: HERCULES INC - Form 10-K/A

December 31, 1999	13,540	\$	39.91
December 31, 2000	26,440	\$	39.32
December 31, 2001	32,730	\$	39.11

Following is a summary of stock options outstanding at December 31, 2001:

Exercise Price Range	Outstanding Options			Exercisable Number 12/31/2001
	Number Outstanding at 12/31/2001	Weighted-average Remaining Contractual Life	Weighted- average exercise price	
Regular Stock Options				
\$30 - \$40	34,850	6.53	\$38.55	31,000
\$40 - \$50	1,650	6.35	\$47.81	1,650
	----- 36,500 -----			----- 32,730 -----

The Company's employees may also participate in the Hercules Employee Stock Purchase Plan ("ESSP"). The ESSP is a qualified non-compensatory plan, which allows eligible employees to acquire shares of common stock through systematic payroll deductions. The plan consists of three-month subscription periods, beginning July 1 of each year. The purchase price is 85% of the fair market value of the common stock on either the first or last day of that subscription period, whichever is lower. Purchases may range from 2% to 15% of an employee's base salary each pay period, subject to certain limitations. Currently, there are no shares of Hercules common stock registered for offer and sale under the plan. Shares issued at December 31, 2001 and 2000, were 1,758,081 and 1,597,861, respectively. The Company applies APB Opinion 25 and related interpretations in accounting for its Employee Stock Purchase Plan. Accordingly, no compensation cost has been recognized for the Employee Stock Purchase Plan.

230

HERCULES GB HOLDINGS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Had compensation cost for Hercules' Stock-Based Incentive Plans and Employee Stock Purchase Plan been determined on the basis of fair value according to SFAS No. 123, the fair value of each option granted or share purchased would be estimated on the grant date using the Black-Scholes option pricing model.

The following weighted-average assumptions would be used in estimating fair value for 2001, 2000 and 1999:

Assumption	Regular Plan	Performance Accelerated Plan	Employee Stock Purchase Plan
------------	--------------	---------------------------------	---------------------------------

## Edgar Filing: HERCULES INC - Form 10-K/A

Dividend yield	0.96%	3.83%	0.0%
Risk-free interest rate	5.80%	5.57%	4.86%
Expected life	7.1 yrs.	5 yrs.	3 mos.
Expected volatility	33.36%	29.78%	49.11%

The Company's net income and earnings per share for 2001, 2000 and 1999 would approximate the pro forma amounts below:

	(Dollars in thousands)		
	2001	2000	1999
	----	----	----
Net (loss) income			
As reported	\$(11,065)	\$ (339)	\$ 6,055
Pro forma	\$(11,104)	\$ (399)	\$ 6,000

### 8. ADDITIONAL BALANCE SHEET DETAIL

	(Dollars in thousands)	
	2001	2000
	----	----
PROPERTY, PLANT, AND EQUIPMENT		
Land	\$ 1,395	\$ 1,864
Buildings and equipment	45,121	49,303
	-----	-----
Total	46,516	51,167
Accumulated depreciation and amortization	(22,004)	(21,480)
	-----	-----
Net property, plant, and equipment	\$ 24,512	\$ 29,687
	=====	=====

### ACCRUED EXPENSES

	(Dollars in thousands)	
	2001	2000
	----	----
Payroll and employee benefits	\$ 1,432	\$ 1,453
Income taxes payable	4,551	1,973
Restructuring liability (Note 10)	1,425	2,420
Other	1,915	1,420
	-----	-----
	\$ 9,323	\$ 7,266
	=====	=====

### 9. GOODWILL AND OTHER INTANGIBLES ASSETS

At December 31, 2001 and 2000, the goodwill and other intangible assets were:

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousands)	
	2001	2000
	----	----
Goodwill	\$ 130,878	\$ 146,363
Other intangibles	5,813	5,391
	-----	-----
Total	136,691	151,754
Less accumulated amortization	(15,439)	(12,597)
	-----	-----
Net goodwill and other intangible assets	\$ 121,252	\$ 139,157
	=====	=====

Goodwill and other intangible assets primarily represent amounts capitalized from the Hercules acquisition of BetzDearborn (Note 1).

231

HERCULES GB HOLDINGS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

-----

10. RESTRUCTURING

Coincident with the acquisition of BetzDearborn Inc. and its subsidiaries worldwide by Hercules in October 1998, plans were put in place to merge certain BetzDearborn and Hercules operations and support infrastructure, including facility closures and personnel reduction. The estimated costs of these plans was established as a liability as part of the overall purchase price allocation of the BetzDearborn acquisition, in accordance with purchase accounting methods. The principle constituent part of the restructuring reserves in the Company's accounts was the estimate for these exit and severance costs attributable to the Hercules operations in the United Kingdom. The remaining balance of these restructuring reserves, as reassessed during the year, was in excess of requirements, principally due to the cancellation of plans to transfer accounting activities to the Hercules European Shared Service Centre. This excess was written back as a reduction of original purchase cost and consequent goodwill on acquisition.

During the year, the company adopted Hercules plans to improve future profitability using "Work Process Redesign" methods. An estimate of severance costs to implement these plans was charged against income and established as additionally accrued restructuring reserves. The balance of these reserves was reassessed at the end of the year and the amount in excess of estimated remaining costs was released back to income.

For 2000, the severance and exit costs incurred include the costs for 9 employees, including 8 employees at the former Argo Scientific Limited office and workshop in Edinburgh, Scotland. For 2001, the severance and exit costs incurred include the costs for 25 employees associated with operations at Widnes, Cheshire, 18 from Sales and Marketing departments and 7 from other departments.

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousands)	
	2001	2000
	----	----
Balance at beginning of year	\$ 2,420	\$ 2,628
Additional accrual	2,122	363
Severance and exit costs incurred	(2,914)	(527)
Reversals	(203)	(44)
	-----	-----
Balance at end of year	\$ 1,425	\$ 2,420
	=====	=====

232

HERCULES GB HOLDINGS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

11. PENSION BENEFITS

The Company provides defined benefit pension plans to all eligible employees. The following chart lists benefit obligations, plan assets, and funded status of the plans.

	(Dollars in thousands)	
	Pension Benefits	
	2001	2000
	----	----
CHANGE IN BENEFIT OBLIGATION		
Benefit obligation at January 1	\$ 77,311	\$ 75,968
Service cost	1,571	2,092
Interest cost	4,941	4,189
Amendments	711	12
Employee contributions	710	760
Translation difference	(1,915)	(6,872)
Actuarial loss	11,658	3,154
Benefits paid from plan assets	(2,019)	(1,992)
	-----	-----
Benefit obligation at December 31	\$ 92,968	\$ 77,311
	=====	=====
CHANGE IN PLAN ASSETS		
Fair value of plan assets at January 1	87,229	89,389
Actual return on plan assets	(9,368)	5,143
Employee contributions	710	760
Company contributions	1,932	1,789
Actuarial loss	--	(1,748)
Translation difference	(2,370)	(6,112)
Benefits paid from plan assets	(2,019)	(1,992)
	-----	-----
Fair value of plan assets at December 31	\$ 76,114	\$ 87,229
	=====	=====
Funded status of the plans	(16,854)	9,918
Unrecognized actuarial loss (gain)	25,880	(2,176)
Unrecognized prior service cost	909	217

Edgar Filing: HERCULES INC - Form 10-K/A

Amendments	--	(174)
	-----	-----
Prepaid benefit cost	\$ 9,935	\$ 7,785
	=====	=====

AMOUNTS RECOGNIZED IN THE STATEMENT OF FINANCIAL POSITION CONSIST OF:

Additional minimum liability	\$ (22,139)	--
Intangible asset	1,050	--
Other comprehensive income	21,089	--
Prepaid benefit cost	9,935	7,785
	-----	-----
	\$ 9,935	\$ 7,785
	=====	=====

ASSUMPTIONS AS OF DECEMBER 31

Weighted-average discount rate	6.50%	6.50%
Expected average return on plan assets	7.00%	8.00%
Average rate of compensation increase	3.50%	3.75%

COMPONENTS OF NET PERIOD PENSION COST

(Dollars in thousands)  
Pension Benefits

	2001	2000	1999
	----	----	----
Service cost	\$ 1,571	\$ 2,092	\$ 2,313
Interest cost	4,941	4,189	4,326
Expected return on plan assets	(6,825)	(6,304)	(5,864)
Amortization and deferrals	19	(384)	269
Amortization of transition asset	--	(160)	(185)
	-----	-----	-----
Benefit (credit) cost	\$ (294)	\$ (567)	\$ 859
	=====	=====	=====

12. OTHER OPERATING EXPENSE, NET

Other operating expense, net, in 2001 includes \$7,194 thousand in net losses from the sale of the Company's hydrocarbon resins business, select portions of its rosin resins business, and its peroxy chemicals business. Furthermore, other operating expense, net includes Hercules Group affiliate royalty costs of \$5,664 thousand, net losses on asset sales of \$981 thousand, net restructuring costs of \$1,919 thousand, and foreign currency gains amounting to \$155 thousand.

HERCULES GB HOLDINGS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Other operating expenses, net, in 2000 include Hercules Group affiliate royalty costs of \$5,675 thousand, net restructuring costs of \$319 thousand, foreign currency gains amounting to \$444 thousand and other net losses amounting

## Edgar Filing: HERCULES INC - Form 10-K/A

to \$698 thousand.

Other operating expenses, net, in 1999 include Hercules Group affiliate royalty costs of \$5,902 thousand, net gains on restructuring reversals of \$357 thousand, foreign currency losses amounting to \$100 thousand and other net gains amounting to \$284 thousand.

### 13. INTEREST AND DEBT EXPENSE

Interest and debt costs incurred and expensed were as follows. No interest or debt costs were capitalised.

	(Dollars in thousands)		
	2001	2000	1999
	----	----	----
Intercompany interest expense	\$ 9,740	\$ 11,641	\$ 5,343
Third party interest expense	12	466	33
	-----	-----	-----
	\$ 9,752	\$ 12,107	\$ 5,376
	=====	=====	=====

### 14. OTHER INCOME (EXPENSE), NET

Other (expense) income, net, consists of the following:

	(Dollars in thousands)		
	2001	2000	1999
	----	----	----
Interest income	\$ 569	\$ 242	\$ 391
Miscellaneous (expense) income	(9)	(145)	174
	-----	-----	-----
	\$ 560	\$ 97	\$ 565
	=====	=====	=====

### 15. NET HERCULES GROUP INVESTMENT

Changes in net Hercules Group investment were as follows:-

Balance, January 1, 1999	\$ 230,375
Net income	6,055
Other comprehensive loss	(8,724)
Intercompany transactions, net	(9,597)
	-----
Balance, December 31, 1999	218,109
Net loss	(339)
Other comprehensive loss	(2,534)
Intercompany transactions, net	(24,523)
	-----
Balance, December 31, 2000	190,713
Net loss	(11,065)
Other comprehensive loss	(13,566)
Intercompany transactions, net	(13,015)



Edgar Filing: HERCULES INC - Form 10-K/A

Balance, December 31, 2001 -----  
\$ 153,067  
=====

The Company includes accumulated other comprehensive losses in Net Hercules Group Investment. At December 31, 2001, accumulated other comprehensive losses consisted of an additional minimum pension liability and foreign currency translation adjustments, net of tax, of \$(14,762) thousand and \$(5,192) thousand, respectively. At December 31, 2000 and 1999, accumulated other comprehensive losses consisted of foreign currency translation adjustments, net of tax, of \$(6,388) thousand and \$(3,854) thousand, respectively.

234

HERCULES GB HOLDINGS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
-----

16. TAXES

A summary of the components of the tax provision in respect of United Kingdom Corporation Tax follows:

	(Dollars in thousands)		
	2001	2000	1999
	----	----	----
Current	\$ 1,679	\$ 1,550	\$ 3,202
Deferred	(898)	410	1,615
	-----	-----	-----
Provision for income taxes	\$ 781	\$ 1,960	\$ 4,817
	=====	=====	=====

Deferred tax (liabilities) assets at December 31 consist of:

	(Dollars in thousands)	
	2001	2000
	----	----
Components of temporary differences		
-----		
Depreciation	\$ (5,703)	\$ (7,369)
Accrued (Prepaid) pension	11,118	(7,786)
Employee Intangible Asset	(4,943)	(4,757)
Net Operating Losses	10,491	--
Restructuring Provisions	477	2,284
Allowance for doubtful accounts	1,223	1,064
Other temporary differences	207	461
	-----	-----
Cumulative temporary differences	12,870	(16,103)
	-----	-----
Net deferred tax assets (liabilities)	\$ 3,861	\$ (4,831)
	=====	=====

## Edgar Filing: HERCULES INC - Form 10-K/A

A reconciliation of the statutory income tax rate to the effective rate follows:

	2001	2000	1999
	----	----	----
Statutory income tax rate	30.0%	30.0%	31%
Goodwill amortization	(32.1)	85.0%	11%
Other non-deductible expenses	(5.5)	6.0%	2%
	-----		
Effective tax rate	(7.6)%	121.0%	44%
	=====		

### 17. COMMITMENTS AND CONTINGENCIES

#### Leases

The Company has operating leases (including office space, transportation, and data processing equipment) expiring at various dates. Rental expense was \$2,348 thousand, \$2,981 thousand and \$2,759 thousand in 2001, 2000 and 1999 respectively.

At December 31, 2001, minimum rental payments under non-cancelable leases aggregated \$2,893 thousand. The net minimum payments over the next five years are \$1,527 thousand in 2002, \$915 thousand in 2003, \$427 thousand in 2004, \$24 thousand in 2005, and \$0 thousand in 2006.

#### Litigation

The Company currently and from time to time is involved in litigation incidental to the conduct of its business. In the opinion of the Company's management, none of such litigation as of December 31, 2001 is likely to have a material adverse effect on the financial position, results of operations, or cash flows of the Company.

### 18. RELATED PARTY TRANSACTIONS

The Company has entered into certain agreements with affiliated entities. These agreements were developed in the context of parent/subsidiary relationship and therefore may not necessarily reflect the result of arms-length negotiations between independent parties. The Company records sales with affiliates based on a cost-plus formula developed and agreed-upon by both parties. All transactions described below are eliminated on consolidation of Hercules Incorporated.

**Intercompany borrowing and interest:** The Company has intercompany loans with Hercules affiliated entities. The loans with affiliates are presented in Net Hercules Group Investment in the consolidated balance sheet. Interest paid to affiliated entities was \$3,175 thousand, \$11,641 thousand and \$5,343 thousand in 2001, 2000 and 1999, respectively.

**Corporate and other allocations:** As discussed in Note 1, the financial statements of the Company reflect certain allocated support costs incurred by other entities in the Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations and charges included in the Company's financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for

such

235

HERCULES GB HOLDINGS LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

services provided based on factors such as sales, net assets, costs of sales or a relative weighting of geographic activity. These allocations are reflected in the selling, general and administrative line item in our statement of income. Such allocations and corporate charges totaled \$8,745 thousand, \$5,921 thousand and \$6,314 thousand in 2001, 2000 and 1999, respectively.

**Royalties:** The Company entered into license agreements in respect of the use of manufacturing formulations and specifications which are developed and owned by other Hercules Group companies. The Company paid royalties in respect of these agreements of \$5,664 thousand, \$5,675 thousand and \$5,902 thousand in 2001, 2000 and 1999, respectively. The royalties are included as other operating expenses in the financial statements.

**Sales to affiliates:** The Company sells manufactured chemical products in the normal course of business to affiliated companies. Company's revenues from sales to affiliated companies were \$18,932 thousand, \$23,072 and \$22,334 thousand in 2001, 2000 and 1999, respectively.

**Purchases from affiliates:** The Company has commercial relationships with affiliated companies for the purchase of chemical products and raw materials. The value of these purchases were \$23,403 thousand, \$16,639 thousand and \$16,408 for 2001, 2000 and 1999, respectively.

19. DERIVATIVE INSTRUMENTS AND RISK MANAGEMENT

The Company enters into forward-exchange contracts to hedge currency exposure.

NOTIONAL AMOUNTS AND CREDIT EXPOSURE OF DERIVATIVES

The notional amounts of derivatives summarized below do not represent amounts exchanged by the parties and, thus, are not a measure of the exposure of the Company through its use of derivatives. The amounts exchanged are calculated on the basis of the notional amounts and the other terms of the derivatives, which relate to interest rates or exchange rates.

FOREIGN EXCHANGE RISK MANAGEMENT

The Company has selectively used foreign currency forward contracts to offset the effects of exchange rate changes on reported earnings, cash flow, and net asset positions. The primary exposures are denominated in the U.S. Dollar and the British Pound Sterling. Some of the contracts involve the exchange of two foreign currencies, according to local needs in foreign subsidiaries. The term of the currency derivatives is rarely more than three months. At December 31, 2001, the Company had outstanding forward-exchange contracts to purchase foreign currencies aggregating \$6,418 thousand, and to sell foreign currencies aggregating \$6,414 thousand. The Company had no material outstanding forward-exchange contracts at December 31, 2000. The foreign exchange contracts outstanding at December 31, 2001 will mature during 2002.

## Edgar Filing: HERCULES INC - Form 10-K/A

### FAIR VALUES

The following table presents the carrying amounts and fair values of the Company's financial instruments at December 31, 2001 and 2000:

	(Dollars in thousands)	
	2001	
	Carrying Amount	Fair Value
Foreign exchange contracts	\$ (3)	\$ (3)

The carrying amount represents the net unrealized gain or net interest payable associated with the contracts at the end of the period. Fair values of derivative contracts are indicative of cash that would have been required had settlement been December 31, 2001. Foreign exchange contracts are valued based on year-end exchange rates.

### 20. SUBSEQUENT EVENT

On April 29, 2002, Hercules completed the sale of its Water Treatment Business to GE Specialty Materials (GESM). Pursuant to the Stock and Asset Agreement for the transaction, the sale included all of the stock of BetzDearborn and the Company. Hercules used the proceeds from the sale to prepay borrowings under its Senior Credit Facility and ESOP Credit Facility. Pursuant to the prepayment, among other things, the stock pledges were released.

236

### REPORT OF INDEPENDENT ACCOUNTANTS

TO THE SHAREHOLDERS AND THE BOARD OF DIRECTORS OF  
HERCULES INCORPORATED  
WILMINGTON, DELAWARE

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income and comprehensive income and of cash flows present fairly, in all material respects, the financial position of Hercules International Limited, a subsidiary of Hercules Incorporated, and its subsidiaries at December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our

Edgar Filing: HERCULES INC - Form 10-K/A

audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP  
Philadelphia, Pennsylvania  
November 12, 2002

237

HERCULES INTERNATIONAL LIMITED  
CONSOLIDATED STATEMENT OF INCOME AND COMPREHENSIVE INCOME

	(Dollars in thousands)	
	Year Ended December 31	
	2001	2000
	----	----
Sales to third parties	\$ 572,859	\$ 791,771
Sales to Hercules Group	49,459	93,717
	-----	-----
	622,318	885,488
Cost of sales	376,908	530,321
Selling, general, and administrative expenses	140,310	153,928
Research and development	14,057	19,977
Goodwill and intangible asset amortization	6,166	8,292
Other operating expenses (income), net (Note 13)	10,064	(131,749)
	-----	-----
Profit from operations	74,813	304,719
Interest and debt expense (Note 14)	3,077	8,028
Other income, net (Note 15)	34,101	12,714
	-----	-----
Income before income taxes, equity (loss) income and minority interest, net	105,837	309,405
Provision for income taxes (Note 16)	45,906	119,794
	-----	-----
Income before equity (loss) income and minority interest, net	59,931	189,611
Equity (loss) income of affiliated companies	(10,026)	(3,891)
Minority interest, net	(1,328)	(1,107)
	-----	-----
Net income	48,577	184,613
Additional minimum pension liability, net of tax of \$(1,036)	(1,646)	--
Foreign currency translation, net of tax of \$0 for each year	(28,164)	(100,135)
	-----	-----
Comprehensive (loss) income	\$ 18,767	\$ 84,478
	=====	=====

The accompanying notes are an integral part of the consolidated  
financial statements

238

HERCULES INTERNATIONAL LIMITED  
CONSOLIDATED BALANCE SHEETS

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousands)	
	December 31,	
	2001	2000
	----	----
ASSETS		
Current assets		
Cash and cash equivalents	\$ 17,585	\$ 14,340
Accounts receivable, net (Note 3)	128,951	149,346
Inventories (Note 4)	49,526	79,787
Deferred income taxes (Note 16)	2,533	2,669
	-----	-----
Total current assets	198,595	246,142
	-----	-----
Property, plant, and equipment, net (Note 9)	216,488	275,325
Investments in affiliates (Note 5)	19,565	30,279
Goodwill and other intangible assets, net (Note 10)	207,689	224,443
Deferred charges and other assets	10,194	12,696
	-----	-----
Total assets	\$ 652,531	\$ 788,885
	=====	=====
LIABILITIES AND NET HERCULES GROUP INVESTMENT		
Current liabilities		
Accounts payable	\$ 78,700	\$ 94,908
Short-term debt (Note 6)	5,144	91,007
Accrued expenses (Note 9)	107,236	118,162
	-----	-----
Total current liabilities	191,080	304,014
Long-term debt - third parties (Note 7)	264	75
Deferred income taxes (Note 16)	65,009	59,841
Pension liability (Note 12)	25,850	20,066
Deferred credits and other liabilities	3,720	2,031
	-----	-----
Total liabilities	285,923	386,090
Commitments and contingencies (Note 17)		
Minority Interest	18,555	18,599
Net Hercules Group Investment (Note 20)		
Accumulated other comprehensive losses	(170,615)	(140,805)
Intercompany transactions, net	518,668	525,001
	-----	-----
Total Net Hercules Group Investment	348,053	384,196
	-----	-----
Total liabilities and Net Hercules Group Investment	\$ 652,531	\$ 788,885
	=====	=====

The accompanying notes are an integral part of the consolidated  
financial statements

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in Year Ended D	
	2001	2000
	----	----
CASH FLOW FROM OPERATING ACTIVITIES:		
Net Income	\$ 48,577	\$ 184
Adjustments to reconcile net income to net cash provided by operations:		
Depreciation and amortization of property, plant and equipment	20,774	28
Amortization of goodwill and other intangible assets	6,166	8
Restructuring plans	3,876	3
Deferred income tax	10,470	13
Loss on disposals of property, plant and equipment	1,608	1
Gain on sale of investments	(15,731)	(167)
Equity loss (income) of affiliates	10,026	3
Dividends received	593	
Minority interest, net	1,328	1
Corporate and other cost allocations	19,053	13
Accruals and deferrals of cash receipts and payments:		
Accounts receivable	12,269	3
Inventories	1,868	(11)
Accounts payable and accrued expenses	(23,858)	37
Noncurrent assets and liabilities	6,811	(1)
Net transfers from (to) Hercules Group	17,152	69
	-----	-----
Net cash provided by operations	120,982	187
	-----	-----
CASH FLOW FROM INVESTING ACTIVITIES:		
Capital expenditures, net of proceeds from sale	(17,554)	(68)
Proceeds from sale of investment	--	
Purchase of equity method investments	--	
	-----	-----
Net cash used in investing activities	(17,554)	(68)
	-----	-----
CASH FLOW FROM FINANCING ACTIVITIES:		
Change in short-term debt	(84,302)	78
Long-term debt repayments	--	
Proceeds from issuance of long-term debt	193	41
Net transfers (to) from Hercules Group	(16,030)	(239)
	-----	-----
Net cash used in financing activities	(100,139)	(119)
	-----	-----
Effect of exchange rate changes on cash	(44)	(1)
	-----	-----
Net increase (decrease) in cash and cash equivalents	3,245	(1)
Cash and cash equivalents at beginning of year	14,340	16
	-----	-----
Cash and cash equivalents at end of year	17,585	14
	=====	=====
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the year for:		
Interest (net of amount capitalized)	\$ 3,737	\$ 7
Income taxes, net	15,088	65
Noncash investing and financing activities:		
Sale of investment in CP Kelco ApS (Note 13)	--	119
Corporate and other cost allocations	19,053	13

HERCULES INTERNATIONAL LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## 1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

Hercules International Limited (the "Company") is a subsidiary of Hercules Incorporated (ultimate parent) ("Hercules"). Hercules and its wholly owned subsidiaries comprise the Hercules Group. The Company supplies engineered process and water treatment chemical programs, as well as products that manage the properties of aqueous systems, for industrial, commercial and institutional establishments. These products and services contribute to preserving or enhancing productivity, reliability and efficiency in plant operations and in complying with environmental regulations.

When Hercules acquired all of the outstanding shares of BetzDearborn Inc. on October 15, 1998 it paid \$2,235 million in cash and \$186 million in common stock exchanged for the shares held by the BetzDearborn ESOP Trust. The purchase price allocated to the Company and its subsidiaries was approximately \$682 million. During 1999, Hercules completed the purchase price allocation and the final determination of goodwill was \$2,170 million of which the amount attributable to the Company was approximately \$278 million. These financial statements include the push down of fair value adjustments to assets and liabilities, including goodwill, other intangible assets and property, plant and equipment and their related amortization and depreciation adjustments.

As a result of the Hercules acquisition of BetzDearborn Inc., the Company entered into several internal reorganization transactions during 1999 and 2000. The transactions included the Company selling several of its investments in subsidiaries to Hercules affiliates, purchasing several investments in subsidiaries from Hercules affiliates, merging companies, and acquiring certain investments in Hercules group companies that are valued at cost. As all investments in this reorganization are under the common control of Hercules, these transactions have been accounted for in a manner similar to pooling of interests.

Prior to the 2000 fiscal year, separate company stand-alone financial statements were not prepared for the Company. In November 2000, Hercules amended its senior credit facility and ESOP credit facility (the "Facilities"). The Facilities, as amended, are secured by liens on Hercules' property and assets (and those of Hercules' Canadian Subsidiaries), a pledge of the stock of substantially all of Hercules' domestic subsidiaries (including the Company) and 65% of the stock of foreign subsidiaries directly owned by Hercules, and a pledge of Hercules' domestic intercompany indebtedness. These consolidated financial statements present the financial information of the Company, a collateral party to the Hercules debt, based on Hercules' understanding of the Securities and Exchange Commission's interpretation and application of Rule 3-16 under the Securities and Exchange Commission's Regulation S-X. These statements were derived from historical accounting records.

On April 29, 2002, in connection with Hercules' sale of its Water Treatment Business (see Note 21) and the repayment of the Facilities, the stock pledges were released. As a result, based on Hercules' current debt structure, these separate company stand-alone financial statements will not be required for the fiscal year ending December 31, 2002.



## Edgar Filing: HERCULES INC - Form 10-K/A

The consolidated financial statements of the Company reflect certain allocated support costs incurred by the Hercules Group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations and charges included in the Company's consolidated financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on factors such as sales, net assets, or cost of sales; or a relative weighting of geographic activity. Management believes that the allocation method is reasonable. See Note 18 for more information.

A number of the operating companies participate in Hercules' centralized cash management system. Accordingly, cash received from operations may be transferred to Hercules on a periodic basis, and Hercules funds operational and capital requirements upon request.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its majority-owned subsidiaries where control exists. Following the acquisition of BetzDearborn by Hercules in 1998, the Company continued BetzDearborn's practice of using a November 30 fiscal year end for certain former BetzDearborn Inc. non-U.S. subsidiaries to expedite the year end closing process. All intercompany transactions and profits have been eliminated.

241

#### HERCULES INTERNATIONAL LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

#### USE OF ESTIMATES

Preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

#### REVENUE RECOGNITION

The Company recognizes revenue when the earnings process is complete. This generally occurs when products are shipped to the customer or services are performed in accordance with terms of the agreement, title and risk of loss have been transferred, collectibility is probable, and pricing is fixed and determinable. Accruals are made for sales returns and other allowances based on the Company's experience. The corresponding shipping and handling costs are included in cost of sales.

#### RESEARCH AND DEVELOPMENT EXPENDITURES

Research and development expenditures are expensed as incurred.

#### ENVIRONMENTAL EXPENDITURES

Environmental expenditures that pertain to current operations or future

## Edgar Filing: HERCULES INC - Form 10-K/A

revenues are expensed or capitalized according to the Company's capitalization policy. Expenditures for remediation of an existing condition caused by past operations that do not contribute to current or future revenues are expensed. Liabilities are recognized for remedial activities when the cleanup is probable and can be reasonably estimated.

### CASH AND CASH EQUIVALENTS

Cash in excess of operating requirements is invested in short-term, income-producing instruments. Cash equivalents include commercial paper and other securities with original maturities of 90 days or less. Book value approximates fair value because of the short maturity of those instruments.

### INVENTORIES

Inventories are stated at the lower of cost or market. Inventories are valued on the average cost method.

### PROPERTY AND DEPRECIATION

Property, plant, and equipment are stated at cost. The Company changed to the straight-line method of depreciation, effective January 1, 1991, for newly acquired processing facilities and equipment. Assets acquired before then continue to be depreciated by accelerated methods. The Company believes straight-line depreciation provides a better matching of costs and revenues over the lives of the assets. The estimated useful lives of depreciable assets are as follows: buildings - 30 years; plant, machinery and equipment - 15 years; other machinery and equipment - 3 to 15 years.

Maintenance, repairs, and minor renewals are charged to income; major renewals and betterments are capitalized. Upon normal retirement or replacement, the net book value of property (less proceeds of sale or salvage) is charged to income.

### INVESTMENTS

Investments in affiliated companies with a 20% or greater ownership interest in which the Company has significant influence are accounted for using the equity method of accounting. Accordingly, these investments are included in investments in affiliates on the Company's balance sheet and the income or loss from these investments is included in equity in (loss) income of affiliated companies in the Company's statement of income.

### GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill and other intangible assets are amortized on a straight-line basis over the estimated future periods to be benefited, generally 40 years for goodwill, customer relationships, and trademarks and tradenames and 5 to 15 years for other intangible assets. Pursuant to Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (SFAS 142), beginning January 1, 2002, goodwill will not be amortized but will be tested for

242

HERCULES INTERNATIONAL LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

impairment annually and any necessary adjustment charged to expense. Intangible assets with finite lives will be amortized over their useful lives.

## Edgar Filing: HERCULES INC - Form 10-K/A

### LONG-LIVED ASSETS

The Company reviews its long-lived assets, including goodwill and other intangibles, for impairment on an exception basis whenever events or changes in circumstances indicate carrying amounts of the assets may not be recoverable through undiscounted future cash flows. If an impairment loss has occurred based on expected future cash flows (undiscounted), the loss is recognized in the income statement. The amount of the impairment loss is the excess of the carrying amount of the impaired asset over the fair value of the asset. The fair value represents expected future cash flows from the use of the assets, discounted at the rate used to evaluate potential investments.

### INCOME TAXES

Income tax expense in the accompanying consolidated financial statements has been computed assuming the Company filed separate income tax returns.

The provisions for income taxes has been determined using the asset and liability approach of accounting for income taxes. Under this approach, deferred taxes represent the future tax consequences expected to occur when the reported amounts of assets and liabilities are recovered or paid. The provision for income taxes represents income taxes paid or payable for the current year plus the change in deferred taxes during the year. Deferred taxes result from differences between the financial and tax basis of the Company's assets and liabilities and are adjusted for changes in tax rates and tax laws when changes are enacted. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized.

The company provides taxes on undistributed earnings of subsidiaries and affiliates included in consolidated retained earnings to the extent such earnings are planned to be remitted and not re-invested permanently. The undistributed earnings/(loss) of subsidiaries and affiliates on which no provision for foreign withholding or US income taxes has been made amounted to approximately \$25,645 thousand, \$(7,730) thousand and \$9,273 thousand at December 31, 2001, 2000 and 1999, respectively. US and foreign income taxes that would be payable if such earnings were distributed may be lower than the amount computed at the US statutory rate because of the availability of tax credits.

### FOREIGN CURRENCY TRANSLATION AND TRANSACTIONS

The accompanying consolidated financial statements are reported in U.S. dollars. The US dollar is the functional currency for the Company. The translation of the functional currencies of the Company's subsidiaries into U.S. dollars (reporting currency) is performed for assets and liabilities using the current exchange rates in effect at the balance sheet date, and for revenues, costs and expenses using average exchange rates prevailing during the reporting periods. Adjustments resulting from the translation of functional currency financial statements to reporting currency are accumulated and reported as other comprehensive income (loss), a separate component of Net Hercules Group Investment.

Transactions in foreign currency are recorded at the exchange rate prevailing on the date of transaction. Monetary assets and liabilities denominated in foreign currencies are expressed in the functional currency at the exchange rates in effect at the balance sheet date. Revenues, costs and expenses are recorded using average exchange rates prevailing during the reporting periods. Gains or losses resulting from foreign currency transactions are included in the statement of income.

### CONCENTRATIONS OF CREDIT RISK

## Edgar Filing: HERCULES INC - Form 10-K/A

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of trade receivables and receivables from affiliated companies, which are included in the Net Hercules Group Investment in the consolidated balance sheet. Concentrations of credit risk with respect to trade receivables are limited due to the Company's large number of customers and their dispersion across many different industries and locations.

### DERIVATIVE INSTRUMENTS AND HEDGING

On January 1, 2001, the Company adopted Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"). SFAS 133, as amended by Statement No. 137, "Accounting for Derivative Instruments and Hedging Activities-Deferral of the Effective Date of FASB Statement No.

243

### HERCULES INTERNATIONAL LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

133" and Statement No. 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities," requires that all derivative instruments be recorded on the balance sheet at their fair value. The Company has not designated any derivative as a hedge instrument and accordingly, changes in fair value of derivatives are recorded each period in earnings. The adoption of SFAS 133 did not result in a pre-tax or post-tax cumulative-effect-type adjustment to income and did not result in a change to other comprehensive income (loss).

Derivative financial instruments have been used to hedge risk caused by fluctuating currency. The Company enters into forward-exchange contracts to hedge foreign currency exposure. Decisions regarding hedging are made on a case-by-case basis, taking into consideration the amount and duration of the exposure, market volatility, and economic trends. The Company uses the fair-value method of accounting, recording to other income (expense), net realized and unrealized gains and losses on these contracts monthly, except for gains and losses on contracts to hedge specific foreign currency commitments, which are deferred and accounted for as part of the transaction. Gains or losses on instruments which have been used to hedge the value of investments in certain non-U.S. subsidiaries have been accounted for under the deferral method and are included in the foreign currency translation adjustment. It is the Company's policy to match the term of financial instruments with the term of the underlying designated item. If the designated item is an anticipated transaction no longer likely to occur, gains or losses from the instrument designated as a hedge are recognized in current period earnings. The Company does not hold or issue financial instruments for trading purposes. In the consolidated statement of cash flow, the Company reports the cash flows resulting from its hedging activities in the same category as the related item that is being hedged.

### STOCK-BASED COMPENSATION

Compensation costs attributable to stock option and similar plans are recognized based on any excess of the quoted market price of the stock on the date of grant over the amount the employee is required to pay to acquire the stock (the intrinsic-value method under Accounting Principles Board Opinion 25 (APB 25)). Such amount, if any, is accrued over the related vesting period, as appropriate. Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation," requires companies electing to continue to use the intrinsic-value method to make pro forma disclosures of net income as if the

## Edgar Filing: HERCULES INC - Form 10-K/A

fair-value-based method of accounting had been applied.

### MINORITY INTEREST

Minority interest at December 31, 2001 and 2000 represents a 38.97% proportionate share of the equity of Hercules Quimica S.A., owned by a Hercules Group affiliate.

### COMPUTER SOFTWARE COSTS

Effective January 1, 1999, the Company adopted the American Institute of Certified Public Accountants Statement of Position 98-1, "Accounting for the Cost of Computer Software Developed or Obtained for Internal Use" (SOP 98-1). The prior accounting was generally consistent with the requirements of SOP 98-1 and, accordingly, adoption of SOP 98-1 had no material effect. Computer software costs are being amortized over a period of 5 to 10 years.

### NET HERCULES GROUP INVESTMENT

The Net Hercules Group Investment account reflects the balance of the Company's historical earnings, intercompany amounts, foreign currency translation and other transactions between the Company and the Hercules Group.

### NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 141, "Business Combinations" ("SFAS 141"), and Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"). SFAS 141 supersedes Accounting Principles Board Opinion ("APB") No. 16, Business Combinations. The provisions of SFAS 141 (1) require that the purchase method of accounting be used for all business combinations initiated after June 30, 2001, (2) provide specific criteria for the initial recognition and measurement of intangible assets apart from goodwill and (3) require that unamortized negative goodwill be written off immediately as extraordinary gain instead of being deferred and amortized. SFAS 141 also requires that upon adoption of SFAS 142 the Company reclassify the carrying amounts of certain intangible assets into or out of goodwill, based on certain criteria. SFAS 142 supersedes APB No. 17, Intangible Assets, and is effective for fiscal years beginning after December 15, 2001. SFAS 142 primarily addresses the accounting for goodwill and

244

### HERCULES INTERNATIONAL LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

-----

intangible assets subsequent to their initial recognition. The provisions of SFAS 142 (1) prohibit the amortization of goodwill and indefinite-lived intangible assets, (2) require that goodwill and indefinite-lived intangible assets be tested annually for impairment (and in interim periods if certain events occur indicating that the carrying value of goodwill and/or indefinite-lived intangible assets may be impaired), based on fair value (as opposed to cost recovery using future undiscounted cash flows), (3) require that reporting units be identified for the purpose of assessing potential future impairments of goodwill and (4) remove the forty-year limitation on the amortization period of intangible assets that have finite lives.

Effective January 1, 2002 Hercules adopted the provisions of SFAS 142. Hercules identified the following reporting units: BetzDearborn and Pulp and

## Edgar Filing: HERCULES INC - Form 10-K/A

Paper, Aqualon and FiberVisions. In connection with Hercules' transitional review, recorded goodwill was determined to be impaired in the BetzDearborn reporting unit. In the first quarter 2002, Hercules completed its transitional impairment review of the identified reporting units and recognized an after tax impairment loss of \$368 million as a cumulative effect of a change in accounting principle. As a result of Hercules' adoption of SFAS 142, the Company will no longer record approximately \$6.2 million of annual amortization relating to existing goodwill and intangibles.

Goodwill related to the BetzDearborn business was evaluated for impairment at December 31, 2001 under Statement of Financial Accounting Standards No. 121 "Accounting for the Impairment of Long-Fixed Assets and for Long-Lived Assets to Be Disposed of". Such evaluation indicated that goodwill associated with the business was recoverable from anticipated future undiscounted cash flows. Accordingly, no impairment loss was recorded in the December 31, 2001 financial statements.

In June 2001, the Financial Accounting Standards Board ("FASB") approved the issuance of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143"). SFAS 143 establishes accounting standards for the recognition and measurement of legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 will become effective for the Company on January 1, 2003 and requires recognition of a liability for an asset retirement obligation in the period in which it is incurred. The Company does not believe it will have a material effect on its financial statements.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company does not believe it will have a material effect on its financial statements.

In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment to FASB Statement No. 13, and Technical Corrections." The Company elected to early adopt the provisions of SFAS 145 related to the rescission of SFAS 4, "Reporting Gains and Losses from the Extinguishment of Debt" ("SFAS 4"). The early adoption of SFAS 145 had no effect on the Company's financial statements.

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146"). SFAS 146 addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs in a Restructuring)". SFAS 146 defines the timing of the recognition of costs associated with exit or disposal activities, the types of costs that may be recognized and the methodology for calculating the fair value of such costs. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. The Company does not believe this statement will have a material effect on its financial statements.

### RECLASSIFICATIONS

Certain amounts in the 2000 and 1999 consolidated financial statements and notes have been reclassified to conform to the 2001 presentation.

## Edgar Filing: HERCULES INC - Form 10-K/A

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

#### 3. ACCOUNTS RECEIVABLE, NET

Accounts receivable, net, consists of:

	(Dollars in thousands)	
	2001	2000
	----	----
Trade	\$ 123,410	\$ 138,464
Other	8,610	13,634
	-----	-----
	132,020	152,098
Less allowance for doubtful accounts	(3,069)	(2,752)
	-----	-----
Total	\$ 128,951	\$ 149,346
	=====	=====

Other accounts receivable mainly comprise VAT receivable.

#### 4. INVENTORIES

The components of inventories are:

	(Dollars in thousands)	
	2001	2000
	----	----
Finished products	\$ 32,579	\$ 54,573
Materials, supplies, and work in process	16,947	25,214
	-----	-----
Total	\$ 49,526	\$ 79,787
	=====	=====

#### 5. INVESTMENTS

The Company has various equity investments in companies, as described below. Summarized financial information for these equity affiliates at December 31, and for the years then ended is as follows:

	(Dollars in thousands)	
	2001	2000
	----	----
Current assets	\$241,134	\$269,814
Non-current assets	890,455	942,946
Current liabilities	\$ 81,123	\$109,486
Non-current liabilities	725,523	730,579

## Edgar Filing: HERCULES INC - Form 10-K/A

	2001 ----	2000 ----	1999 ----
Net sales	\$ 471,411	\$ 143,245	\$ 56,410
Gross profit	148,987	17,290	14,489
Net (losses) earnings	(50,021)	(15,864)	5,865

At December 31, 2001, the Company's equity investments, all affiliates of Hercules consisted of a 50% ownership of Abieta Chemie GmbH and BetzDearborn Nippon KK, a 49% ownership of Hercules Mas Indonesia, and a 28.57% ownership of the consolidated group CP Kelco ApS. The Company's carrying value for these investments at December 31, 2001 and 2000 equals its share of the underlying equity in net assets of the respective affiliates. Dividends paid to the Company from its equity investees were \$593 thousand, \$579 thousand, \$3,093 thousand during 2001, 2000, 1999, respectively. Except for CP Kelco ApS, each of these entities operates in lines of business similar to the Company, supplying engineered process and water treatment chemical programs, as well as products that manage the properties of aqueous systems, for industrial, commercial and institutional establishments. As discussed further in Note 13, CP Kelco ApS was the Company's Food Gums business that was divested in 2000.

246

HERCULES INTERNATIONAL LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

6. SHORT-TERM DEBT AND OTHER FINANCING ARRANGEMENTS

Short-term debt of \$5,144 thousand and \$91,007 thousand at December 31, 2001 and 2000, respectively, consists of bank borrowings primarily representing foreign overdraft facilities and short-term lines of credit, which are generally payable on demand with interest at various rates. Book values of bank borrowings approximate market value because of their short maturity period.

Short-term debt with affiliates of \$3,539 thousand and \$32,685 thousand at December 31, 2001 and 2000, respectively, is recorded in Net Hercules Group Investment in the consolidated balance sheet.

At December 31, 2001 and 2000, the Company had \$7,155 thousand and \$34,774 thousand, respectively, of unused lines of credit that may be drawn as needed, with interest at a negotiated spread over lenders' cost of funds. Lines of credit in use at December 31, 2001 and 2000 were \$3,860 thousand and \$91,007 thousand, respectively.

Weighted-average interest rates on all short-term borrowings at December 31, 2001 and 2000 were 4.40% and 5.60%, respectively.

7. LONG-TERM DEBT AND OTHER FINANCING ARRANGEMENTS

Long-term debt with third parties and affiliates at December 31, 2001 and 2000 is summarized as follows:

(Dollars in thousand)  
2001                      2000



Edgar Filing: HERCULES INC - Form 10-K/A

	----	----
5.72% third party note	\$ 309	\$ 93
Other	24	45
	-----	-----
Less current maturities	69	63
	-----	-----
Total long-term debt, third party	264	75
	-----	-----
5.51% affiliate note	21,799	22,853
5.80% affiliate note	19,496	20,516
	-----	-----
Less current maturities	--	--
	-----	-----
Total long-term debt, affiliates	41,295	43,369
	-----	-----
Total long term debt, third party and affiliates	\$ 41,559	\$ 43,444
	=====	=====

Long-term debt with affiliates, which is recorded in Net Hercules Group Investment in the consolidated balance sheet, has no stated maturity. Third party long-term debt at December 31, 2001 matures as follows: \$69 thousand, \$48 thousand, \$50 thousand, \$53 thousand and \$113 thousand in the years 2002, 2003, 2004, 2005 and 2006 and thereafter, respectively. The fair value of the Company's long-term debt was \$41,559 thousand at December 31, 2001 and \$43,444 thousand at December 31, 2000. The Company believes that the carrying value of long-term debt borrowings approximates fair value, based on discounting future cash flows using rates currently available for debt of similar terms and remaining maturities.

8. LONG-TERM INCENTIVE COMPENSATION PLANS

The Company participates in long-term incentive compensation plans sponsored by Hercules. These plans provide for the grant of stock options and the award of common stock and other market-based units to certain key employees and non-employee directors.

In 1995, Hercules changed the structure of the long-term incentive compensation plans to place a greater emphasis on shareholder value creation through grants of regular stock options, performance-accelerated stock options, and Cash Value Awards (performance-based awards denominated in cash and payable in shares of common or restricted stock, subject to the same restrictions as restricted stock). Restricted stock and other market-based units are awarded with respect to certain programs. The number of awarded shares outstanding was 189,704 at December 31, 2001, and 491,488 and 929,689 at December 31, 2000 and 1999, respectively.

At December 31, 2001, under Hercules' incentive compensation plans, 1,265,493 shares of common stock were available for grant as stock awards or stock option awards. Stock awards are limited to approximately 15% of the total authorizations. Regular stock options are granted at the market price on the date of grant and are exercisable at various

## Edgar Filing: HERCULES INC - Form 10-K/A

periods from one to five years after date of grant. Performance-accelerated stock options are also granted at the market price on the date of grant and are normally exercisable at nine and one-half years. Exercisability may be accelerated based upon the achievement of predetermined performance goals. Both regular and performance-accelerated stock options expire 10 years after the date of grant.

Restricted shares, options and performance-accelerated stock options are forfeited and revert to Hercules in the event of employment termination, except in the case of death, disability, retirement, or other specified events.

The Company applies APB Opinion 25 in accounting for its plans. Accordingly, no compensation cost has been recognized for the stock option plans. There were no charges to income for the cost of stock awards over the restriction or performance period for 2001, 2000 and 1999, respectively.

Below is a summary of outstanding stock option grants under the incentive compensation plans during 1999, 2000 and 2001:

	Regular		Performance-Accelerated	
	Number of Shares	Weighted-average price	Number of Shares	Weighted-average price
December 31, 1998	448,390	\$ 39.56	101,100	\$ 45.34
Granted	219,175	\$ 37.53	68,525	\$ 37.35
Exercised	--	--	--	--
Forfeited	--	--	(900)	\$ 45.73
December 31, 1999	667,565	\$ 38.89	168,725	\$ 42.09
Granted	162,875	\$ 17.25	--	\$ --
Exercised	--	--	--	--
Forfeited	(19,650)	\$ 36.82	(1,350)	\$ 37.56
December 31, 2000	810,790	\$ 34.59	167,375	\$ 42.13
Granted	102,000	\$ 11.28	--	\$ --
Exercised	--	--	--	--
Forfeited	(60,460)	\$ 30.85	(900)	\$ 45.73
December 31, 2001	852,330	\$ 32.07	166,475	\$ 42.11

The weighted-average fair value of regular stock options granted during 1999, 2000 and 2001 was \$8.25, \$8.85 and \$5.69, respectively. The weighted-average fair value of performance-accelerated stock options granted during 1999, 2000 and 2001 was \$7.99, \$0 and \$0.

Following is a summary of regular stock options exercisable at December 31, 1999, 2000, and 2001, and their respective weighted-average share prices:

Options Exercisable	Number of Shares	Weighted-average exercise price
December 31, 1999	306,825	\$39.84
December 31, 2000	561,295	\$37.20

Edgar Filing: HERCULES INC - Form 10-K/A

December 31, 2001

654,195

\$36.38

There were no performance-accelerated stock options exercisable at December 31, 2001.

248

HERCULES INTERNATIONAL LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Following is a summary of stock options outstanding at December 31, 2001:

Exercise Price Range	Outstanding Options		
	Number Outstanding at 12/31/2001	Weighted-average Remaining Contractual Life	Weighted-average exercise price
Regular Stock Options			
\$11 - \$20	240,025	8.78	\$14.71
\$20 - \$30	54,525	6.67	\$25.56
\$30 - \$40	474,255	6.23	\$38.68
\$40 - \$50	74,125	6.11	\$47.81
\$50 - \$60	9,400	4.11	\$55.38
	852,330		
Performance-Accelerated Stock Options			
\$14 - \$40	102,250	6.68	\$37.92
\$40 - \$50	56,125	5.85	\$47.82
\$50 - \$61	8,100	4.11	\$55.38
	166,475		

The Company's employees may also participate in the Hercules Employee Stock Purchase Plan ("ESSP"). The ESSP is a qualified non-compensatory plan, which allows eligible employees to acquire shares of common stock through systematic payroll deductions. The plan consists of three-month subscription periods, beginning July 1 of each year. The purchase price is 85% of the fair market value of the common stock on either the first or last day of that subscription period, whichever is lower. Purchases may range from 2% to 15% of an employee's base salary each pay period, subject to certain limitations. Currently, there are no shares of Hercules common stock are registered for offer and sale under the plan. Shares issued at December 31, 2001 and 2000, were 1,758,081 and 1,597,861, respectively. The Company applies APB Opinion 25 and related interpretations in accounting for its Employee Stock Purchase Plan. Accordingly, no compensation cost has been recognized for the Employee Stock Purchase Plan.

Had compensation cost for Hercules' Stock-Based Incentive Plans and Employee Stock Purchase Plan been determined on the basis of fair value according to SFAS No. 123, the fair value of each option granted or share

## Edgar Filing: HERCULES INC - Form 10-K/A

purchased would be estimated on the grant date using the Black-Scholes option pricing model.

The following weighted-average assumptions would be used in estimating fair value for 2001, 2000 and 1999:

Assumption -----	Regular Plan -----	Performance Accelerated Plan -----	Employee Stock Purchase Plan -----
Dividend yield	0.96%	3.83%	0.0%
Risk-free interest rate	5.80%	5.57%	4.86%
Expected life	7.1 yrs.	5 yrs.	3 mos.
Expected volatility	33.36%	29.78%	49.11%

The Company's net income and earnings per share for 2001, 2000 and 1999 would approximate the pro forma amounts below:

	(Dollars in thousands)		
	2001 ----	2000 ----	1999 ----
Net income			
As reported	\$ 48,577	\$184,613	\$141,154
Pro forma	\$ 47,531	\$183,163	\$139,801

249

HERCULES INTERNATIONAL LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

9. ADDITIONAL BALANCE SHEET DETAIL

	(Dollars in thousands)	
	2001 ----	2000 ----
Property, plant, and equipment		
Land	\$ 4,659	\$ 7,240
Buildings and equipment	436,298	533,902
Total	440,957	541,142
Accumulated depreciation and amortization	(224,469)	(265,817)
Net property, plant, and equipment	\$ 216,488 =====	\$ 275,325 =====
Accrued expenses		
Payroll and employee benefits	\$ 15,281	\$ 14,834
Income taxes payable	59,654	72,078
Restructuring (Note 11)	10,656	12,743

Edgar Filing: HERCULES INC - Form 10-K/A

Environmental	9,300	9,300
Other	12,345	9,207
	-----	-----
	\$ 107,236	\$ 118,162
	=====	=====

10. GOODWILL AND OTHER INTANGIBLE ASSETS

At December 31, 2001 and 2000, the goodwill and other intangible assets were:

	(Dollars in thousands)	
	2001	2000
	----	----
Goodwill	\$ 225,727	\$ 241,425
Other intangibles	5,035	7,829
	-----	-----
Total	230,762	249,254
Less accumulated amortization	(23,073)	(24,811)
	-----	-----
Net goodwill and other intangible assets	\$ 207,689	\$ 224,443
	=====	=====

Goodwill and other intangible assets primarily represent amounts capitalized from the Hercules acquisition of BetzDearborn (Note 1).

11. RESTRUCTURING

The consolidated balance sheet reflects liabilities for employee severance benefits and other exit costs, primarily related to the plans initiated upon the creation of the European Shared Service Center in 1997, the acquisition of BetzDearborn in 1998 and the Work Process Redesign ("WPR") program in 2001. During the third quarter of 2001, Hercules started a Work Process Redesign program. The WPR program has been set up to analyze and change the way we work to improve the mechanics of how we do business - to do it better, quicker and at less costs. Teams were established to focus initially on seven work processes of our business that needed major improvement: manufacturing, solicit order to cash, finance and control fundamentals, logistics, information technology, purchase to pay and discovery to commercialization.

Pursuant to the plans in place to merge the operations of BetzDearborn with Hercules and to rationalize the support infrastructure and other existing operations, facilities were closed and in total approximately 68 employees were terminated and approximately \$13.6 million cash was paid in severance benefits and other exit costs. The estimate for the remaining plans was decreased by approximately \$3.3 million against goodwill due to lower than planned severance benefits as the result of higher than anticipated attrition, with voluntary resignations not requiring the payment of termination benefits. The estimate for the plans related to the shared service center were decreased by approximately \$1.7 million against operating expense.

Edgar Filing: HERCULES INC - Form 10-K/A

As a result of the WPR program, we estimate approximately 74 employees to leave and have charged \$4.3 million to operating expense for these costs. These employees come from various parts of the business, including but not limited to all above-mentioned processes.

During the year 2001, approximately 209 employees were terminated and cash worth approximately \$5.5 million was paid in severance benefits and other exit costs. The estimate for the remaining plans was decreased by \$435 thousand against goodwill due to lower than planned severance benefits as the result of higher than anticipated attrition, with voluntary resignations not requiring the payment of termination benefits. The estimate for the plans related to the shared service center were decreased by \$ 386 thousand against operating expense.

Severance benefits payments are based on years of service and generally continue for 3 months to 24 months subsequent to termination. We expect to substantially complete remaining actions under the plans in 2002.

A reconciliation of activity with respect to the liabilities established for these plans is as follows:

	(Dollars in thousands)	
	2001	2000
	----	----
Balance at beginning of year	\$ 12,743	\$ 26,546
Cash payments	(5,528)	(13,556)
Additional termination benefits and exit costs	4,262	4,731
Reversals against goodwill	(435)	(3,320)
Reversals against earnings	(386)	(1,658)
	-----	-----
Balance at end of year	\$ 10,656	\$ 12,743
	=====	=====

251

HERCULES INTERNATIONAL LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

12. PENSION

The Company has a number of pension plans in Europe, covering substantially all employees. The following chart lists benefit obligations, plan assets, and funded status of the plans.

	(Dollars in thousands)	
	2001	2000
	----	----
CHANGE IN BENEFIT OBLIGATION		
Benefit obligation at January 1	\$ 137,156	\$ 150,800
Service cost	3,506	3,800

Edgar Filing: HERCULES INC - Form 10-K/A

Interest cost	6,676	7,6
Employee contributions	576	6
Reclassification of assets for plan settlement	--	(4
Settlements and transfers	(23,547)	(10,6
Translation difference	(6,760)	(12,3
Actuarial loss	13,961	5
Benefits paid from plan assets	(4,559)	(2,5
Benefits paid by company	(674)	(5
	-----	-----
Benefit obligation at December 31	\$ 126,335	\$ 137,1
	=====	=====
CHANGE IN PLAN ASSETS		
Fair value of plan assets at January 1	128,577	136,8
Actual return on plan assets	(8,317)	6,2
Employee contributions	576	6
Settlements and transfers	(25,921)	(1,1
Company refund	(4,859)	(3
Translation difference	(5,802)	(11,1
Benefits paid from plan assets	(4,559)	(2,5
	-----	-----
Fair value of plan assets at December 31	\$ 79,695	\$ 128,5
	=====	=====
Funded status of the plans	(46,640)	(8,5
Unrecognized actuarial gain (loss)	20,315	(17,4
Unrecognized prior service cost	3,138	4,6
Unrecognized net transition obligation	822	1,3
Amount included in other accrued expenses	353	
	-----	-----
Accrued benefit cost	\$ (22,012)	\$ (20,0
	=====	=====
AMOUNTS RECOGNIZED IN THE STATEMENT OF FINANCIAL POSITION CONSIST OF:		
Intangible asset	1,156	
Other comprehensive income	2,682	
Additional minimum liability	(3,838)	
Accrued benefit liability	(22,012)	(20,0
	-----	-----
	\$ (22,012)	\$ (20,0
	=====	=====
ASSUMPTIONS AS OF DECEMBER 31		
Weighted-average discount rate	5.00%	5.
Expected return on plan assets	6.00%	6.
Rate of compensation increase	3.00%	3.

252

HERCULES INTERNATIONAL LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

COMPONENTS OF NET PERIOD PENSION COST

(Dollars in Thousands)

2001	2000	1999
----	----	----

## Edgar Filing: HERCULES INC - Form 10-K/A

Service cost	\$ 3,506	\$ 3,846	\$ 6,270
Interest cost	6,676	7,696	8,593
Expected return on plan assets	(6,623)	(7,793)	(9,253)
Amortization and deferrals	(428)	(238)	458
Gain on settlements	--	(8,675)	--
Amortization of prior service cost	396	10	12
Amortization of transition asset	303	2,437	708
	-----	-----	-----
Benefit cost (credit)	\$ 3,830	\$ (2,717)	\$ 6,788
	=====	=====	=====

The projected benefit obligation, accumulated benefit obligation and fair value of plan assets for the pension plans with accumulated benefits obligations in excess of plan assets were \$ 115,493 thousand, \$ 95,943 thousand and \$ 78,054 thousand, respectively, as of December 31, 2001 and \$27,060 thousand, \$22,753 thousand and \$2,058 thousand, respectively, as of December 31, 2000.

During 1999 and up to March 1, 2000, the Company's Belgian employees participated in a defined benefit pension plan. On March 1, 2000, the Company terminated its participation in the defined benefit pension plan and primarily all Belgian employees were transferred into a Company sponsored defined contribution plan on that date. The Company's cost of the defined contribution plan for the year ended December 31, 2001 was \$330 thousand and for the period March 1, 2000 through December 31, 2000 was \$222 thousand.

### 13. OTHER OPERATING (INCOME) EXPENSES, NET

Other operating expense, net, in 2001 includes \$15,731 thousand in net gains from the sale of the Company's hydrocarbon resins business, select portions of its rosin resins business, and its peroxy chemicals business. Furthermore, other operating expense, net, includes Hercules Group affiliate royalty costs totaling \$25,164 thousand, net restructuring costs totaling \$3,876 thousand, net losses on asset sales totaling \$1,608 thousand and foreign currency gains totaling \$4,853 thousand.

Other operating income, net, in 2000 include a gain of \$167,566 thousand from the sale of the Food Gums division. On September 28, 2000, the Company sold its Food Gums division to CP Kelco, a joint venture with Lehman Brothers Merchant Banking Partners II, L.P., which contributed approximately \$300 million in equity. The Company received a note of approximately \$248 million from Hercules, which collected the original cash proceeds, recorded tax expenses of approximately \$61 million and retained a 28.57% equity position in CP Kelco. CP Kelco simultaneously acquired Kelco biogums business of Pharmacia Corporation (formerly Monsanto Corporation). Other operating expenses, net, also include Hercules Group affiliate royalty costs, net restructuring costs, environmental costs, net losses on asset dispositions and foreign currency losses totaling \$22,471 thousand, \$3,073 thousand, \$8,500 thousand, \$1,617 thousand and \$156 thousand, respectively.

Other operating expenses, net, in 1999 include Hercules Group affiliate royalty costs of \$27,318 thousand, a gain on sale of investments of \$13,302 thousand, net restructuring costs of \$12,551, environmental costs of \$800 thousand, net losses on asset dispositions of \$184 thousand and foreign currency losses amounting to \$149 thousand.

### 14. INTEREST AND DEBT EXPENSE

No interest and debt costs were capitalized during 2001, 2000 and 1999. The costs incurred are presented separately in the consolidated statement of income and are primarily from debt with affiliates.



HERCULES INTERNATIONAL LIMITED  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

-----

## 15. OTHER INCOME (EXPENSE), NET

Other income (expense), net, consists of the following:

	(Dollars in thousands)		
	2001	2000	1999
	----	----	----
Interest income	\$32,488	\$12,380	\$ 5,180
Rent	28	26	(6)
Miscellaneous income (expense), net	1,585	308	(4,524)
	-----	-----	-----
	\$34,101	\$12,714	\$ 650
	=====	=====	=====

## 16. INCOME TAXES

A summary of the components of the tax provision follows:

	(Dollars in thousands)		
	2001	2000	1999
	----	----	----
Current	\$ 35,436	\$106,398	\$ 51,632
Deferred	10,470	13,396	11,789
	-----	-----	-----
Provision for income taxes	\$ 45,906	\$119,794	\$ 63,421
	=====	=====	=====

Deferred tax (liabilities) assets at December 31 consist of:

	(Dollars in thousands)	
	2001	2000
	----	----
Depreciation	\$ (38,028)	\$ (41,661)
Amortization	(9,498)	(8,819)
Fixed asset valuation	(101)	(2,207)
Insurance provision	(4,193)	(4,989)
Replacement reserve	(10,491)	(3,282)
Intangible asset	(613)	(1,385)
Other	(4,747)	(2,314)
	-----	-----
Gross deferred tax liabilities	(67,671)	(64,657)
	-----	-----

Edgar Filing: HERCULES INC - Form 10-K/A

Allowance for doubtful accounts	1,113	--
Loss carryforwards	950	2,959
Inventory valuation	1,416	2,551
Accrued pension	2,583	--
Other	602	2,677
	-----	-----
Gross deferred tax assets	6,664	8,187
	-----	-----
Valuation allowance	(1,469)	(702)
	-----	-----
	\$ (62,476)	\$ (57,172)
	=====	=====

254

HERCULES INTERNATIONAL LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A reconciliation of the statutory income tax rate to the effective rate follows:

	2001	2000	1999
	----	----	----
Statutory income tax rate	35.0%	35.0%	35.0%
Non-deductible expenses	8.1%	0.5%	1.6%
Non-taxable income	(13.4)%	(3.9)%	(1.4)%
Gain on sale of investment	(1.9)%	(19.3)%	(2.9)%
Tax rate differences on subsidiary earnings	1.3%	0.4%	1.1%
Foreign dividends, net of credits	13.6%	23.2%	0.3%
Other	0.7%	2.8%	(2.4)%
	-----	-----	-----
Effective tax rate	43.4%	38.7%	31.3%
	=====	=====	=====

The net operating losses have a carryforward period ranging from 5 years to indefinite, but may be limited in their use in any given year.

17. COMMITMENTS AND CONTINGENCIES

Leases

The Company has operating leases (including office space, transportation, and data processing equipment) expiring at various dates. Rental expense was \$9,445 thousand, \$8,713 thousand and \$9,075 thousand in 2001, 2000 and 1999, respectively.

At December 31, 2001, minimum rental payments under noncancelable leases aggregated \$21,995 thousand. The net minimum payments over the next five years and thereafter are \$6,245 thousand in 2002, \$4,527 thousand in 2003, \$2,722 thousand in 2004, \$1,595 thousand in 2005, \$1,459 thousand in 2006 and \$5,447 thousand beyond 2006, respectively.

Litigation

## Edgar Filing: HERCULES INC - Form 10-K/A

The Company currently and from time to time is involved in litigation incidental to the conduct of its business. In the opinion of the Company's management, none of such litigation as of December 31, 2001 is likely to have a material adverse effect on the financial position, results of operations, or cash flows of the Company.

### Environmental

The Company has potential liability in connection with obligations to authorities of various EU countries in which it has manufacturing facilities, and to private parties pursuant to contract, for the cost of environmental investigation and/or cleanup at several sites. The estimated range of the reasonably possible share of costs for the investigation and cleanup is between \$5,000 thousand and \$12,000 thousand. The actual costs will depend upon numerous factors, including the actual methods of remediation required or agreed to; outcomes of negotiations with regulatory authorities and private parties; changes in environmental laws and regulations; technological developments; and the years of remedial activity required, which could range from 0 to 30 years.

The Company becomes aware of its obligations relating to sites in which it may have liability for the costs of environmental investigations and/or remedial activities through correspondence from government authorities, or through correspondence from companies with which the Company has contractual obligations, who either request information or notify us of our potential liability. We have established procedures for identifying environmental issues at our plant sites. In addition to environmental audit programs, we have environmental coordinators who are familiar with environmental laws and regulations and act as a resource for identifying environmental issues.

255

### HERCULES INTERNATIONAL LIMITED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

In December 2000, PFW Aroma Chemicals B.V., a company that in 1996 purchased from the Company a Fragrances Plant in Barneveld, NL, submitted a claim of 7,295 thousand EURO. The claim seeks payment of costs alleged to be owed under the 1996 Agreement between the parties. The claim generally alleges that the Company is obligated to pay for the costs of cleaning up contamination at the Barneveld plant and to pay various costs relating to compliance with permit obligations. The Company has questioned its obligation to pay the amounts sought, and is currently in negotiations with PFW regarding this claim.

On May 1, 2001, the Company sold a hydrocarbon resins manufacturing facility located in Middelburg, the Netherlands as part of the sale by Hercules of its Resins Division to Eastman Chemical Resins, Inc. Under the Purchase and Sale Agreement between the parties, Hercules retained certain specific liabilities relating to environmental conditions at the Middelburg hydrocarbon resins plant, including pre-existing contamination

At December 31, 2001, the total accrued liability of \$9,300 thousand for environmental remediation represents management's best estimate of the probable and reasonably estimable costs related to environmental remediation. The extent of liability is evaluated quarterly. The measurement of the liability is evaluated based on currently available information, including the process of remedial investigations at each site and the current status of negotiations with regulatory authorities regarding the method and extent of remediation that will be required and the negotiations regarding apportionment of costs among other

## Edgar Filing: HERCULES INC - Form 10-K/A

private parties. While it is not feasible to predict the outcome of all pending suits and claims, the ultimate resolution of these environmental matters could have a material effect upon the results of operations and the financial position of the Company.

### 18. RELATED PARTY TRANSACTIONS

The Company has entered into certain agreements with affiliated entities. These agreements were developed in the context of a Hercules Group/subsidiary relationship and therefore may not necessarily reflect the result of arm's-length negotiations between independent parties. All transactions described below are eliminated on consolidation of Hercules.

**Intercompany borrowing and interest:** The Company has intercompany loans with Hercules affiliated entities. The loans with affiliates are presented in net Hercules Group Investment in the consolidated balance sheet. Interest paid to affiliated entities was \$3,608 thousand, \$6,992 thousand, and \$1,968 thousand in 2001, 2000 and 1999, respectively.

**Corporate, regional and other allocations:** As discussed in Note 1, the consolidated financial statements of the Company reflect certain allocated support costs incurred by other entities in the Hercules group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations and charges included in the Company's consolidated financial statements were based either on a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on factors such as sales, net assets, cost of sales; or a relative weighting of geographic activity. These allocations are reflected in the selling, general and administrative line item in the consolidated statement of income. Such allocations and corporate charges totaled approximately \$47,416 thousand, \$25,303 thousand and \$33,712 thousand in 2001, 2000 and 1999, respectively.

**Sales to affiliates:** The Company sells raw material and finished goods inventory in the normal course of business to affiliated companies. The Company's revenues from sales to affiliated companies are presented separately in the consolidated statement of income.

**Purchases from affiliates:** The Company purchases in the normal course of business raw material and finished goods inventory from affiliated companies. The Company's purchases of inventory from affiliated companies is reflected in costs of sales in the consolidated statement of income and totaled \$49,964 thousand, \$107,593 thousand and \$115,269 thousand in 2001, 2000 and 1999, respectively.

**Royalties:** The Company entered into a license agreement in respect of the use of manufacturing formulations and specifications developed and owned by an affiliated entity. Total royalties accrued in respect of this agreement are included in the other operating (income) expenses line item in the consolidated statement of income and totaled \$25,164 thousand, \$22,471 thousand and \$27,318 thousand and thousand in 2001, 2000 and 1999, respectively.

### 19. DERIVATIVE INSTRUMENTS AND RISK MANAGEMENT

The Company enters into forward-exchange contracts to hedge currency exposure.

## Edgar Filing: HERCULES INC - Form 10-K/A

HERCULES INTERNATIONAL LIMITED  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

### NOTIONAL AMOUNTS AND CREDIT EXPOSURE OF DERIVATIVES

The notional amounts of derivatives summarized below do not represent amounts exchanged by the parties and, thus, are not a measure of the exposure of the Company through its use of derivatives. The amounts exchanged are calculated on the basis of the notional amounts and the other terms of the derivatives, which relate to interest rates or exchange rates.

### FOREIGN EXCHANGE RISK MANAGEMENT

The Company has selectively used foreign currency forward contracts to offset the effects of exchange rate changes on reported earnings, cash flow, and net asset positions. The primary exposures are denominated in the U.S. Dollar, the Japanese Yen and the British Pound Sterling. Some of the contracts involve the exchange of two foreign currencies, according to local needs in foreign subsidiaries. The term of the currency derivatives is rarely more than three months. At December 31, 2001 and 2000, the Company had outstanding forward-exchange contracts to purchase foreign currencies aggregating \$84,615 thousand and \$62,393 thousand, respectively, and to sell foreign currencies aggregating \$84,667 thousand and \$62,833 thousand, respectively. The foreign exchange contracts outstanding at December 31, 2001 will mature during 2002.

### FAIR VALUES

The following table presents the carrying amounts and fair values of the Company's financial instruments at December 31, 2001 and 2000:

	(Dollars in thousands)			
	2001		2000	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Foreign exchange contracts	\$ (52)	\$ (52)	\$ 205	\$ 205

The carrying amount represents the net unrealized gain or net interest payable associated with the contracts at the end of the period. Fair values of derivative contracts are indicative of cash that would have been required had settlement been December 31, 2001. Foreign exchange contracts are valued based on year-end exchange rates.

### 20. NET HERCULES GROUP INVESTMENT

Changes in Net Hercules Group Investment were as follows:

Balance, January 1, 1999	\$ 713,974
Net income	141,154
Other comprehensive loss	(51,868)
Intercompany transactions, net	(97,204)
	-----
Balance, December 31, 1999	706,056

## Edgar Filing: HERCULES INC - Form 10-K/A

Net income	184,613
Other comprehensive loss	(100,135)
Intercompany transactions, net	(406,338)
	-----
Balance, December 31, 2000	384,196
Net income	48,577
Other comprehensive loss	(29,810)
Intercompany transactions, net	(54,910)
	-----
Balance, December 31, 2001	\$ 348,053
	=====

The Company includes accumulated other comprehensive losses in Net Hercules Group Investment. At December 31, 2001, accumulated other comprehensive losses consisted of an additional minimum pension liability and foreign currency translation adjustments, net of tax, of \$(1,646) thousand and \$(168,969) thousand, respectively. At December

257

HERCULES INTERNATIONAL LIMITED  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

-----

31, 2000 and 1999, accumulated other comprehensive losses consisted of foreign currency translation adjustments, net of tax, of \$(140,805) thousand and \$(40,670) thousand, respectively.

21. SUBSEQUENT EVENT

On April 29, 2002, Hercules completed the sale of its Water Treatment Business to GE Specialty Materials (GESM). Pursuant to the Stock and Asset Agreement for the transaction, the sale included all of the stock of BetzDearborn and the Company. Hercules used the proceeds from the sale to prepay borrowings under its Senior Credit Facility and ESOP Credit Facility. Pursuant to the prepayment, among other things, the stock pledges were released.

258

REPORT OF INDEPENDENT ACCOUNTANTS

TO THE SHAREHOLDERS AND THE BOARD OF DIRECTORS OF  
HERCULES INCORPORATED  
WILMINGTON, DELAWARE

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income and comprehensive income and of cash flows present fairly, in all material respects, the financial position of Hercules Investments Sarl, a subsidiary of Hercules Incorporated, and its subsidiaries at December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these

## Edgar Filing: HERCULES INC - Form 10-K/A

financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers Accountants N.V.  
Amsterdam, The Netherlands  
November 12, 2002

259

### HERCULES INVESTMENTS SARL CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME

	2001	Year Ended December 31, 2000
	-----	-----
Sales to third parties	\$ 512,579	\$ 580,730
Sales to Hercules Group	80,579	328,822
	-----	-----
	593,158	909,552
Cost of sales	354,441	580,886
Selling, general, and administrative expenses	130,016	137,403
Research and development	14,057	19,977
Goodwill and intangible asset amortization	6,114	8,279
Other operating expense (income), net (Note 13)	9,354	(131,862)
	-----	-----
Profit from operations	79,176	294,869
Interest and debt expense (Note 14)	90,005	38,990
Other income, net (Note 15)	20,441	11,460
	-----	-----
Income before income taxes, equity (loss) income and minority interest, net	9,612	267,339
Provision for income taxes (Note 16)	28,176	46,244
	-----	-----
Income before equity (loss) income and minority interest, net	(18,564)	221,095
Equity (loss) income of affiliated companies	(10,026)	(3,891)
Minority interest, net	(1,563)	(1,441)
	-----	-----
Net (loss) income	(30,153)	215,763
Additional minimum pension liability, net of tax of \$(872)	(1,340)	--
Foreign Currency Translation, net of tax of \$0 for each year	59,040	(71,025)
	-----	-----
Comprehensive income	\$ 27,547	\$ 144,738
	=====	=====

## Edgar Filing: HERCULES INC - Form 10-K/A

The accompanying notes are an integral part of the consolidated financial statements

260

HERCULES INVESTMENTS SARL  
CONSOLIDATED BALANCE SHEETS

	(Dollars in thousands)	
	December 31,	
	2001	2000
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 17,585	\$ 14,340
Accounts receivable, net (Note 3)	127,314	147,439
Inventories (Note 4)	49,333	56,109
Deferred income taxes (Note 16)	2,614	2,231
	-----	-----
Total current assets	196,846	220,119
	-----	-----
Property, plant, and equipment, net (Note 9)	216,488	275,325
Investments in affiliates (Note 5)	19,565	30,279
Goodwill and other intangible assets, net (Note 10)	206,902	224,150
Deferred charges and other assets	9,902	12,427
	-----	-----
Total assets	\$ 649,703	\$ 762,300
	=====	=====
<b>LIABILITIES AND NET HERCULES GROUP INVESTMENT</b>		
Current liabilities		
Accounts payable	\$ 73,888	\$ 84,955
Short-term debt (Note 6)	5,144	91,007
Accrued expenses (Note 9)	53,864	47,514
	-----	-----
Total current liabilities	132,896	223,413
Long-term debt - third parties (Note 7)	264	75
Deferred income taxes (Note 16)	65,440	59,679
Pension liability (Note 12)	24,203	20,757
Deferred credits and other liabilities	3,720	2,030
	-----	-----
Total liabilities	226,523	306,017
Commitments and contingencies (Note 17)		
Minority Interest	22,249	22,649
Net Hercules Group Investment (Note 20)		
Accumulated other comprehensive losses	(50,559)	(108,259)
Intercompany transactions	451,490	541,893
	-----	-----
Total Net Hercules Group Investment	400,931	433,634
	-----	-----
Total liabilities and Net Hercules Group Investment	\$ 649,703	\$ 762,300
	=====	=====

The accompanying notes are an integral part of the consolidated financial



Edgar Filing: HERCULES INC - Form 10-K/A

statements

261

HERCULES INVESTMENTS SARL  
CONSOLIDATED STATEMENT OF CASH FLOWS

(Dollar  
Year En

	2001 ----
CASH FLOW FROM OPERATING ACTIVITIES:	
Net (loss) income	\$ (30,153)
Adjustments to reconcile net income to net cash provided by operations:	
Depreciation and amortization of property, plant and equipment	20,774
Amortization of goodwill and other intangible assets	6,114
Restructuring plans	3,016
Deferred income tax	9,835
Loss on disposals of property, plant and equipment	1,608
Gain on sale of investments	(15,219)
Equity loss (income) of affiliates	10,026
Dividends received	593
Minority interest, net	1,563
Corporate and other cost allocations	10,681
Accruals and deferrals of cash receipts and payments:	
Accounts receivable	12,858
Inventories	(20,978)
Accounts payable and accrued expenses	(717)
Noncurrent assets and liabilities	5,537
Net transfers from (to) Hercules Group	70,621
	-----
Net cash provided by operations	86,159
	-----
CASH FLOW FROM INVESTING ACTIVITIES:	
Capital expenditures, net of proceeds from sale	(17,554)
Proceeds from sale of investment	--
Purchase of equity method investments	--
	-----
Net cash used in investing activities	(17,554)
	-----
CASH FLOW FROM FINANCING ACTIVITIES:	
Change in short-term debt	(84,303)
Long-term debt repayments	--
Proceeds from issuance of long-term debt	193
Net transfers from (to) Hercules Group	18,798
	-----
Net cash used in financing activities	(65,312)
	-----
Effect of exchange rate changes on cash	(48)
	-----
Net increase (decrease) in cash and cash equivalents	3,245
Cash and cash equivalents at beginning of year	14,340
	-----
Cash and cash equivalents at end of year	\$ 17,585
	=====
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:	

## Edgar Filing: HERCULES INC - Form 10-K/A

Cash paid during the year for:	
Interest (net of amount capitalized)	\$ 114,765
Income taxes, net	15,591
Noncash investing and financing activities:	
Sale of investment in CP Kelco ApS (Note 13)	--
Corporate and other cost allocations	10,681
Reversal of restructuring accruals to goodwill (Note 11)	435

The accompanying notes are an integral part of the consolidated financial statements

262

### HERCULES INVESTMENTS SARL NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

#### 1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

Hercules Investments Sarl (the "Company") is a wholly owned subsidiary of Hercules International Limited (immediate parent) and Hercules Incorporated (ultimate parent) or ("Hercules"). Hercules and its wholly owned subsidiaries comprise the Hercules Group. The Company supplies engineered process and water treatment chemical programs, as well as products that manage the properties of aqueous systems, for industrial, commercial and institutional establishments. These products and services contribute to preserving or enhancing productivity, reliability and efficiency in plant operations and in complying with environmental regulations.

When Hercules acquired all of the outstanding shares of BetzDearborn Inc on October 15, 1998 it paid \$2,235 million in cash and \$186 million in common stock exchanged for the shares held by the BetzDearborn ESOP Trust. The purchase price allocated to the Company and its subsidiaries was approximately \$682 million. During 1999, Hercules completed the purchase price allocation and the final determination of goodwill was \$2,170 million of which the amount attributable to the Company was approximately \$278 million. These financial statements include the push down of fair value adjustments to assets and liabilities, including goodwill, other intangible assets and property, plant and equipment and their related amortization and depreciation adjustments.

As a result of the Hercules acquisition of BetzDearborn Inc., the Company entered into several internal reorganization transactions during 1999 and 2000. The transactions included the Company selling several of its investments in subsidiaries to Hercules affiliates, purchasing several investments in subsidiaries from Hercules affiliates, merging companies, and acquiring certain investments in Hercules group companies that are valued at cost. As all investments in this reorganization are under the common control of Hercules, these transactions have been accounted for in a manner similar to pooling of interests.

Prior to fiscal year 2000, separate company stand-alone financial statements were not prepared for the Company. In November 2000, Hercules amended its senior credit facility and ESOP credit facility (the "Facilities"). The Facilities, as amended, are secured by liens on Hercules' property and assets (and those of Hercules' Canadian Subsidiaries), a pledge of the stock of substantially all of Hercules' domestic subsidiaries (including the Company) and 65% of the stock of foreign subsidiaries directly owned by Hercules, and a pledge of Hercules' domestic intercompany indebtedness. These consolidated financial statements present the financial information of the Company, a collateral party to the Hercules debt, based on the Hercules' understanding of

## Edgar Filing: HERCULES INC - Form 10-K/A

the Securities and Exchange Commission's interpretation and application of Rule 3-16 under the Securities and Exchange Commission's Regulation S-X. These statements were derived from historical accounting records.

On April 29, 2002, in connection with Hercules' sale of its Water Treatment Business (see Note 21) and the repayment of the Facilities, the stock pledges were released. As a result, based on Hercules' current debt structure, these separate company stand-alone financial statements will not be required for the fiscal year ending December 31, 2002.

The consolidated financial statements of the Company reflect certain allocated support costs incurred by the Hercules Group. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations and charges included in the Company's consolidated financial statements were based on either a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on factors such as sales, net assets, or cost of sales; or a relative weighting of geographic activity. Management believes that the allocation method is reasonable. See Note 18 for more information.

A number of the operating companies participate in Hercules' centralized cash management system. Accordingly, cash received from operations may be transferred to Hercules on a periodic basis, and Hercules funds operational and capital requirements upon request.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its majority-owned subsidiaries where control exists. Following the acquisition of BetzDearborn by Hercules in 1998, the Company continued BetzDearborn's practice of using a November 30 fiscal year end for certain former BetzDearborn Inc. non-U.S. subsidiaries to expedite the year end closing process. All intercompany transactions and profits have been eliminated.

263

#### HERCULES INVESTMENTS SARL NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

#### USE OF ESTIMATES

Preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

#### REVENUE RECOGNITION

The Company recognizes revenue when the earnings process is complete. This generally occurs when products are shipped to the customer or services are performed in accordance with terms of the agreement, title and risk of loss have been transferred, collectibility is probable, and pricing is fixed and determinable. Accruals are made for sales returns and other allowances based on the Company's experience. The corresponding shipping and handling costs are

## Edgar Filing: HERCULES INC - Form 10-K/A

included in cost of sales.

### RESEARCH AND DEVELOPMENT EXPENDITURES

Research and development expenditures are expensed as incurred.

### ENVIRONMENTAL EXPENDITURES

Environmental expenditures that pertain to current operations or future revenues are expensed or capitalized according to the Company's capitalization policy. Expenditures for remediation of an existing condition caused by past operations that do not contribute to current or future revenues are expensed. Liabilities are recognized for remedial activities when the cleanup is probable and can be reasonably estimated.

### CASH AND CASH EQUIVALENTS

Cash in excess of operating requirements is invested in short-term, income-producing instruments. Cash equivalents include commercial paper and other securities with original maturities of 90 days or less. Book value approximates fair value because of the short maturity of those instruments.

### INVENTORIES

Inventories are stated at the lower of cost or market. Inventories are valued on the average cost method.

### PROPERTY AND DEPRECIATION

Property, plant, and equipment are stated at cost. The Company changed to the straight-line method of depreciation, effective January 1, 1991, for newly acquired processing facilities and equipment. Assets acquired before then continue to be depreciated by accelerated methods. The Company believes straight-line depreciation provides a better matching of costs and revenues over the lives of the assets. The estimated useful lives of depreciable assets are as follows: buildings - 30 years; plant, machinery and equipment - 15 years; other machinery and equipment - 3 to 15 years.

Maintenance, repairs, and minor renewals are charged to income; major renewals and betterments are capitalized. Upon normal retirement or replacement, the net book value of property (less proceeds of sale or salvage) is charged to income.

### INVESTMENTS

Investments in affiliated companies with a 20% or greater ownership interest in which the Company has significant influence are accounted for using the equity method of accounting. Accordingly, these investments are included in investments in affiliates on the Company's balance sheet and the income or loss from these investments is included in equity in (loss) income of affiliated companies in the Company's statement of income.

### GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill and other intangible assets are amortized on a straight-line basis over the estimated future periods to be benefited, generally 40 years for goodwill, customer relationships, and trademarks and tradenames and 5 to 15 years for other intangible assets. Pursuant to Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (SFAS 142), beginning January 1, 2002, goodwill will not be amortized but will be tested for impairment annually and any necessary adjustment charged to expense. Intangible assets with finite lives will be amortized over their useful lives.

HERCULES INVESTMENTS SARL  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

LONG-LIVED ASSETS

The Company reviews its long-lived assets, including goodwill and other intangibles, for impairment on an exception basis whenever events or changes in circumstances indicate carrying amounts of the assets may not be recoverable through undiscounted future cash flows. If an impairment loss has occurred based on expected future cash flows (undiscounted), the loss is recognized in the income statement. The amount of the impairment loss is the excess of the carrying amount of the impaired asset over the fair value of the asset. The fair value represents expected future cash flows from the use of the assets, discounted at the rate used to evaluate potential investments.

INCOME TAXES

Income tax expense in the accompanying consolidated financial statements has been computed assuming the Company filed separate income tax returns.

The provisions for income taxes has been determined using the asset and liability approach of accounting for income taxes. Under this approach, deferred taxes represent the future tax consequences expected to occur when the reported amounts of assets and liabilities are recovered or paid. The provision for income taxes represents income taxes paid or payable for the current year plus the change in deferred taxes during the year. Deferred taxes result from differences between the financial and tax basis of the Company's assets and liabilities and are adjusted for changes in tax rates and tax laws when changes are enacted. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized.

The company provides taxes on undistributed earnings of subsidiaries and affiliates included in consolidated retained earnings to the extent such earnings are planned to be remitted and not re-invested permanently. The undistributed earnings/(loss) of subsidiaries and affiliates on which no provision for foreign withholding or US income taxes has been made amounted to approximately \$25,645 thousand, \$(7,730) thousand and \$9,273 thousand at December 31, 2001, 2000 and 1999, respectively. US and foreign income taxes that would be payable if such earnings were distributed may be lower than the amount computed at the US statutory rate because of the availability of tax credits.

FOREIGN CURRENCY TRANSLATION AND TRANSACTIONS

The accompanying consolidated financial statements are reported in U.S. dollars. The Euro is the functional currency for the Company. The translation of the functional currencies of the Company's subsidiaries into U.S. dollars (reporting currency) is performed for assets and liabilities using the current exchange rates in effect at the balance sheet date, and for revenues, costs and expenses using average exchange rates prevailing during the reporting periods. Adjustments resulting from the translation of functional currency financial statements to reporting currency are accumulated and reported as other comprehensive income, a separate component of Net Hercules Group Investment.

Transactions in foreign currency are recorded at the exchange rate prevailing on the date of transaction. Monetary assets and liabilities denominated in foreign currencies are expressed in the functional currency at

## Edgar Filing: HERCULES INC - Form 10-K/A

the exchange rates in effect at the balance sheet date. Revenues, costs and expenses are recorded using average exchange rates prevailing during the reporting periods. Gains or losses resulting from foreign currency transactions are included in the statement of income.

### CONCENTRATIONS OF CREDIT RISK

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of trade receivables and receivables from affiliated companies, which are included in the Net Hercules Group Investment in the consolidated balance sheet. Concentrations of credit risk with respect to trade receivables are limited due to the Company's large number of customers and their dispersion across many different industries and locations.

### DERIVATIVE INSTRUMENTS AND HEDGING

On January 1, 2001, the Company adopted Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS 133"). SFAS 133, as amended by Statement No. 137, "Accounting for Derivative Instruments and Hedging Activities-Deferral of the Effective Date of FASB Statement No. 133" and Statement No. 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities," requires that all derivative instruments be recorded on the balance sheet at their fair value. The Company has not designated any derivative as a hedge instrument and accordingly, changes in fair value of derivatives are recorded each period in earnings. The adoption of SFAS 133 did not result in a pre-tax or post-tax cumulative-effect-type adjustment to income and did not result in a change to other comprehensive income (loss).

265

### HERCULES INVESTMENTS SARL NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

Derivative financial instruments have been used to hedge risk caused by fluctuating currency. The Company enters into forward-exchange contracts to hedge foreign currency exposure. Decisions regarding hedging are made on a case-by-case basis, taking into consideration the amount and duration of the exposure, market volatility, and economic trends. The Company uses the fair-value method of accounting, recording to other income (expense), net realized and unrealized gains and losses on these contracts monthly, except for gains and losses on contracts to hedge specific foreign currency commitments, which are deferred and accounted for as part of the transaction. Gains or losses on instruments which have been used to hedge the value of investments in certain non-U.S. subsidiaries have been accounted for under the deferral method and are included in the foreign currency translation adjustment. It is the Company's policy to match the term of financial instruments with the term of the underlying designated item. If the designated item is an anticipated transaction no longer likely to occur, gains or losses from the instrument designated as a hedge are recognized in current period earnings. The Company does not hold or issue financial instruments for trading purposes. In the consolidated statement of cash flow, the Company reports the cash flows resulting from its hedging activities in the same category as the related item that is being hedged.

### STOCK-BASED COMPENSATION

Compensation costs attributable to stock option and similar plans are recognized based on any excess of the quoted market price of the stock on the date of grant over the amount the employee is required to pay to acquire the

## Edgar Filing: HERCULES INC - Form 10-K/A

stock (the intrinsic-value method under Accounting Principles Board Opinion 25 (APB 25). Such amount, if any, is accrued over the related vesting period, as appropriate. Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation," requires companies electing to continue to use the intrinsic-value method to make pro forma disclosures of net income as if the fair-value-based method of accounting had been applied.

### MINORITY INTEREST

Minority interest at December 31, 2001 and 2000 represents a 38.97% proportionate share of the equity of Hercules Quimica S.A., owned by a Hercules Group affiliate and a 0.4% proportionate share of the equity of Hercules Holding BV/BVBA, owned by a Hercules Group affiliate.

### COMPUTER SOFTWARE COSTS

Effective January 1, 1999, the Company adopted the American Institute of Certified Public Accountants Statement of Position 98-1, "Accounting for the Cost of Computer Software Developed or Obtained for Internal Use" (SOP 98-1). The prior accounting was generally consistent with the requirements of SOP 98-1 and, accordingly, adoption of SOP 98-1 had no material effect. Computer software costs are being amortized over a period of 5 to 10 years.

### NET HERCULES GROUP INVESTMENT

The Net Hercules Group Investment account reflects the balance of the Company's historical earnings, intercompany amounts, foreign currency translation and other transactions between the Company and the Hercules Group.

### NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 141, "Business Combinations" ("SFAS 141"), and Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"). SFAS 141 supersedes Accounting Principles Board Opinion ("APB") No. 16, Business Combinations. The provisions of SFAS 141 (1) require that the purchase method of accounting be used for all business combinations initiated after June 30, 2001, (2) provide specific criteria for the initial recognition and measurement of intangible assets apart from goodwill and (3) require that unamortized negative goodwill be written off immediately as extraordinary gain instead of being deferred and amortized. SFAS 141 also requires that upon adoption of SFAS 142 the Company reclassify the carrying amounts of certain intangible assets into or out of goodwill, based on certain criteria. SFAS 142 supersedes APB No. 17, Intangible Assets, and is effective for fiscal years beginning after December 15, 2001. SFAS 142 primarily addresses the accounting for goodwill and intangible assets subsequent to their initial recognition. The provisions of SFAS 142 (1) prohibit the amortization of goodwill and indefinite-lived intangible assets, (2) require that goodwill and indefinite-lived intangible assets be tested annually for impairment (and in interim periods if certain events occur indicating that the carrying value of goodwill and/or indefinite-lived intangible assets may be impaired), based on fair value (as opposed to cost recovery using future undiscounted cash flows), (3) require that reporting units be identified for the purpose of assessing potential future impairments of goodwill and (4) remove the forty-year limitation on the amortization period of intangible assets that have finite lives.

## Edgar Filing: HERCULES INC - Form 10-K/A

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

Effective January 1, 2002 Hercules adopted the provisions of SFAS 142. Hercules identified the following reporting units: BetzDearborn and Pulp and Paper, Aqualon and FiberVisions. In connection with Hercules' transitional review, recorded goodwill was determined to be impaired in the BetzDearborn reporting unit. In the first quarter 2002, Hercules completed its transitional impairment review of the identified reporting units and recognized an after tax impairment loss of \$368 million as a cumulative effect of a change in accounting principle. As a result of Hercules' adoption of SFAS 142, the Company will no longer record approximately \$6.1 million of annual amortization relating to existing goodwill and intangibles.

Goodwill related to the BetzDearborn business was evaluated for impairment at December 31, 2001 under Statement of Financial Accounting Standards No. 121 "Accounting for the Impairment of Long-Fixed Assets and for Long-Lived Assets to Be Disposed of". Such evaluation indicated that goodwill associated with the business was recoverable from anticipated future undiscounted cash flows. Accordingly, no impairment loss was recorded in the December 31, 2001 financial statements.

In June 2001, the Financial Accounting Standards Board ("FASB") approved the issuance of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143"). SFAS 143 establishes accounting standards for the recognition and measurement of legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 will become effective for the Company on January 1, 2003 and requires recognition of a liability for an asset retirement obligation in the period in which it is incurred. The Company does not believe it will have a material effect on its financial statements.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company does not believe it will have a material effect on its financial statements.

In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment to FASB Statement No. 13, and Technical Corrections." The Company elected to early adopt the provisions of SFAS 145 related to the rescission of SFAS 4, "Reporting Gains and Losses from the Extinguishment of Debt" ("SFAS 4"). The early adoption of SFAS 145 had no effect on the Company's financial statements.

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146"). SFAS 146 addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs in a Restructuring)". SFAS 146 defines the timing of the recognition of costs associated with exit or disposal activities, the types of costs that may be recognized and the methodology for calculating the fair value of such costs. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. The Company does not believe this statement will have a material effect on its financial statements.

#### RECLASSIFICATIONS

Certain amounts in the 2000 and 1999 consolidated financial statements and notes have been reclassified to conform to the 2001 presentation.



Edgar Filing: HERCULES INC - Form 10-K/A

3. ACCOUNTS RECEIVABLE, NET

Accounts receivable, net, consists of:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Trade	\$ 121,937	\$ 139,568
Other	8,440	10,228
	-----	-----
	130,377	149,796
Less allowance for doubtful accounts	(3,063)	(2,357)
	-----	-----
Total	\$ 127,314	\$ 147,439
	=====	=====

267

HERCULES INVESTMENTS SARL  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

-----  
Other accounts receivable mainly comprise VAT receivable.

4. INVENTORIES

The components of inventories are:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Finished products	\$32,386	\$30,895
Materials, supplies, and work in process	16,947	25,214
	-----	-----
Total	\$49,333	\$56,109
	=====	=====

5. INVESTMENTS

The Company has various equity investments in companies, as described below. Summarized financial information for these equity affiliates at December 31, and for the three years then ended is as follows:

	(Dollars in thousands)	
	2001	2000
	----	----
Current assets	\$241,134	\$269,814
Non-current assets	890,455	942,946

## Edgar Filing: HERCULES INC - Form 10-K/A

Current liabilities	\$ 81,123	\$109,486
Non-current liabilities	725,523	730,579

	2001 ----	2000 ----	1999 ----
Net sales	\$471,411	\$143,245	\$56,410
Gross profit	148,987	17,290	14,488
Net (losses) earnings	(50,021)	(15,864)	5,865

At December 31, 2001, the Company's equity investments, all affiliates of the Hercules Group, consisted of a 50% ownership of Abieta Chemie GmbH and BetzDearborn Nippon KK, a 49% ownership of Hercules Mas Indonesia, and a 28.57% ownership of the consolidated group CP Kelco ApS. The Company's carrying value for these investments at December 31, 2001 and 2000 equals its share of the underlying equity in net assets of the respective affiliates. Dividends paid to the Company from its equity investees were \$593 thousand, \$579 thousand and \$3,093 thousand during 2001, 2000 and 1999, respectively. Except for CP Kelco ApS, each of these entities operates in lines of business similar to the Company, supplying engineered process and water treatment chemical programs, as well as products that manage the properties of aqueous systems, for industrial, commercial and institutional establishments. As discussed further in Note 13, CP Kelco ApS was the Company's Food Gums business that was divested in 2000.

### 6. SHORT-TERM DEBT AND OTHER FINANCING ARRANGEMENTS

Short-term debt of \$5,144 thousand and \$91,007 thousand at December 31, 2001 and 2000, respectively, consists of bank borrowings primarily representing foreign overdraft facilities and short-term lines of credit, which are generally payable on demand with interest at various rates. Book values of bank borrowings approximate market value because of their short maturity period.

Short-term debt with affiliates of \$3,539 thousand and \$32,734 thousand at December 31, 2001 and 2000, respectively, is recorded in Net Hercules Group Investment in the consolidated balance sheet and is generally payable on demand with interest at various rates.

At December 31, 2001 and 2000, the Company had \$7,155 thousand and \$34,774 thousand, respectively, of unused lines of credit that may be drawn as needed, with interest at a negotiated spread over lenders' cost of funds.

Weighted-average interest rates on all short-term borrowings at December 31, 2001 and 2000 were 4.40% and 5.60%, respectively.

268

HERCULES INVESTMENTS SARL  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 7. LONG-TERM DEBT AND OTHER FINANCING ARRANGEMENTS

Long-term debt with third parties and affiliates at December 31, 2001 and 2000 is summarized as follows:

Edgar Filing: HERCULES INC - Form 10-K/A

	(Dollars in thousand)	
	2001	2000
	----	----
5.72% third party note	\$ 309	\$ 93
Other	24	45
	-----	-----
Less current maturities	69	63
	-----	-----
Total long-term debt, third party	264	75
	-----	-----
4.93% affiliate note	1,614,562	1,698,968
Cibor + 0.0075% affiliate note	21,799	22,853
Euribor + 0.5% affiliate note	19,496	20,516
	-----	-----
Less current maturities	--	--
	-----	-----
Total long-term debt, affiliates	1,655,857	1,742,337
	-----	-----
Total long term debt, third party and affiliates	\$1,656,121	\$1,742,412
	=====	=====

Long-term debt with affiliates, which is recorded in Net Hercules Group Investment in the consolidated balance sheet, has no stated maturity. Third party long-term debt at December 31, 2001 matures as follows: \$69 thousand, \$48 thousand, \$50 thousand, \$53 thousand and \$113 thousand in the years 2002, 2003, 2004, 2005 and 2006 and thereafter, respectively. The fair values of the Company's long-term debt were \$1,656 thousand at December 31, 2001 and \$1,742 thousand at December 31, 2000. The Company believes that the carrying value of long-term debt borrowings approximates fair value, based on discounting future cash flows using rates currently available for debt of similar terms and remaining maturities.

8. LONG-TERM INCENTIVE COMPENSATION PLANS

The Company participates in long-term incentive compensation plans sponsored by Hercules. These plans provide for the grant of stock options and the award of common stock and other market-based units to certain key employees and non-employee directors.

In 1995, Hercules changed the structure of the long-term incentive compensation plans to place a greater emphasis on shareholder value creation through grants of regular stock options, performance-accelerated stock options, and Cash Value Awards (performance-based awards denominated in cash and payable in shares of common or restricted stock, subject to the same restrictions as restricted stock). Restricted stock and other market-based units are awarded with respect to certain programs. The number of awarded shares outstanding was 189,704 at December 31, 2001, and 491,488 and 926,689 at December 31, 2000 and 1999, respectively.

At December 31, 2001, under Hercules' incentive compensation plans, 1,265,493 shares of common stock were available for grant as stock awards or stock option awards. Stock awards are limited to approximately 15% of the total authorizations. Regular stock options are granted at the market price on the date of grant and are exercisable at various periods from one to five years after date of grant. Performance-accelerated stock options are also granted at the market price on the date of grant and are normally exercisable at nine and one-half years. Exercisability may be accelerated based upon the achievement of

## Edgar Filing: HERCULES INC - Form 10-K/A

predetermined performance goals. Both regular and performance-accelerated stock options expire 10 years after the date of grant.

Restricted shares, options and performance-accelerated stock options are forfeited and revert to Hercules in the event of employment termination, except in the case of death, disability, retirement, or other specified events.

The Company applies APB Opinion 25 in accounting for its plans. Accordingly, no compensation cost has been recognized for the stock option plans. There were no charges to income for the cost of stock awards over the restriction or performance period for 2001, 2000 and 1999, respectively.

269

HERCULES INVESTMENTS SARL  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

Below is a summary of outstanding stock option grants under the incentive compensation plans during 1999, 2000 and 2001:

	Regular		Performance-
	Number of Shares	Weighted-average price	Number of Shares
December 31, 1998	418,250	\$39.64	89,050
Granted	215,500	\$37.61	60,775
Exercised	-	-	-
Forfeited	-	-	(900)
December 31, 1999	633,750	\$38.95	148,925
Granted	141,000	\$17.25	-
Exercised	-	-	-
Forfeited	(19,650)	\$36.82	(1,350)
December 31, 2000	755,100	\$34.95	147,575
Granted	80,125	\$11.28	-
Exercised	-	-	-
Forfeited	(60,460)	\$30.85	(900)
December 31, 2001	774,765	\$32.82	146,675

The weighted-average fair value of regular stock options granted during 1999, 2000 and 2001 was \$8.25, \$8.85 and \$5.69, respectively. The weighted-average fair value of performance-accelerated stock options granted during 1999, 2000 and 2001 was \$7.99, \$0 and \$0, respectively.

Following is a summary of regular stock options exercisable at December 31, 1999, 2000, and 2001, and their respective weighted-average share prices:

	Number of Shares	Weighted-average exercise price
Options Exercisable		

Edgar Filing: HERCULES INC - Form 10-K/A

December 31, 1999	290,545	\$39.85
December 31, 2000	533,705	\$37.14
December 31, 2001	612,365	\$36.57

There were no performance-accelerated stock options exercisable at December 31, 1999, 2000 and 2001.

Following is a summary of stock options outstanding at December 31, 2001:

Exercise Price Range	Outstanding Options			Number Exercised 12/31/2001
	Number Outstanding at 12/31/2001	Weighted-average Remaining Contractual Life	Weighted-average exercise price	
Regular Stock Options				
\$11 - \$20	196,275	8.75	\$14.81	68,84
\$20 - \$30	44,475	6.67	\$25.56	44,47
\$30 - \$40	462,540	6.23	\$38.71	427,57
\$40 - \$50	63,075	6.11	\$47.82	63,07
\$50 - \$60	8,400	4.11	\$55.38	8,40
	-----			-----
	774,765			612,36
	-----			-----
Performance-Accelerated Stock Options				
\$14 - \$40	89,500	6.69	\$37.98	
\$40 - \$50	50,075	5.82	\$47.83	
\$50 - \$61	7,100	4.11	\$55.38	
	-----			-----
	146,675			
	-----			-----

The Company currently expects that 100% of performance-accelerated stock options will eventually vest.

The Company's employees may also participate in the Hercules Employee Stock Purchase Plan ("ESSP"). The ESSP is a qualified non-compensatory plan, which allows eligible employees to acquire shares of common stock through systematic payroll deductions. The plan consists of three-month subscription periods, beginning July 1 of each year. The purchase price is 85% of the fair market value of the common stock on either the first or last day of that subscription period, whichever is lower. Purchases may range from 2% to 15% of an employee's base salary each pay period, subject to certain limitations. Currently, there are no shares of Hercules common stock registered for offer and sale under the plan. Shares issued at December 31, 2001 and 2000, were 1,758,081 and 1,597,861, respectively. The Company applies APB Opinion 25 and related interpretations in accounting for its Employee Stock Purchase Plan. Accordingly, no compensation cost has been recognized for the Employee Stock Purchase Plan.

## Edgar Filing: HERCULES INC - Form 10-K/A

HERCULES INVESTMENTS SARL  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Had compensation cost for Hercules' Stock-Based Incentive Plans and Employee Stock Purchase Plan been determined on the basis of fair value according to SFAS No. 123, the fair value of each option granted or share purchased would be estimated on the grant date using the Black-Scholes option pricing model.

The following weighted-average assumptions would be used in estimating fair value for 2001, 2000 and 1999:

Assumption	Regular Plan	Performance Accelerated Plan	Employee Stock Purchase Plan
Dividend yield	0.96%	3.83%	0.0%
Risk-free interest rate	5.80%	5.57%	4.86%
Expected life	7.1 yrs.	5 yrs.	3 mos.
Expected volatility	33.36%	29.78%	49.11%

The Company's net income and earnings per share for 2001, 2000 and 1999 would approximate the pro forma amounts below:

	(Dollars in thousands)		
	2001	2000	1999
Net (loss) income			
As reported	\$(30,153)	\$215,763	\$137,779
Pro forma	\$(31,100)	\$214,434	\$136,521

### 9. ADDITIONAL BALANCE SHEET DETAIL

	(Dollars in thousands)	
	2001	2000
Property, plant, and equipment		
Land	\$ 4,659	\$ 7,240
Buildings and equipment	436,298	533,902
Total	440,957	541,142
Accumulated depreciation and amortization	(224,469)	(265,817)
Net property, plant, and equipment	\$ 216,488	\$ 275,325
Accrued expenses		
Payroll and employee benefits	\$ 14,986	\$ 14,395
Income taxes payable	9,315	4,966
Restructuring (Note 11)	10,002	12,743
Environmental	9,300	9,300
Other	10,261	6,110

Edgar Filing: HERCULES INC - Form 10-K/A

-----	-----
\$ 53,864	\$ 47,514
=====	=====

10. GOODWILL AND OTHER INTANGIBLES ASSETS

At December 31, 2001 and 2000, the goodwill and other intangible assets were:

	(Dollars in thousands)	
	2001	2000
	----	----
Goodwill	\$ 225,472	\$ 241,109
Other intangibles	4,467	7,820
	-----	-----
Total	229,939	248,929
Less accumulated amortization	(23,037)	(24,779)
	-----	-----
Net goodwill and other intangible assets	\$ 206,902	\$ 224,150
	=====	=====

Goodwill and other intangible assets primarily represent amounts capitalized from the Hercules acquisition of BetzDearborn (Note 1).

271

HERCULES INVESTMENTS SARL  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

11. RESTRUCTURING

The consolidated balance sheet reflects liabilities for employee severance benefits and other exit costs, primarily related to the plans initiated upon the creation of the European Shared Service Center in 1997, the acquisition of BetzDearborn in 1998 and the Work Process Redesign ("WPR") program in 2001. During the third quarter of 2001, Hercules started a Work Process Redesign program. The WPR program has been set up to analyze and change the way we work to improve the mechanics of how we do business - to do it better, quicker and at less costs. Teams were established to focus initially on seven work processes of our business that needed major improvement: manufacturing, solicit order to cash, finance and control fundamentals, logistics, information technology, purchase to pay and discovery to commercialization.

Pursuant to the plans in place to merge the operations of BetzDearborn with Hercules and to rationalize the support infrastructure and other existing operations, facilities were closed and in total approximately 68 employees were terminated in the year 2000 and cash worth approximately \$13.6 million was paid for severance benefits and other exit costs. The estimate for the remaining plans was decreased by approximately \$3.3 million against goodwill due to lower than planned severance benefits as the result of higher than anticipated attrition, with voluntary resignations not requiring the payment of termination benefits. The estimate for the plans related to the shared service center was decreased by approximately \$1.7 million against operating expense.

## Edgar Filing: HERCULES INC - Form 10-K/A

As a result of the WPR program, we estimate approximately 68 employees to leave and have charged \$3.4 million to operating expense for these costs. These employees come from various parts of the business, including but not limited to all above-mentioned processes.

During the year 2001, a total of approximately 183 employees were terminated and cash worth approximately \$5.3 million was paid for severance benefits and other exit costs. The estimate for the remaining plans was decreased by \$435 thousand against goodwill due to lower than planned severance benefits as the result of higher than anticipated attrition, with voluntary resignations not requiring the payment of termination benefits. The estimate for the plans related to the shared service center was decreased by \$386 thousand against operating expense.

Severance benefits payments are based on years of service and generally continue for 3 months to 24 months subsequent to termination. We expect to substantially complete remaining actions under the plans in 2002.

A reconciliation of activity with respect to the liabilities established for these plans is as follows:

	(Dollars in thousands)	
	2001	2000
	----	----
Balance at beginning of year	\$ 12,743	\$ 26,546
Cash payments	(5,322)	(13,556)
Additional termination benefits and exit costs	3,402	4,731
Reversals against goodwill	(435)	(3,320)
Reversals against earnings	(386)	(1,658)
	-----	-----
Balance at end of year	\$ 10,002	\$ 12,743
	=====	=====

272

HERCULES INVESTMENTS SARL  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

### 12. PENSION

The Company has a number of pension plans in Europe, covering substantially all employees. The following chart lists benefit obligations, plan assets, and funded status of the plans.

	(Dollars in thousands)	
	2001	2000
	----	----
CHANGE IN BENEFIT OBLIGATION		
Benefit obligation at January 1	\$ 25,087	\$37,408
Service cost	909	842
Interest cost	1,454	1,388
Employee contributions	-	7



Edgar Filing: HERCULES INC - Form 10-K/A

Reclassification of assets for plan settlement	-	(416)
Settlements and transfers	-	(10,612)
Translation difference	(1,307)	(3,108)
Actuarial loss	2,794	111
Benefits paid from plan assets	-	(10)
Benefits paid by company	(674)	(523)
	-----	-----
Benefit obligation at December 31	\$ 28,263	\$25,087
	=====	=====

CHANGE IN PLAN ASSETS		
Fair value of plan assets at January 1	1,616	2,817
Actual return on plan assets	11	22
Employee contributions	-	7
Settlements and transfers	--	(1,109)
Company contributions	103	122
Translation difference	(81)	(233)
Benefits paid from plan assets	--	(10)
	-----	-----
Fair value of plan assets at December 31	\$ 1,649	\$ 1,616
	=====	=====

Funded status of the plans	(26,614)	(23,471)
Unrecognized actuarial loss	4,514	1,876
Unrecognized prior service cost	103	119
Unrecognized net transition obligation	602	719
	-----	-----
Accrued benefit cost	\$ (21,395)	\$ (20,757)
	=====	=====

AMOUNTS RECOGNIZED IN THE STATEMENT OF FINANCIAL POSITION CONSIST OF:

Intangible asset	596	-
Other comprehensive income	2,212	-
Additional minimum liability	(2,808)	-
Accrued benefit liability	(21,395)	(20,757)
	-----	-----
	\$ (21,395)	\$ (20,757)
	=====	=====

ASSUMPTIONS AS OF DECEMBER 31

Weighted-average discount rate	5.00%	5.75%
Expected return on plan assets	6.00%	6.50%
Rate of compensation increase	3.00%	3.50%

273

HERCULES INVESTMENTS SARL  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

COMPONENTS OF NET PERIOD PENSION COST

	Pension Benefits		
	2001	2000	1999
	----	----	----

## Edgar Filing: HERCULES INC - Form 10-K/A

Service cost	\$ 909	\$ 842	\$ 1,510
Interest cost	1,454	1,388	2,258
Expected return on plan assets	(37)	(36)	(98)
Amortization and deferrals	(8)	(17)	(14)
Gain on settlements	-	(8,675)	-
Amortization of prior service cost	66	10	12
Amortization of transition asset	82	2,129	351
	-----	-----	-----
Benefit (credit) cost	\$ 2,466	\$(4,359)	\$ 4,019
	-----	-----	-----

The projected benefit obligation, accumulated benefit obligation and fair value of plan assets for the pension plans with accumulated benefits obligations in excess of plan assets were \$17,410 thousand, \$16,241 thousand and \$0, respectively, as of December 31, 2001 and \$23,562 thousand, \$19,780 thousand and \$ 0 thousand, respectively, as of December 31, 2000.

The Company's employees in The Netherlands participate in a multi-employer pension fund which is administered by an affiliated company. Contribution amounts are based upon costs allocated to the Company by the Plan administrator. Pension costs/(benefits) relating to the multi-employer plan were \$1,265 thousand, \$(428) thousand and \$199 thousand in 2001, 2000 and 1999, respectively.

During 1999 and up to March 1, 2000, the Company's Belgian employees participated in a defined benefit pension plan. On March 1, 2000, the Company terminated its participation in the defined benefit pension plan and primarily all Belgian employees were transferred into a Company sponsored defined contribution plan on that date. The Company's cost of the defined contribution plan for the year ended December 31, 2001 was \$330 thousand and for the period March 1, 2000 through December 31, 2000 was \$222 thousand.

### 13. OTHER OPERATING (INCOME) EXPENSES, NET

Other operating expense, net, in 2001 includes \$15,219 thousand in net gains from the sale of the Company's hydrocarbon resins business, select portions of its rosin resins business, and its peroxy chemicals business. Furthermore, other operating expense, net, includes Hercules Group affiliate royalty costs totaling \$25,164 thousand, net restructuring costs totaling \$3,016 thousand, net losses on assets sales totaling \$1,608 thousand and foreign currency gains totaling \$5,215 thousand.

Other operating income, net, in 2000 include a gain of \$167,566 thousand from the sale of the Food Gums division. On September 28, 2000, the Company sold its Food Gums division to CP Kelco, a joint venture with Lehman Brothers Merchant Banking Partners II, L.P., which contributed approximately \$300 million in equity. The Company received a note of approximately \$248 million from Hercules, which collected the original cash proceeds, recorded tax expenses of approximately \$61 million and retained a 28.57% equity position in CP Kelco. CP Kelco simultaneously acquired Kelco biogums business of Pharmacia Corporation (formerly Monsanto Corporation). Other operating expenses, net, also include Hercules Group affiliate royalty costs, net restructuring costs, environmental costs, net losses on asset dispositions and foreign currency losses totaling \$22,471 thousand, \$3,073 thousand, \$8,500 thousand, \$1,617 thousand and \$43 thousand, respectively.

Other operating expenses, net, in 1999 include Hercules Group affiliate royalty costs of \$27,318 thousand, a gain on sale of investments of \$13,302 thousand, net restructuring costs of \$12,551, environmental costs of \$800 thousand, net losses on asset dispositions of \$184 thousand and foreign currency losses amounting to \$289 thousand.

Edgar Filing: HERCULES INC - Form 10-K/A

14. INTEREST AND DEBT EXPENSE

No interest and debt costs were capitalized during 2001, 2000 and 1999. The costs incurred are presented separately in the consolidated statement of income and are primarily from debt with affiliates.

274

HERCULES INVESTMENTS SARL  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

15. OTHER INCOME (EXPENSE), NET

Other income (expense), net, consists of the following:

	(Dollars in thousands)		
	2001	2000	1999
	----	----	----
Interest income, net	\$ 18,682	\$ 11,124	\$ 9,742
Rent	28	27	(6)
Miscellaneous income (expense), net	1,731	309	(4,532)
	-----	-----	-----
	\$ 20,441	\$ 11,460	\$ 5,204
	=====	=====	=====

16. INCOME TAXES

A summary of the components of the tax provision follows:

	(Dollars in thousands)		
	2001	2000	1999
	----	----	----
Current	\$ 18,341	\$ 31,884	\$ 48,052
Deferred	9,835	14,360	12,967
	-----	-----	-----
Provision for income taxes	\$ 28,176	\$ 46,244	\$ 61,019
	=====	=====	=====

Deferred tax (liabilities) assets at December 31 consist of:

	(Dollars in thousands)	
	2001	2000
	----	----
Depreciation	\$ (37,991)	\$ (41,661)

Edgar Filing: HERCULES INC - Form 10-K/A

Goodwill amortization	(9,497)	(8,819)
Fixed asset valuation	(101)	(2,207)
Intangible asset	(613)	(1,385)
Insurance provision	(4,193)	(4,989)
Replacement provision	(10,491)	(3,282)
Other	(4,817)	(2,151)
	-----	-----
Gross deferred tax liabilities	(67,703)	(64,494)
	-----	-----
Loss carryforwards	950	2,959
Accrued pension	2,169	--
Allowance for doubtful accounts	1,119	58
Inventory valuation	1,506	2,551
Other	602	2,181
	-----	-----
Gross deferred tax assets	6,346	7,749
	-----	-----
Valuation allowance	(1,469)	(703)
	-----	-----
	\$ (62,826)	\$ (57,448)
	=====	=====

275

HERCULES INVESTMENTS SARL  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A reconciliation of the statutory income tax rate to the effective rate follows:

	2001	2000	1999
	----	----	----
Statutory income tax rate	37.5%	37.5%	37.5%
Goodwill amortization	18.1%	0.0%	0.0%
Non-deductible expenses	78.9%	5.0%	1.8%
Non-taxable income	(157.9)%	(4.8)%	(1.6)%
Tax rate differences on subsidiary earnings	344.8%	(1.4)%	(1.2)%
Gain on sale of investment	(22.5)%	(23.5)%	(3.3)%
Effects of rate changes	(14.0)%	0.0%	0.0%
Other	8.2%	4.5%	(2.5)%
	-----	-----	-----
Effective tax rate	293.1%	17.3%	30.7%
	=====	=====	=====

The net operating losses have a carryforward period ranging from 5 years to indefinite, but may be limited in their use in any given year.

17. COMMITMENTS AND CONTINGENCIES

Leases

The Company has operating leases (including office space, transportation, and data processing equipment) expiring at various dates. Rental expense was \$8,822 thousand, \$ 8,076 thousand and \$ 8,786 thousand in 2001, 2000 and 1999,

## Edgar Filing: HERCULES INC - Form 10-K/A

respectively.

At December 31, 2001, minimum rental payments under non-cancelable leases aggregated \$18,823 thousand. The net minimum payments over the next five years and thereafter are \$5,697 thousand in 2002, \$4,008 thousand in 2003, \$2,201 thousand in 2004, \$1,071 thousand in 2005, \$931 thousand in 2006 and \$4,915 thousand beyond 2006.

### Litigation

The Company currently and from time to time is involved in litigation incidental to the conduct of its business. In the opinion of the Company's management, none of such litigation as of December 31, 2001 is likely to have a material adverse effect on the financial position, results of operations, or cash flows of the Company.

### Environmental

The Company has potential liability in connection with obligations to authorities of various EU countries in which it has manufacturing facilities, and to private parties pursuant to contract, for the cost of environmental investigation and/or cleanup at several sites. The estimated range of the reasonably possible share of costs for the investigation and cleanup is between \$5,000 thousand and \$12,000 thousand. The actual costs will depend upon numerous factors, including the actual methods of remediation required or agreed to; outcomes of negotiations with regulatory authorities and private parties; changes in environmental laws and regulations; technological developments; and the years of remedial activity required, which could range from 0 to 30 years.

The Company becomes aware of its obligations relating to sites in which it may have liability for the costs of environmental investigations and/or remedial activities through correspondence from government authorities, or through correspondence from companies with which the Company has contractual obligations, who either request information or notify us of our potential liability. We have established procedures for identifying environmental issues at our plant sites. In addition to environmental audit programs, we have environmental coordinators who are familiar with environmental laws and regulations and act as a resource for identifying environmental issues.

In December 2000, PFW Aroma Chemicals B.V., a company that in 1996 purchased from the Company a Fragrances Plant in Barneveld, NL, submitted a claim of 7,295 thousand EURO. The claim seeks payment of costs alleged to be owed under the 1996 Agreement between the parties. The claim generally alleges that the Company is obligated to pay for the costs of cleaning up contamination at the Barneveld plant and to pay various costs relating to compliance with permit obligations. The Company has questioned its obligation to pay the amounts sought, and is currently in negotiations with PFW regarding this claim.

276

HERCULES INVESTMENTS SARL  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

---

On May 1, 2001, the Company sold a hydrocarbon resins manufacturing facility located in Middelburg, the Netherlands as part of the sale by Hercules of its Resins Division to Eastman Chemical Resins, Inc. Under the Purchase and Sale Agreement between the parties, Hercules retained certain specific liabilities relating to environmental conditions at the Middelburg hydrocarbon resins plant, including pre-existing contamination

## Edgar Filing: HERCULES INC - Form 10-K/A

At December 31, 2001, the total accrued liability of \$9,300 thousand for environmental remediation represents management's best estimate of the probable and reasonably estimable costs related to environmental remediation. The extent of liability is evaluated quarterly. The measurement of the liability is evaluated based on currently available information, including the process of remedial investigations at each site and the current status of negotiations with regulatory authorities regarding the method and extent of remediation that will be required and the negotiations regarding apportionment of costs among other private parties. While it is not feasible to predict the outcome of all pending suits and claims, the ultimate resolution of these environmental matters could have a material effect upon the results of operations and the financial position of the Company.

### 18. RELATED PARTY TRANSACTIONS

The Company has entered into certain agreements with affiliated entities. These agreements were developed in the context of a Hercules Group/subsidiary relationship and therefore may not necessarily reflect the result of arm's-length negotiations between independent parties. All transactions described below are eliminated on consolidation of Hercules.

**Intercompany borrowing and interest:** The Company has intercompany loans with Hercules affiliated entities. The loans with affiliates are included in net Hercules Group investment in the consolidated balance sheet. Interest paid to affiliated entities was \$115,325 thousand, \$42,602 thousand and \$2,581 thousand in 2001, 2000 and 1999, respectively.

**Corporate, regional and other allocations:** As discussed in Note 1, the consolidated financial statements of the Company reflect certain allocated support costs incurred by other entities in the Hercules group and incurred by the Company.. These costs include executive, legal, accounting, tax, auditing, cash management, purchasing, human resources, safety, health and environmental, information management, investor relations and other corporate services. Allocations and charges included in the Company's consolidated financial statements were based either on a direct cost pass-through for items directly identified as related to the Company's activities; a percentage allocation for such services provided based on factors such as sales, net assets, cost of sales; or a relative weighting of geographic activity. These allocations are reflected in the selling, general and administrative line item in the consolidated statement of income. Such allocations and corporate charges totaled approximately \$43,836 thousand, \$23,980 thousand and \$31,596 thousand in 2001, 2000 and 1999, respectively.

**Sales to affiliates:** The Company sells raw material and finished goods inventory in the normal course of business to affiliated companies. The Company's revenues from sales to affiliated companies are presented separately in the consolidated statement of income.

**Purchases from affiliates:** The Company purchases in the normal course of business raw material and finished goods inventory from affiliated companies. The Company's purchases of inventory from affiliated companies is reflected in costs of sales in the consolidated statement of income and totaled \$66,648 thousand, \$221,230 thousand and \$241,737 thousand in 2001, 2000 and 1999, respectively.

**Royalties:** The Company entered into a license agreement in respect of the use of manufacturing formulations and specifications developed and owned by an affiliated entity. Total royalties accrued in respect of this agreement are included in the other operating (income) expense line item in the consolidated statement of income and totaled \$25,164 thousand, \$22,471 thousand and \$27,318 thousand in 2001, 2000 and 1999, respectively.

## Edgar Filing: HERCULES INC - Form 10-K/A

### 19. DERIVATIVE INSTRUMENTS AND RISK MANAGEMENT

The Company enters into forward-exchange contracts to hedge currency exposure.

#### NOTIONAL AMOUNTS AND CREDIT EXPOSURE OF DERIVATIVES

The notional amounts of derivatives summarized below do not represent amounts exchanged by the parties and, thus, are not a measure of the exposure of the Company through its use of derivatives. The amounts exchanged are calculated on the basis of the notional amounts and the other terms of the derivatives, which relate to interest rates or exchange rates.

#### FOREIGN EXCHANGE RISK MANAGEMENT

The Company has selectively used foreign currency forward contracts to offset the effects of exchange rate changes on reported earnings, cash flow, and net asset positions. The primary exposures are denominated in the U.S. Dollar, the

277

### HERCULES INVESTMENTS SARL NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Japanese Yen and the British Pound Sterling. Some of the contracts involve the exchange of two foreign currencies, according to local needs in foreign subsidiaries. The term of the currency derivatives is rarely more than three months. At December 31, 2001 and 2000, the Company had outstanding forward-exchange contracts to purchase foreign currencies aggregating \$87,616 thousand and \$78,281 thousand, respectively, and to sell foreign currencies aggregating \$87,676 thousand and \$78,712 thousand, respectively. The foreign exchange contracts outstanding at December 31, 2001 will mature during 2002.

#### FAIR VALUES

The following table presents the carrying amounts and fair values of the Company's financial instruments at December 31, 2001 and 2000:

	(Dollars in thousands)			
	2001 ----	Fair Value	2000 ----	Fair Value
	Carrying Amount -----	-----	Carrying Amount -----	-----
Foreign exchange contracts	\$ (60)	\$ (60)	\$ (430)	\$ (430)

The carrying amount represents the net unrealized gain or net interest payable associated with the contracts at the end of the period. Fair values of derivative contracts are indicative of cash that would have been required had settlement been December 31, 2001. Foreign exchange contracts are valued based on year-end exchange rates.

### 20. NET HERCULES GROUP INVESTMENT

## Edgar Filing: HERCULES INC - Form 10-K/A

Changes in Net Hercules Group Investment were as follows:

Balance, January 1, 1999	\$ 694,589
Net income	137,779
Other comprehensive loss	(49,869)
Intercompany transactions, net	(95,424)
	-----
Balance, December 31, 1999	687,075
Net income	215,763
Other comprehensive loss	(71,025)
Intercompany transactions, net	(398,179)
	-----
Balance, December 31, 2000	433,634
Net loss	(30,153)
Other comprehensive income	57,700
Intercompany transactions, net	(60,250)
	-----
Balance, December 31, 2001	\$ 400,931
	=====

The Company includes accumulated other comprehensive losses in Net Hercules Group Investment. At December 31, 2001, accumulated other comprehensive income consisted of an additional minimum pension liability and foreign currency translation adjustments, net of tax, of \$1,340 thousand and \$(51,899) thousand, respectively. At December 31, 2000 and 1999, accumulated other comprehensive losses consisted of foreign currency translation adjustments, net of tax, of \$(108,259) thousand and \$(37,234) thousand, respectively.

### 21. SUBSEQUENT EVENT

On April 29, 2002, Hercules completed the sale of its Water Treatment Business to GE Specialty Materials (GESM). Pursuant to the Stock and Asset Agreement for the transaction, the sale included all of the stock of BetzDearborn and the Company. Hercules used the proceeds from the sale to prepay borrowings under its Senior Credit Facility and ESOP Credit Facility. Pursuant to the prepayment, among other things, the stock pledges were released.

278

### REPORT OF INDEPENDENT ACCOUNTANTS

TO THE SHAREHOLDERS AND THE BOARD OF DIRECTORS OF  
HERCULES INCORPORATED  
WILMINGTON, DELAWARE

In our opinion, the accompanying balance sheets and the related statements of operations and comprehensive income (loss) and of cash flows present fairly, in all material respects, the financial position of WSP, Inc., a subsidiary of Hercules Incorporated, at December 31, 2001 and 2000, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2001 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on



Edgar Filing: HERCULES INC - Form 10-K/A

these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America that require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As more fully discussed in Note 7, the Company has restated its December 31, 2000 and 1999 financial statements to correctly reflect equity income (loss) from an equity investment.

PricewaterhouseCoopers LLP  
Philadelphia, Pennsylvania  
December 2, 2002

279

WSP, INC.  
STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

	(Dollars in thousands)		
	2001	Restated 2000	Restated 1999
	-----	-----	-----
Interest income	\$ --	\$ 2,452	\$ --
	-----	-----	-----
Income before income taxes and equity income (loss)	--	2,452	--
Provision for income taxes (Note 6)	--	(3,523)	3,108
	-----	-----	-----
Income before equity income (loss)	--	5,975	(3,108)
Equity income (loss) of affiliated company, net of tax (Note 3)	2,691	(22,770)	7,769
	-----	-----	-----
Net income (loss)	2,691	(16,795)	4,661
Translation gain, net of tax	624	637	440
	-----	-----	-----
Comprehensive income (loss)	\$ 3,315	\$ (16,158)	\$ 5,101
	-----	-----	-----

The accompanying notes are an integral part of the financial statements.

280

WSP, INC.  
BALANCE SHEETS

(Dollars in thousands)

Edgar Filing: HERCULES INC - Form 10-K/A

	Restated	
	December 31,	
	2001	2000
	-----	-----
ASSETS		
Investments (Note 3)	\$126,828	\$123,513
	-----	-----
Total assets	\$126,828	\$123,513
	=====	=====
LIABILITIES AND NET HERCULES GROUP INVESTMENT		
Current liabilities		
Current tax liability (Note 6)	\$ --	\$ 981
	-----	-----
Total current liabilities	--	981
Deferred income taxes (Note 6)	--	--
	-----	-----
Total liabilities	--	981
Commitments and contingencies (Note 4)	--	--
	-----	-----
Net Hercules Group investment (Note 5)		
Accumulated other comprehensive income	1,701	1,077
Intercompany balances, net	125,127	121,455
	-----	-----
Net Hercules Group investment	126,828	122,532
	-----	-----
Total liabilities and net Hercules Group investment	\$126,828	\$123,513
	=====	=====

The accompanying notes are an integral part of the financial statements.

281

WSP, INC.  
STATEMENTS OF CASH FLOWS

	(Dollars in	
	Re	
	Year Ende	
	2001	2000
	-----	-----
CASH FLOW FROM OPERATING ACTIVITIES:		
Net income (loss)	\$ 2,691	\$(1,077)
Adjustments to reconcile net income (loss) to net cash provided from operations:		
Affiliates' (earnings) losses in excess of dividends received	(2,691)	--
Deferred income taxes	--	--
Accruals and deferrals of cash receipts and payments:		
Accounts payable and accrued expenses	(981)	--
	-----	-----
Net cash (used in) provided by operations	(981)	(981)
CASH FLOW FROM INVESTING ACTIVITIES:		

## Edgar Filing: HERCULES INC - Form 10-K/A

Net cash (used in) investing activities	--	
<hr/>		
CASH FLOW FROM FINANCING ACTIVITIES:		
Transfers from (to) Hercules Group	981	
<hr/>		
Net cash provided by (used in) financing activities	981	
<hr/>		
Net increase in cash and cash equivalents	--	
Cash and cash equivalents at beginning of year	--	
<hr/>		
Cash and cash equivalents at end of year	\$ --	\$
<hr/>		
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash paid during the year for:		
Income taxes paid, net	\$ 981	

The accompanying notes are an integral part of the financial statements.

282

WSP, INC.  
NOTES TO FINANCIAL STATEMENTS

### 1. DESCRIPTION OF BUSINESS AND BASIS OF PRESENTATION

WSP, Inc. ("WSP"), a U.S. holding company, is owned 100% by Hercules Incorporated ("Hercules"). WSP owns 0.5818% of Aqualon Company, a U.S. partnership that is engaged in providing products and services to manage the properties of aqueous (water-based) systems. WSP also owns 49% of FiberVisions, L.L.C., a limited liability corporation that serves worldwide markets for polypropylene nonwoven fiber used to make disposable hygiene products.

Historically, separate company stand-alone financial statements were not prepared for WSP. In November 2000, Hercules amended its senior credit facility and ESOP credit facility (the "Facilities"). The Facilities, as amended, are secured by liens on Hercules' property and assets (and those of Hercules' Canadian Subsidiaries), a pledge of the stock and partnership interests of substantially all of Hercules' domestic subsidiaries (including WSP) and 65% of the stock of foreign subsidiaries directly owned by Hercules, and a pledge of Hercules' domestic intercompany indebtedness. These financial statements present the financial information on WSP, a collateral party to the Hercules debt, based on Hercules' understanding of Securities and Exchange Commission's interpretation and application of Rule 3-16 under the Securities and Exchange Commission's Regulation S-X. These statements were derived from historical accounting records.

On April 29, 2002, in connection with Hercules' sale of its Water Treatment Business (see Note 8) and the repayment of the Facilities, the stock pledges were released. As a result, based on Hercules' current debt structure, these separate company stand-alone financial statements will not be required for the fiscal year ending December 31, 2002.

WSP participates in Hercules' centralized cash management system. Accordingly, cash received from WSP operations is transferred to Hercules on a periodic basis, and Hercules funds all operational and capital requirements.

## Edgar Filing: HERCULES INC - Form 10-K/A

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### USE OF ESTIMATES

Preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

#### REVENUE RECOGNITION

WSP recognizes revenue, including interest income, when the earnings process is complete.

#### INCOME TAXES

The Company's operations have historically been included in the consolidated income tax returns filed by its parent. Income tax expense in the accompanying financial statements has been computed assuming the Company filed separate income tax returns. Differences between this calculation of income taxes currently payable and consolidated amounts reported in the consolidated financial statements of the parent have been reflected as net Hercules Group investment.

#### NET HERCULES GROUP INVESTMENT

The net Hercules Group investment account reflects the balance of WSP's historical earnings, intercompany amounts, income taxes, taxes accrued and deferred, foreign currency translation and other transactions between WSP and the Hercules Group.

#### NEW ACCOUNTING PRONOUNCEMENTS

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets. The Company does not believe this statement will have a material effect on its financial statements.

283

WSP, INC.

NOTES TO FINANCIAL STATEMENTS

#### RECLASSIFICATIONS

Certain amounts in the 2000 and 1999 consolidated financial statements and notes have been reclassified to conform to the 2001 presentation.

### 3. INVESTMENTS

Total investments in affiliated companies were as follows:

(Dollars in thousands)	
2001	2000
-----	-----

## Edgar Filing: HERCULES INC - Form 10-K/A

Investment in FiberVisions, L.L.C	\$125,013	\$121,698
Investment in Aqualon Company	1,815	1,815
	-----	-----
 Total Investments	 \$126,828	 \$123,513
	=====	=====

Summarized financial information for FiberVisions, L.L.C. at December 31, 2001 and 2000 and the years then ended is as follows:

	(Dollars in thousands)	
	2001	2000
	-----	-----
Current assets	\$ 61,232	\$ 68,290
Non-current assets	301,892	322,085
Current liabilities	40,430	45,780
Other non-current liabilities	68,805	74,024

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Net sales	\$ 218,366	\$ 251,859	\$ 253,648
Gross profit	33,973	28,726	59,952
Net earnings	5,491	(46,468)	15,855

The summarized financial information above does not include certain intercompany assets and liabilities recorded in FiberVisions, L.L.C. These intercompany accounts have been reclassified to the net Hercules Group investment in accordance with the Company's accounting policy (see Note 2).

#### 4. COMMITMENTS AND CONTINGENCIES

WSP currently and from time to time is involved in litigation incidental to the conduct of its business. In the opinion of WSP's management, none of such litigation as of December 31, 2001 is likely to have a material adverse effect on the financial position and results of operations of WSP.

284

WSP, INC.  
NOTES TO FINANCIAL STATEMENTS

#### 5. NET HERCULES GROUP INVESTMENT

Changes in net Hercules Group investment were as follows:

(Dollars in thousands)

Edgar Filing: HERCULES INC - Form 10-K/A

Balance, January 1, 1999	\$ 136,041
Net income	4,661
Other comprehensive income	440
Intercompany transactions, net	--
	-----
Balance, December 31, 1999	141,142
Net loss	(16,795)
Other comprehensive income	637
Intercompany transactions, net	(2,452)
	-----
Balance, December 31, 2000	122,532
Net income	2,691
Other comprehensive income	624
Intercompany transactions, net	981
	-----
Balance, December 31, 2001	\$ 126,828
	-----

6. INCOME TAXES

The domestic components of income before taxes are presented below:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Domestic	\$ --	\$ 2,452	\$ --
	-----	-----	-----
	\$ --	\$ 2,452	\$ --
	=====	=====	=====

A summary of the components of the tax provision follows:

	(Dollars in thousands)		
	2001	2000	1999
	-----	-----	-----
Currently payable	\$ --	\$ 981	\$ --
Deferred	--	(4,504)	3,108
	-----	-----	-----
Provision for income taxes	\$ --	\$(3,523)	\$3,108
	=====	=====	=====

Deferred tax assets at December 31, consist of the following:

	(Dollars in thousands)	
	2001	2000
	-----	-----

Edgar Filing: HERCULES INC - Form 10-K/A

Partnership basis	\$ --	\$ --
	----	----
Gross deferred tax assets	--	--
Valuation allowance	--	--
	----	----
	\$ --	\$ --
	=====	=====

285

WSP, INC.  
NOTES TO FINANCIAL STATEMENTS

7. RESTATEMENT

The Company has restated its December 31, 2000 and 1999 financial statements to correctly reflect equity income (loss) from an equity investment. During 2002, the Company discovered that the prior financial statements of its 49% investment in FiberVisions, L.L.C. did not include income tax provisions for its subsidiaries whose income is subject to corporate income taxes at the subsidiary level. Accordingly, the financial statements for December 31, 2000 and 1999 have been restated. The effect of these adjustments on the Company's December 31, 2000 and 1999 financial statements is as follows:

	(Dollars in thousands)		
	December 31, 2000		
	As Previously Reported	As Restated	As Pre Repo
	-----	-----	-----
<b>BALANCE SHEET</b>			
Investments	\$ 126,138	\$ 123,513	\$ 151
Current tax liability	919	981	
Deferred income taxes (asset) liability	(4,143)	-	4
Net Hercules Group investment			
January 1	146,043	141,142	136
December 31	129,362	122,532	146
<b>INCOME STATEMENT</b>			
(Benefit)/Provision for income taxes	\$ (8,205)	\$ (3,523)	\$ 4
Equity (loss) income of affiliated company	(25,895)	(22,770)	13
Net (loss) income	(15,238)	(16,795)	8
Translation gain	910	637	
Comprehensive (loss) income	(14,328)	(16,158)	9
<b>CASH FLOW STATEMENT</b>			
Net (loss) income	\$ (15,238)	\$ (16,795)	\$ 8
Affiliates' losses (earnings) in excess of dividends			

## Edgar Filing: HERCULES INC - Form 10-K/A

received	25,895	22,770	(13
Accounts payable and accrued expenses	820	981	
Noncurrent assets and liabilities	(9,124)	(4,504)	4
Transfers (to) from Hercules Group	(2,353)	(2,452)	
Cash paid during the year for:			
Income taxes paid, net	\$ 99	\$ -	\$

### 8. SUBSEQUENT EVENTS

On April 29, 2002, Hercules completed the sale of its Water Treatment Business to GE Specialty Materials (GESM). Pursuant to the Stock and Asset Agreement for the transaction, the sale was executed using the stock of BetzDearborn, Inc. and all of the assets, liabilities, and/or equity interests relating to the Water Treatment Business. Hercules used the proceeds from the sale to prepay borrowings under its Senior Credit Facility and ESOP Credit Facility. Pursuant to the prepayment, among other things, the stock pledges were released.

Effective January 1, 2002, Hercules adopted the provisions of Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142") and determined it has the following reporting units: BetzDearborn, Pulp and Paper, Aqualon, FiberVisions and Pinova (formerly Rosins and Terpenes). In the first quarter, 2002 Hercules completed its transitional impairment review and determined that FiberVisions' recorded goodwill was impaired. Accordingly, at March 31, 2002 Hercules recognized an after-tax impairment loss of \$87 million as a cumulative effect of a change in accounting principle relating to its FiberVisions reporting unit.

286

### PART IV

#### ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K:

(a) Documents filed as part of this Report:

1. Financial Statements

See Item 8 for an Index to the Consolidated Financial Statements of Hercules Incorporated.

2. Financial Statement Schedules:

None

3. Exhibits:

A complete listing of exhibits required is included in the Exhibit Index that precedes the Exhibits filed with this Report.

(b) Reports on Form 8K:

None

HERCULES INCORPORATED



Edgar Filing: HERCULES INC - Form 10-K/A

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following person on behalf of the registrant in the capacity indicated on December 13, 2002.

HERCULES INCORPORATED

By: /s/ Fred G. Aanonsen

-----  
Fred G. Aanonsen  
Vice President and Controller  
(Principal Accounting Officer and duly  
authorized signatory)  
December 13, 2002

CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, William H. Joyce, Chairman and Chief Executive Officer, certify that:

1. I have reviewed this annual report on Form 10-K/A of Hercules Incorporated;
2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;
3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report.

/s/ William H. Joyce

-----  
William H. Joyce  
Chairman & Chief Executive Officer  
December 13, 2002

CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Fred G. Aanonsen, Vice President and Controller, certify that:

## Edgar Filing: HERCULES INC - Form 10-K/A

1. I have reviewed this annual report on Form 10-K/A of Hercules Incorporated;
2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;
3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report.

/s/ Fred G. Aanonsen

-----  
Fred G. Aanonsen  
Vice President and Controller  
December 13, 2002

### EXHIBIT INDEX

NUMBER	DESCRIPTION
-----	-----
23.1	Consent of PricewaterhouseCoopers LLP with respect to Hercules Incorporated
23.2	Consent of PricewaterhouseCoopers LLP with respect to Aqualon Company
23.3	Consent of PricewaterhouseCoopers LLP with respect to BetzDearborn Inc.
23.4	Consent of PricewaterhouseCoopers LLP with respect to BetzDearborn Canada, Inc.
23.5	Consent of PricewaterhouseCoopers LLP with respect to BetzDearborn Europe, Inc.
23.6	Consent of PricewaterhouseCoopers LLP with respect to BetzDearborn International, Inc.
23.7	Consent of PricewaterhouseCoopers LLP with respect to BL Technologies, Inc.
23.8	Consent of PricewaterhouseCoopers with respect to FiberVisions A/S
23.9	Consent of PricewaterhouseCoopers LLP with respect to FiberVisions Incorporated

## Edgar Filing: HERCULES INC - Form 10-K/A

- 23.10 Consent of PricewaterhouseCoopers LLP with respect to FiberVisions L.L.C.
- 23.11 Consent of PricewaterhouseCoopers LLP with respect to FiberVisions Products, Inc.
- 23.12 Consent of PricewaterhouseCoopers LLP with respect to Hercules Canada, Inc.
- 23.13 Consent of PricewaterhouseCoopers LLP with respect to Hercules Chemicals (Taiwan) Co., Limited
- 23.14 Consent of PricewaterhouseCoopers LLP with respect to Hercules Credit, Inc.
- 23.15 Consent of PricewaterhouseCoopers Accountants N.V. with respect to Hercules GB Holdings Limited
- 23.16 Consent of PricewaterhouseCoopers LLP with respect to Hercules International Limited
- 23.17 Consent of PricewaterhouseCoopers Accountants N.V. with respect to Hercules Investments Sarl
- 23.18 Consent of PricewaterhouseCoopers LLP with respect to WSP, Inc.
- 99.1 Certification of Chairman and Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 99.2 Certification of Vice President and Controller Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002