KBR, INC.
Form 10-Q
November 01, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

ý Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended September 30, 2016
OR
¨ Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from to
Commission File Number: 1-33146

KBR, Inc.
(Exact name of registrant as specified in its charter)

Delaware	20-4536774
(State of incorporation)	(I.R.S. Employer Identification No.)
601 Jefferson Street, Suite 3400, Houston, Texas	77002
(Address of principal executive offices)	(Zip Code)

(713) 753-3011
(Registrant's telephone number including area code)

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 ý No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No ¨

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

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

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

As of October 12, 2016, there were 142,668,161 shares of KBR, Inc. Common Stock, par value $0.001 per share, outstanding.

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Forward-Looking and Cautionary Statements

This Quarterly Report on Form 10-Q contains certain statements that are, or may be deemed to be, "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. The Private Securities Litigation Reform Act of 1995 provides safe harbor provisions for forward-looking information. Some of the statements contained in this Quarterly Report on Form 10-Q are forward-looking statements. All statements other than statements of historical fact are, or may be deemed to be, forward-looking statements. The words "believe," "may," "estimate," "continue," "anticipate," "intend," "plan," "expect" and similar expressions are intended to identify forward-looking statements. Forward-looking statements include information concerning our possible or assumed future financial performance and results of operations.

We have based these statements on our assumptions and analyses in light of our experience and perception of historical trends, current conditions, expected future developments and other factors we believe are appropriate in the circumstances. Forward-looking statements by their nature involve substantial risks and uncertainties that could significantly affect expected results, and actual future results could differ materially from those described in such statements. While it is not possible to identify all factors, factors that could cause actual future results to differ materially, include the risks and uncertainties disclosed in our 2015 Annual Report on Form 10-K contained in Part I under "Risk Factors" and in our Quarterly Reports on Form 10-Q for the quarterly periods ended March 31, 2016 and June 30, 2016 in Part II under "Risk Factors" and in this Quarterly Report on Form 10-Q in Part II under "Risk Factors."

Many of these factors are beyond our ability to control or predict. Any of these factors, or a combination of these factors, could materially and adversely affect our future financial condition or results of operations and the ultimate accuracy of the forward-looking statements. These forward-looking statements are not guarantees of our future performance, and our actual results and future developments may differ materially and adversely from those projected in the forward-looking statements. We caution against putting undue reliance on forward-looking statements or projecting any future results based on such statements or on present or prior earnings levels. In addition, each forward-looking statement speaks only as of the date of the particular statement, and we undertake no obligation to publicly update or revise any forward-looking statement.

PART I. FINANCIAL INFORMATION

Item 1. Financial Information

KBR, Inc.
Condensed Consolidated Statements of Operations
(In millions, except for per share data)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Revenues	$1,073	$1,199	$3,078	$4,016
Cost of revenues	(1,109)	(1,112)	(2,972)	(3,785)
Gross profit (loss)	(36)	87	106	231
Equity in earnings of unconsolidated affiliates	19	35	81	123
General and administrative expenses	(43)	(38)	(111)	(119)
Asset impairment and restructuring charges	(7)	(15)	(21)	(34)
Gain on disposition of assets	—	6	6	34
Operating income (loss)	(67)	75	61	235
Other non-operating income (expense)	(1)	3	1	4
Income (loss) before income taxes and noncontrolling interests	(68)	78	62	239
Benefit (provision) for income taxes	11	(19)	(27)	(61)
Net income (loss)	(57)	59	35	178
Net income attributable to noncontrolling interests	(6)	(4)	(9)	(17)
Net income (loss) attributable to KBR	$(63)	$55	$26	$161
Net income (loss) attributable to KBR per share:				
Basic	$(0.44)	$0.38	$0.18	$1.11
Diluted	$(0.44)	$0.38	$0.18	$1.11
Basic weighted average common shares outstanding	142	144	142	144
Diluted weighted average common shares outstanding	142	144	142	144
Cash dividends declared per share	$0.08	$0.08	$0.24	$0.24

See accompanying notes to condensed consolidated financial statements.

KBR, Inc.
Condensed Consolidated Statements of Comprehensive Income (Loss)
(In millions)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Net income (loss)	$(57)	$59	$35	$178
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments:				
Foreign currency translation adjustments, net of tax	10	(13)	21	(74)
Reclassification adjustment included in net income	—	—	—	—
Foreign currency translation adjustments, net of taxes of $2, $(5), $2 and $(4)	10	(13)	21	(74)
Pension and post-retirement benefits, net of tax:				
Actuarial gains (losses), net of tax	—	—	—	—
Reclassification adjustment included in net income	6	10	18	32
Pension and post-retirement benefits, net of taxes of $(1), $(2), $(4) and $(7)	6	10	18	32
Changes in fair value of derivatives:				
Changes in fair value of derivatives, net of tax	—	—	—	—
Reclassification adjustment included in net income	(1)	1	(1)	1
Changes in fair value of derivatives, net of taxes of $0, $0, $0 and $0	(1)	1	(1)	1
Other comprehensive income (loss), net of tax	15	(2)	38	(41)
Comprehensive income	(42)	57	73	137
Less: Comprehensive income attributable to noncontrolling interests	(5)	(6)	(8)	(20)
Comprehensive income (loss) attributable to KBR	$(47)	$51	$65	$117

See accompanying notes to condensed consolidated financial statements.

KBR, Inc.
Condensed Consolidated Balance Sheets
(In millions, except share data)

	September 30, 2016 (Unaudited)	December 31, 2015
Assets		
Current assets:		
Cash and equivalents	$ 569	$ 883
Accounts receivable, net of allowance for doubtful accounts of $15 and $17	708	628
Costs and estimated earnings in excess of billings on uncompleted contracts ("CIE")	390	224
Other current assets	123	109
Total current assets	1,790	1,844
Claims and accounts receivable	528	526
Property, plant, and equipment, net of accumulated depreciation of $338 and $352 (including net PPE of $39 and $48 owned by a variable interest entity)	165	169
Goodwill	953	324
Intangible assets, net of accumulated amortization of $97 and $91	257	35
Equity in and advances to unconsolidated affiliates	327	281
Deferred income taxes	94	99
Other assets	128	134
Total assets	$ 4,242	$ 3,412
Liabilities and Shareholders’ Equity		
Current liabilities:		
Accounts payable	$ 568	$ 438
Billings in excess of costs and estimated earnings on uncompleted contracts ("BIE")	537	509
Accrued salaries, wages and benefits	203	173
Nonrecourse project debt	9	10
Other current liabilities	233	263
Total current liabilities	1,550	1,393
Pension obligations	258	333
Employee compensation and benefits	90	105
Income tax payable	90	78
Deferred income taxes	163	94
Nonrecourse project debt	40	51
Revolving credit agreement	650	—
Deferred income from unconsolidated affiliates	96	100
Other liabilities	208	206
Total liabilities	3,145	2,360
KBR shareholders’ equity:		
Preferred stock, $0.001 par value, 50,000,000 shares authorized, 0 shares issued and outstanding	—	—
Common stock, $0.001 par value, 300,000,000 shares authorized, 175,688,535 and 175,108,100 shares issued, and 142,667,745 and 142,058,356 shares outstanding	—	—
Paid-in capital in excess of par ("PIC")	2,083	2,070
Accumulated other comprehensive loss ("AOCL")	(792)	(831)
Retained earnings	587	595
Treasury stock, 33,020,790 and 33,049,744 shares, at cost	(767)	(769)

Total KBR shareholders’ equity	1,111	1,065
Noncontrolling interests ("NCI")	(14)	(13)
Total shareholders’ equity	1,097	1,052
Total liabilities and shareholders’ equity	$ 4,242	$ 3,412

See accompanying notes to condensed consolidated financial statements.

KBR, Inc.
Condensed Consolidated Statements of Cash Flows
(In millions)
(Unaudited)

	Nine Months Ended September 30,	
	2016	2015
Cash flows provided by (used in) operating activities:		
Net income	$35	$178
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	31	29
Equity in earnings of unconsolidated affiliates	(81)	(123)
Deferred income tax expense	7	14
Gain on disposition of assets	(6)	(34)
Other	10	29
Changes in operating assets and liabilities:		
Accounts receivable, net of allowance for doubtful accounts	9	(19)
Costs and estimated earnings in excess of billings on uncompleted contracts	25	168
Accounts payable	39	(239)
Billings in excess of costs and estimated earnings on uncompleted contracts	14	(10)
Accrued salaries, wages and benefits	(19)	(5)
Reserve for loss on uncompleted contracts	(15)	(100)
(Advances to) payments from unconsolidated affiliates, net	(3)	10
Distributions of earnings from unconsolidated affiliates	43	84
Income taxes payable	(19)	(7)
Pension funding	(31)	(37)
Net settlement of derivative contracts	(8)	(40)
Other assets and liabilities	(23)	17
Total cash flows provided by (used in) operating activities	8	(85)
Cash flows (used in) provided by investing activities:		
Purchases of property, plant and equipment	(8)	(8)
Proceeds from sale of assets or investments	2	71
Payments for investments in equity method joint ventures	(5)	(15)
Acquisition of businesses, net of cash acquired	(911)	—
Total cash flows (used in) provided by investing activities	$(922)	$48

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KBR, Inc.
Condensed Consolidated Statements of Cash Flows
(In millions)
(Unaudited)

	Nine Months Ended September 30,	
	2016	2015
Cash flows provided by (used in) financing activities:		
Payments to reacquire common stock	$(2)	$(22)
Acquisition of noncontrolling interest	—	(40)
Distributions to noncontrolling interests	(9)	(21)
Payments of dividends to shareholders	(34)	(35)
Net proceeds from issuance of common stock	—	1
Borrowings on revolving credit agreement	700	—
Payments on revolving credit agreement	(50)	—
Payments on short-term and long-term borrowings	(5)	(7)
Other	—	(4)
Total cash flows provided by (used in) financing activities	600	(128)
Effect of exchange rate changes on cash	—	(37)
Decrease in cash and equivalents	(314)	(202)
Cash and equivalents at beginning of period	883	970
Cash and equivalents at end of period	$569	$768
Supplemental disclosure of cash flows information:		
Cash paid for interest	$7	$8
Cash paid for income taxes (net of refunds)	$31	$56
Noncash financing activities		
Dividends declared	$12	$12

See accompanying notes to condensed consolidated financial statements.

KBR, Inc.
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Note 1. Description of Company and Significant Accounting Policies

KBR, Inc., a Delaware corporation, was formed on March 21, 2006 and is headquartered in Houston, Texas. KBR, Inc. and its wholly owned and majority-owned subsidiaries (collectively referred to herein as "KBR", "the Company", "we", "us" or "our") is a global provider of differentiated, professional services and technologies across the asset and program life cycle within the hydrocarbons and government services industries. Our capabilities include highly-specialized engineering services, mission and logistics support solutions, technology licensing, consulting, procurement, construction, construction management, program management, operations, maintenance and other support services to a diverse customer base, including domestic and foreign governments, international and national oil and gas companies, independent refiners, petrochemical producers, fertilizer producers and manufacturers.

Principles of Consolidation

Our condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP") and include the accounts of KBR and our wholly owned and majority-owned subsidiaries and variable interest entities ("VIEs") of which we are the primary beneficiary. We account for investments over which we have significant influence but not a controlling financial interest using the equity method of accounting. See Note 9 to our condensed consolidated financial statements for further discussion on our equity investments and VIEs. The cost method is used when we do not have the ability to exert significant influence. All material intercompany balances and transactions are eliminated in consolidation.

Certain prior year amounts have been reclassified to conform to the current year presentation on the condensed consolidated statements of operations, condensed consolidated balance sheets and the condensed consolidated statements of cash flows.

We have evaluated all events and transactions occurring after the balance sheet date but before the financial statements were issued and have included the appropriate disclosures.

Use of Estimates

The preparation of our condensed consolidated financial statements in conformity with U.S. GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Areas requiring significant estimates and assumptions by our management include the following:

- project revenues, costs and profits on engineering and construction contracts, including recognition of estimated losses on uncompleted contracts
- project revenues, costs and profits on government services contracts
- provisions for uncollectible receivables and client claims and recoveries of costs from subcontractors, vendors and others
- provisions for income taxes and related valuation allowances and tax uncertainties
- recoverability of goodwill
- recoverability of other intangibles and long-lived assets and related estimated lives
- recoverability of equity method and cost method investments

- valuation of pension obligations and pension assets
- accruals for estimated liabilities, including litigation accruals
- consolidation of VIEs
- valuation of share-based compensation
- valuation of assets and liabilities acquired in business combinations

In accordance with normal practice in the construction industry, we include in current assets and current liabilities amounts related to construction contracts realizable and payable over a period in excess of one year. If the underlying estimates and assumptions upon which the financial statements are based change in the future, actual amounts may differ from those included in the accompanying condensed consolidated financial statements.

Adoption of New Accounting Standards

Consolidation. Effective January 1, 2016, we adopted Accounting Standards Update ("ASU") No. 2015-02, Consolidation (Topic 810) - Amendments to the Consolidation Analysis, which was issued by the Financial Accounting Standards Board ("FASB") on February 18, 2015. This ASU amends the consolidation guidance for VIEs as well as general partners' investments in limited partnerships and modifies the evaluation of whether limited partnerships and similar legal entities are VIEs or voting interest entities. ASU 2015-02 is effective for annual periods beginning after December 15, 2015 and interim periods within those annual periods. The adoption of ASU 2015-02 did not have a material impact on our financial statements.

Additional Balance Sheet Information

Other Current Assets

Included in the "other current assets" balance on our condensed consolidated balance sheets as of September 30, 2016 and December 31, 2015 are prepaid taxes and other prepaid assets of $61 million and $58 million, respectively.

Other Current Liabilities

The components of "other current liabilities" on our condensed consolidated balance sheets as of September 30, 2016 and December 31, 2015 are presented below:

Dollars in millions	September 30, 2016	December 31, 2015
Reserve for estimated losses on uncompleted contracts (a)	$ 53	$ 60
Retainage payable	45	49
Income taxes payable	24	56
Value-added tax payable	14	12
Insurance payable	13	12
Dividend payable	12	12
Other miscellaneous liabilities (b)	72	62
Total other current liabilities	$ 233	$ 263

(a) See Note 2 for further discussion on our reserve for estimated losses on uncompleted contracts.
(b) Included in "other miscellaneous liabilities" is deferred rent of $4 million and $7 million as of September 30, 2016 and December 31, 2015, respectively.

Other Liabilities

Included in "other liabilities" on our condensed consolidated balance sheets as of September 30, 2016 and December 31, 2015 is noncurrent deferred rent of $110 million and $114 million, respectively. Also included in "other liabilities" is a payable to our former parent of $19 million in each of the periods presented. This amount will be paid to our former parent upon receipt of a tax refund from the United States ("U.S.") Internal Revenue Service in an amount greater than or equal to $19 million.

Note 2. Business Segment Information

We are organized into three core business segments and two non-core business segments. Our three core business segments focus on our core strengths in technology and consulting, engineering and construction, and government services. Our two non-core business segments are our Non-strategic Business segment, which includes businesses we intend to exit upon completion of existing contracts because they are no longer a part of our future strategic focus, and "Other", which includes our corporate expenses and general and administrative expenses not allocated to the other business segments. Each business segment excluding Other reflects a reportable segment led by a separate business segment president who reports directly to our chief operating decision maker ("CODM"). Business segment performance is evaluated by our CODM using gross profit (loss) and equity in earnings of unconsolidated affiliates, which is defined as business segment revenues less the cost of revenues, and includes overhead directly attributable to the business segment.

Our business segments are described below.

Technology & Consulting ("T&C"). Our T&C business segment combines proprietary KBR technologies, knowledge-based services and our three specialist consulting brands, Granherne, Energo and GVA, under a single customer-facing global business. This business segment provides licensed technologies and consulting services throughout the oil and gas value chain, from wellhead to crude refining and through to specialty chemicals production. In addition to sharing many of the same customers, these brands share the approach of early and continuous customer involvement as they deliver optimal solutions to meet customer objectives through early planning and scope definition, advanced technologies, and project lifecycle support.

Engineering & Construction ("E&C"). Our E&C business segment leverages our operational and technical excellence as a global provider of engineering, procurement, construction ("EPC"), commissioning and maintenance services for oil and gas, refining, petrochemical and chemical customers. E&C is managed on a geographic basis in order to facilitate close proximity to our customers and our people, while utilizing a consistent global execution strategy.

Government Services ("GS"). Our GS business segment provides full life-cycle support solutions to defense, space, aviation and other programs and missions for governmental agencies in the U.S., United Kingdom ("U.K."), and Australia. These solutions span from research and development, through systems engineering, test and evaluation, to program management, operations, maintenance and field logistics. Our recent acquisitions, as described in Note 3 to our condensed consolidated financial statements, have been combined with our existing U.S. operations within this business segment and are transitioning to operate under the "KBRwyle" brand.

Non-strategic Business. Our Non-strategic Business segment represents the operations or activities that we intend to exit upon completion of existing contracts. This segment also included businesses we exited upon sale to third parties during 2015.

Other. Our Other business segment includes our corporate expenses and general and administrative expenses not allocated to the business segments above and any future activities that do not individually meet the criteria for segment presentation.

The following table presents revenues, gross profit (loss), equity in earnings of unconsolidated affiliates and operating income (loss) by reporting segment.

Operations by Reportable Segment

Dollars in millions	Three Months Ended September 30, 2016	Three Months Ended September 30, 2015	Nine Months Ended September 30, 2016	Nine Months Ended September 30, 2015
Revenues:				
Technology & Consulting	$67	$79	$262	$231
Engineering & Construction	595	828	1,822	2,758
Government Services	401	176	840	489
Other	—	—	—	—
Subtotal	1,063	1,083	2,924	3,478
Non-strategic Business	10	116	154	538
Total revenues	$1,073	$1,199	$3,078	$4,016
Gross profit (loss):				
Technology & Consulting	$17	$17	$49	$57
Engineering & Construction	1	48	65	155
Government Services	32	8	94	3
Other	—	—	—	—
Subtotal	50	73	208	215
Non-strategic Business	(86)	14	(102)	16
Total gross profit (loss)	$(36)	$87	$106	$231
Equity in earnings of unconsolidated affiliates:				
Technology & Consulting	$—	$—	$—	$—
Engineering & Construction	11	26	52	87
Government Services	8	9	29	36
Other	—	—	—	—
Subtotal	19	35	81	123
Non-strategic Business	—	—	—	—
Total equity in earnings of unconsolidated affiliates	$19	$35	$81	$123
Asset impairment and restructuring charges:				
Technology & Consulting	$(1)	$—	$(1)	$(1)
Engineering & Construction	(6)	(13)	(20)	(25)
Government Services	—	—	—	—
Other	—	(1)	—	(5)
Subtotal	(7)	(14)	(21)	(31)
Non-strategic Business	—	(1)	—	(3)
Total asset impairment and restructuring charges	$(7)	$(15)	$(21)	$(34)
Segment operating income (loss):				
Technology & Consulting	$16	$16	$44	$53
Engineering & Construction	(2)	61	76	201
Government Services	25	15	104	34
Other	(21)	(28)	(65)	(92)
Subtotal	18	64	159	196
Non-strategic Business	(85)	11	(98)	39
Total segment operating income (loss)	$(67)	$75	$61	$235

Changes in Estimates

There are many factors that may affect the accuracy of our cost estimates and ultimately our future profitability. These include, but are not limited to, the availability and costs of resources (such as labor, materials and equipment), productivity and weather, and for unit rate and construction service contracts, the availability and detail of customer supplied engineering drawings. With a portfolio of more than one thousand contracts, we generally realize both lower and higher than expected margins on projects in any given period. We recognize revisions of revenues and costs in the period in which the revisions are known. This may result in the recognition of costs before the recognition of related revenue recovery, if any. However, historically, our estimates have been reasonably dependable regarding the recognition of revenues and profit on percentage of completion contracts. Changes in estimates by business segment, which significantly impacted operating income during the periods presented, are as follows:

Engineering & Construction

During the three and nine months ended September 30, 2016, we recognized unfavorable changes in estimates of losses of $40 million and $110 million, respectively, on an EPC ammonia project in the U.S. primarily due to unforeseen costs related to the mechanical failure of a vendor supplied compressor and pumps that occurred during commissioning as well as various mechanical issues encountered during start-up. These issues delayed completion of the project to October 2016, which resulted in increased costs and our recognition of contractual liquidated damages due to the client. Included in the reserve for estimated losses on uncompleted contracts, which is a component of "other current liabilities" on our condensed consolidated financial statements, is $6 million and $4 million as of September 30, 2016 and December 31, 2015, respectively, related to this project. The project has completed performance testing and in October 2016, care, custody and control of the plant were transferred to the customer. Our estimates of revenues and costs at completion have been, and may continue to be, impacted by remaining punch list items and warranty obligations. Our estimated loss at completion as of September 30, 2016 represents our best estimate based on current information. Actual results could differ from the estimates we have used to account for this project as of September 30, 2016. During the three and nine months ended September 30, 2015, we recognized an unfavorable change in estimated costs at completion on this project of $12 million and $13 million, respectively, primarily due to increased subcontractor costs.

During the three and nine months ended September 30, 2016, we recognized $9 million of additional gross profit resulting from a favorable change in estimate resulting from the final settlement of outstanding claims on a legacy project in Canada partially offset by a reduction in gross profit of $7 million on an EPC project in the U.S. from unfavorable changes in estimated costs due to schedule mitigation activities associated with weather delays. The EPC project is 52% complete as of September 30, 2016.

During the three and nine months ended September 30, 2016, revenues, gross profit, and segment operating income include $3 million and $59 million, respectively, related to a favorable change in estimate as a result of reaching a settlement on close out of a liquefied natural gas ("LNG") project in Africa.

During the three and nine months ended September 30, 2015, we recognized favorable changes in estimates of losses of $4 million and $21 million, respectively, on our seven Canadian pipe fabrication and module assembly projects, primarily due to negotiated settlements. All of these projects were completed in 2015.

Government Services

During the nine months ended September 30, 2016, revenues, gross profit, and segment operating income included a favorable change in estimate of $33 million as a result of reaching a settlement with the U.S. government for reimbursement of previously expensed legal fees associated with the sodium dichromate litigation. See Note 13 to our condensed consolidated financial statements for information related to the settlement with the U.S. government. Additionally, we recognized a $15 million favorable change to gross profit related to the approval of a change order on a road construction project in the Middle East. The change order resulted in an extension of the contract terms and increased the total contract value.

Non-strategic Business

During the three and nine months ended September 30, 2016, we recognized unfavorable changes in estimates of losses on a power project of $86 million and $112 million, respectively, primarily due to an increase in forecast costs to complete the project driven by subcontractor cost increases from poor subcontractor productivity, resulting schedule delays and changes in the project execution strategy. Included in the reserve for estimated losses on uncompleted contracts, which is a component of "other current liabilities" on our condensed consolidated financial statements, is $35 million and $47 million as of September 30, 2016 and December 31, 2015, respectively, related to this project. The project has a contract value of $572 million and was approximately 85% complete as of September 30, 2016. We expect to complete this power project in the first half of 2017. Our estimates of revenues and costs at completion have been, and may continue to be, impacted by our performance, the performance of our subcontractors, and the U.S. labor market. Our estimated loss at completion as of September 30, 2016 represents our best estimate based on current information. Actual results could differ from the estimates we have used to account for this project as of September 30, 2016. During the three and nine months ended September 30, 2015, there were no significant changes in our estimates of losses on projects being executed within this business segment.

Note 3. Acquisitions, Dispositions and Other Transactions

During the nine months ended September 30, 2016, we acquired several businesses. In accordance with FASB Accounting Standards Codification ("ASC") Topic 805, Business Combinations, we accounted for these transactions using the acquisition method. We conducted external and internal valuations of certain acquired assets and liabilities for inclusion in our balance sheet as of the date of acquisition. Assets that would not normally be recorded in ordinary operations (i.e., customer relationships and other intangibles) were recorded at their estimated fair values. The excess of preliminary purchase price over the estimated fair values of the net assets acquired was recorded as goodwill. We expect to complete the purchase price allocation during the 12-month period following the acquisition date, in line with the acquisition method of accounting, during which time the value of the assets and liabilities, including any goodwill, may be revised as appropriate.

Honeywell Technology Solutions Inc. ("HTSI") Acquisition

On September 16, 2016, we acquired 100% of the outstanding common stock of HTSI from Honeywell International Inc. HTSI provides an array of mission-critical services and customized solutions throughout the world, primarily to U.S. government agencies. This acquisition provides KBR with complete lifecycle service capabilities, including high-end technical engineering and mission support, cyber security and logistics and equipment maintenance within our GS business segment.

The aggregate consideration paid for the acquisition was $300 million, less $25 million of initial working capital adjustments for net cash consideration of $275 million, all of which was funded by an advance on our Credit Agreement (as defined in Note 11 to our condensed consolidated financial statements). The final settlement of the working capital adjustments is expected in December of 2016. Accordingly, adjustments to the initial purchase accounting for the acquired net assets will likely be completed during the first quarter of 2017, as we obtain additional information regarding the facts and circumstances that existed as of the acquisition date.

We recognized goodwill of $124 million arising from the acquisition, which relates primarily to growth opportunities based on a broader service offering of the combined operations, including HTSI's specialized technical services and KBR's logistical expertise as well as expected cost synergies. Approximately $110 million of the goodwill is deductible for income tax purposes. This acquisition is reported within our GS business segment. We recognized acquisition-related costs of $7 million, which are included in "General and administrative expenses" in our condensed consolidated statement of operations for the nine months ended September 30, 2016.

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The following table summarizes the consideration paid for this acquisition and the fair value of the assets acquired and liabilities assumed as of the acquisition date.

Dollars in millions	
Fair value of total consideration transferred	$275
Recognized amounts of identifiable assets acquired and liabilities assumed:	
Trade receivables, net	29
CIE	93
Prepaids and other current assets	5
Total current assets	127
Property, plant and equipment, net	7
Intangible assets (a):	
Customer relationships	63
Backlog	7
Deferred income taxes	8
Total assets	212
Accounts payable	23
BIE	5
Other current liabilities	33
Total current liabilities	61
Goodwill	$124

(a) These intangible assets are amortized over their estimated useful lives up to 20 years.

HTSI’s results of operations have been included in our condensed consolidated statements of operations for periods subsequent to the acquisition on September16, 2016. The acquired HTSI businesses contributed $21 million of revenues and $2 million of gross profit for the period from September 16, 2016 through September 30, 2016. Due to the timing of the HTSI acquisition in September 2016 and the incomplete nature of the initial purchase accounting for the acquired net assets of HTSI, we have omitted certain disclosures for supplemental pro forma financial information. We intend to provide these disclosures in future filings. In connection with the transaction, we entered into a transition services agreement with the seller for a period of up to six months and primarily relates to payroll processing, human resources, information technology, real estate and other support services provided by the seller.

Wyle Inc. ("Wyle") Acquisition

On July 1, 2016, we acquired 100% of the equity interests of Wyle from its shareholders, including Court Square Capital Partners and certain officers of Wyle, pursuant to an agreement and plan of merger. Wyle delivers an array of custom solutions for customers in the U.S. Department of Defense, NASA and other federal agencies. Wyle's expertise includes systems and sustainment engineering, program and acquisition management, life science research, space medical operations, information technology and the testing and evaluation of aircraft, advanced systems and networks. The acquisition will combine KBR's strengths in international, large-scale government logistics and support operations with Wyle's specialized technical services, largely focused in the contiguous U.S.

The aggregate consideration paid for the acquisition was $600 million, including repayment of outstanding balances under Wyle's credit facility and other transaction expenses, plus $23 million of purchase price adjustments, which resulted in net cash consideration of $623 million. We funded the total cash paid with a $400 million advance on our Credit Agreement and available cash on-hand. See Note 11 to our condensed consolidated financial statements for information related to our Credit Agreement.

We recognized goodwill of $484 million arising from the acquisition, which relates primarily to growth opportunities based on a broader service offering of the combined operations, including Wyle's differentiated technical capabilities and KBR's international program management and logistics expertise. Additionally, goodwill relates to the existence of Wyle's skilled employee base and other expected synergies of the combined operations. Approximately $107 million of the goodwill is deductible for income tax purposes. Certain data necessary to complete the purchase price allocation is not yet available and primarily relates to final tax returns that provide the underlying tax basis of assets and liabilities. This acquisition is reported within our GS business segment. We recognized acquisition related costs in "General and administrative expenses" in our condensed consolidated statement of operations of $3 million for the nine months ended September 30, 2016.

The following table summarizes the consideration paid for this acquisition and the fair value of the assets acquired and liabilities assumed as of the acquisition date.

Dollars in millions	
Fair value of total consideration transferred	$623
Recognized amounts of identifiable assets acquired and liabilities assumed:	
Cash	10
Trade receivables, net	47
CIE	98
Prepaids and other current assets	4
Total current assets	159
Property, plant and equipment, net	10
Intangible assets (a):	
Customer relationships	82
Trademarks/trade names	48
Backlog	11
Total assets	310
Accounts payable	59
Other current liabilities	47
Total current liabilities	106
Deferred income taxes	53
Other liabilities	12
Total liabilities	171
Goodwill	$484

(a) These intangible assets are amortized over their estimated useful lives up to 20 years with the exception of Trademarks/trade names which have an indefinite life.

Wyle’s results of operations have been included in our condensed consolidated statements of operations for periods subsequent to the acquisition on July 1, 2016. The acquired Wyle businesses contributed $177 million of revenues and $12 million of gross profit for the period from July 1, 2016 through September 30, 2016.

The following supplemental pro forma results of operations assume that Wyle had been acquired as of January 1, 2015. The supplemental pro forma financial information was prepared based on the historical financial information of Wyle and has been adjusted to give effect to pro forma adjustments that are both directly attributable to the transaction and factually supportable. The pro forma amounts reflect certain adjustments to amortization expense and interest expense associated with the portion of the purchase price funded by a $400 million advance on our Credit Agreement.

The pro forma amounts also reflect adjustments to the 2016 results to exclude acquisition related costs as they are nonrecurring and directly attributable to the transaction.

The supplemental pro forma financial information presented below does not include any anticipated cost savings or expected realization of other synergies associated with the transaction. Accordingly, this supplemental pro forma financial information is

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presented for informational purposes only and is not necessarily indicative of what the actual results of operations of the combined company would have been had the acquisition occurred on January 1, 2015, nor is it indicative of future results of operations.

	Three Months Ended September 30,		Nine Months Ended September 30,	
Dollars in millions	2016	2015	2016	2015
Revenue	1,072	1,425	3,508	4,680
Net income (loss) attributable to KBR	(62)	60	37	180
Diluted earnings per share	(0.43)	0.42	0.26	1.25

Chematur Subsidiaries Acquisition

On January 11, 2016, we acquired 100% of the outstanding common stock of three subsidiaries of Connell Chemical Industry LLC (through its subsidiary, Chematur Technologies AB): Plinke GmbH ("Plinke"), Weatherly Inc., ("Weatherly") and Chematur Ecoplanning Oy ("Ecoplanning"). Plinke specializes in proprietary technology and specialist equipment for the purification and concentration of inorganic acids used or produced in hydrocarbon processing facilities. Weatherly provides nitric acid and ammonium nitrate proprietary technologies and services to the fertilizer market. Ecoplanning offers proprietary evaporation and crystallization technologies and specialist equipment for weak acid and base solutions. As a result of this acquisition, we can expand our technology and consulting solutions into new markets while leveraging KBR's global sales and EPC capabilities.

The aggregate consideration paid for the acquisition was $25 million, less $3 million of acquired cash and other adjustments resulting in net cash consideration of $23 million. The consideration paid included an escrow of $5 million that secures the indemnification obligations of the seller and other contingent obligations related to the operation of the business.

We recognized goodwill of $22 million arising from the acquisition, which relates primarily to future growth opportunities to extend the acquired technologies outside North America to new customers and in revamping units of the existing customer base globally. None of the goodwill is deductible for income tax purposes. The purchase price allocation is substantially complete with the exception of final tax returns that provide the underlying tax basis of assets and liabilities. This acquisition is reported within our T&C business segment. We recognized acquisition related costs in "General and administrative expenses" on our condensed consolidated statement of operations of $1 million for the nine months ended September 30, 2016.

The following table summarizes the consideration paid for this acquisition and the fair value of the assets acquired and liabilities assumed as of the acquisition date and subsequent working capital adjustments.

Dollars in millions	
Fair value of total consideration transferred	$25
Recognized amounts of identifiable assets acquired and liabilities assumed:	
Cash	2
Trade receivables, net	5
CIE	8
Prepaids and other current assets	8
Total current assets	23
Intangible assets (a):	
Developed technology	10
Customer relationships	7
Trademarks/trade names	2
Other assets	1
Total assets	43
Accounts payable	2
BIE	13
Other current liabilities	8
Total current liabilities	23
Deferred income taxes	11
Other liabilities	6
Total liabilities	40
Goodwill	$22

(a) These intangible assets are amortized over their estimated useful lives up to 20 years with the exception of Trademarks/trade names which have an indefinite life.

As a result of this acquisition, $4 million and $18 million of revenues for the three and nine months ended September 30, 2016, respectively, and a gross loss of less than $1 million for the three months ended September 30, 2016 and break even for the nine months ended September 30, 2016, respectively, were included in our condensed consolidated statements of operations.

New Investments

In February 2016, we executed agreements to establish a new joint venture within our GS business segment. See Note 9 to our condensed consolidated financial statements for information related to the establishment of this new joint venture.

Note 4. Cash and Equivalents

We consider all highly liquid investments with an original maturity of three months or less to be cash equivalents. Cash and equivalents include cash balances held by our wholly owned subsidiaries as well as cash held by joint ventures that we consolidate. Joint venture cash balances are limited to joint venture activities and are not available for other projects, general cash needs or distribution to us without approval of the board of directors of the respective joint ventures. We expect to use joint venture cash for project costs and distributions of earnings related to joint venture operations. However, some of the earnings distributions may be paid to other KBR entities where the cash can be used for general corporate needs.

The components of our cash and equivalents balance are as follows:

Dollars in millions	September 30, 2016 International (a)	Domestic (b)	Total
Operating cash and equivalents	$129	$ 190	$319
Short-term investments (c)	193	5	198
Cash and equivalents held in joint ventures	47	5	52
Total	$369	$ 200	$569

Dollars in millions	December 31, 2015 International (a)	Domestic (b)	Total
Operating cash and equivalents	$177	$ 253	$430
Short-term investments (c)	293	107	400
Cash and equivalents held in joint ventures	49	4	53
Total	$519	$ 364	$883

(a) Includes deposits held in non-U.S. operating accounts.
(b) Includes U.S. dollar and foreign currency deposits held in operating accounts that constitute onshore cash for tax purposes but may reside either in the U.S. or in a foreign country.
(c) Includes time deposits, money market funds, and other highly liquid short-term investments.

Note 5. Accounts Receivable

The components of our accounts receivable, net of allowance for doubtful accounts balance are as follows:

Dollars in millions	September 30, 2016 Retainage	Trade & Other	Total
Technology & Consulting	$3	$ 55	$58
Engineering & Construction	67	368	435
Government Services	5	188	193
Other	—	3	3
Subtotal	75	614	689
Non-strategic Business	5	14	19
Total	$80	$ 628	$708

Dollars in millions	December 31, 2015 Retainage	Trade & Other	Total
Technology & Consulting	$—	$ 70	$70
Engineering & Construction	51	402	453
Government Services	2	75	77
Other	—	2	2
Subtotal	53	549	602
Non-strategic Business	9	17	26

Total	$62	$566	$628

Note 6. Costs and Estimated Earnings in Excess of Billings on Uncompleted Contracts and Billings in Excess of Costs and Estimated Earnings on Uncompleted Contracts

Our CIE balances by business segment are as follows:

Dollars in millions	September 30, 2016	December 31, 2015
Technology & Consulting	$ 25	$ 42
Engineering & Construction	123	114
Government Services	242	68
Subtotal	390	224
Non-strategic Business	—	—
Total	$ 390	$ 224

Our BIE balances by business segment are as follows:

Dollars in millions	September 30, 2016	December 31, 2015
Technology & Consulting	$ 52	$ 72
Engineering & Construction	347	307
Government Services	67	69
Subtotal	466	448
Non-strategic Business	71	61
Total	$ 537	$ 509

Unapproved change orders and claims

The amounts of unapproved change orders and claims included in determining the profit or loss on contracts are as follows:

Dollars in millions	2016	2015
Amounts included in project estimates-at-completion at January 1,	$46	$31
Additions	12	48
Approved change orders	(32)	(40)
Adjustment due to disposition of business	—	(6)
Amounts included in project estimates-at-completion at September 30,	$26	$33
Amounts recorded in revenues on a percentage-of-completion basis at September 30,	$24	$32

The table above excludes unapproved change orders and claims related to our unconsolidated affiliates. Our proportionate share of unapproved change orders and claims was $65 million as of September 30, 2016 and $59 million as of September 30, 2015 on a project in our E&C business segment.

Liquidated damages

Some of our engineering and construction contracts have schedule dates and performance obligations that if not met could subject us to penalties for liquidated damages. These generally relate to specified activities that must be completed by a set contractual date or by achievement of a specified level of output or throughput. Each contract defines the conditions under which a customer may make a claim for liquidated damages. However, in some instances, liquidated damages are not asserted by the customer, but the potential to do so is used in negotiating or settling claims and closing out the contract. Any accrued liquidated damages are recognized as a reduction in revenues in our condensed consolidated statements of operations.

It is possible that liquidated damages related to several projects totaling $5 million and $6 million at September 30, 2016 and December 31, 2015, respectively, could be incurred if the projects are completed as currently forecasted. However, based upon our evaluation of our performance, we have concluded these liquidated damages are not probable and therefore, they have not been recognized.

Note 7. Claims and Accounts Receivable

The components of our claims and accounts receivable account balance not expected to be collected within the next 12 months are as follows:

Dollars in millions	September 30, 2016	December 31, 2015
Engineering & Construction	$ 400	$ 400
Government Services	128	126
Total	$ 528	$ 526

Our E&C business segment's claims and accounts receivable is related to our EPC 1 arbitration. See Note 14 to our condensed consolidated financial statements under PEMEX and PEP Arbitration for further discussion.

Our GS business segment's claims and accounts receivable reflects claims filed with the U.S. government related to payments not yet received for cost incurred under various U.S. government contracts. These claims relate to disputed costs or contracts where our costs have exceeded the U.S. government's funded value on the task order. Included in the amount above is $83 million as of September 30, 2016 and December 31, 2015, related to Form 1s issued by the U.S. government questioning or objecting to costs billed to them. See Note 13 of our condensed consolidated financial statements for additional discussions. The amount above also includes $45 million and $43 million as of September 30, 2016 and December 31, 2015, respectively, related to contracts where our costs have exceeded the U.S. government's funded values on the underlying task orders or task orders where the U.S. government has not authorized us to bill. We believe such disputed costs will be resolved in our favor at which time the U.S. government will be required to obligate funds from appropriations for the year in which resolution occurs.

Note 8. Restructuring

In connection with our long-term strategic reorganization, we announced that beginning in the fourth quarter of 2014 we would undertake a restructuring, which would include actions such as reducing the amount of real estate we utilized and significantly reducing our workforce. There were additional actions undertaken in 2015 and 2016, including staff reductions to support current business levels. The employees affected by these reductions are eligible for separation benefits upon their termination and the dates have occurred or are expected to occur through 2017. The table below provides a rollforward of one-time charges associated with employee terminations based on the fair value of the termination benefits. These amounts are included in "other current liabilities" on our condensed consolidated balance sheets.

Dollars in millions	Severance Accrual
Balance at December 31, 2015	$ 19
Charges	15
Payments	(21)
Balance at September 30, 2016	$ 13
Balance at December 31, 2014	$ 21
Charges	11
Payments	(23)
Balance at September 30, 2015	$ 9

Note 9. Equity Method Investments and Variable Interest Entities

We conduct some of our operations through joint ventures which operate through partnership, corporation, undivided interest and other business forms and are principally accounted for using the equity method of accounting. Additionally, the majority of our joint ventures are VIEs.

The following table presents a rollforward of our equity in and advances to unconsolidated affiliates:

Dollars in millions	September 30, 2016	December 31, 2015
Beginning balance	$ 281	$ 151
Equity in earnings of unconsolidated affiliates	81	149
Distribution of earnings of unconsolidated affiliates (a)	(43)	(92)
Advances (receipts)	3	(10)
Investments (b)	5	80
Foreign currency translation adjustments	(1)	(9)
Other	(7)	1
Balance before reclassification	$ 319	$ 270
Reclassification of excess distributions (a)	12	16
Recognition of excess distributions (a)	(4)	(5)
Ending balance	$ 327	$ 281

(a) We received cash dividends in excess of the carrying value of one of our investments. We have no obligation to return any portion of the cash dividends received. We recorded the excess dividend amount as "deferred income from unconsolidated affiliates" on our condensed consolidated balance sheets and recognize these dividends as earnings are generated by the investment.

(b) In 2015, investments included a $58 million investment in the Brown & Root Industrial Services joint venture, a $24 million investment in EPIC Piping LLC ("EPIC") joint venture, and the disposition of a joint venture included in the sale of the Building Group.

Equity Method Investments

New Investments

U.K. Military Flying Training System ("UKMFTS") project. In February 2016, Affinity Flying Training Services Ltd. ("Affinity"), a joint venture between KBR and Elbit Systems, was awarded a service contract by a third party to procure, operate and maintain aircraft, and aircraft-related assets over an 18-year contract period, in support of the UKMFTS project. KBR owns a 50% interest in Affinity. In addition, KBR owns a 50% interest in the two joint ventures, Affinity Capital Works and Affinity Flying Services, which provide procurement, operations and management support services under subcontracts with Affinity. The remaining 50% interest in these entities is held by Elbit Systems. KBR has provided its proportionate share of certain limited financial and performance guarantees in support of the partners' contractual obligations. The three project-related entities are VIEs; however, KBR is not the primary beneficiary of any of these entities. We account for KBR's interests in each entity using the equity method of accounting within our GS business segment. The project is funded through KBR and Elbit Systems provided equity, subordinated debt and non-recourse third party commercial bank debt. During the first quarter of 2016, under the terms of the subordinated debt agreement between the partners and Affinity, we advanced our proportionate share, or $14 million, to meet initial working capital needs of the venture. We expect repayment on the advance and the associated interest over the term of the project. The amount is included in the "equity in and advances" balance on our condensed consolidated balance sheets as of September 30, 2016 and in "(Advances to) payments from unconsolidated affiliates, net" in our condensed consolidated statement of cash flows for the nine months ended September 30, 2016.

Unconsolidated Variable Interest Entities

Generally, our maximum exposure to loss is limited to our equity investment in the joint venture and any amounts payable to us for services we provided to the joint venture reduced for any unearned revenues on the projects. On the Affinity joint venture, our maximum exposure to loss is limited to our proportionate share of any amounts required to fund future losses incurred by those entities under their respective contracts with the project company. On the Aspire Defence project, in addition to the maximum exposure to loss indicated in the table below, we have exposure to any losses incurred by the construction or operating joint ventures under their respective subcontract arrangements with the project company. Our exposure is, however, limited to our equity participation in these entities. The Ichthys LNG joint venture executes a project that has a lump sum component; in addition to the maximum exposure to loss indicated in the table below, we have an exposure to losses to the extent of our ownership percentage in the joint venture if the project exceeds the lump sum component. Our maximum exposure to loss on the EBIC Ammonia plant reflects our 65% ownership of the development corporation which owns 25% of the company that consolidates the ammonia plant. We continue to monitor our investment in this joint venture as the profitability of its operations has been impacted by the challenges related to the availability of natural gas feedstock in Egypt.

The following summarizes the total assets and total liabilities as reflected in our condensed consolidated balance sheets as well as our maximum exposure to losses related to our unconsolidated VIEs in which we have a significant variable interest but are not the primary beneficiary.

	September 30, 2016		
Dollars in millions	Total assets	Total liabilities	Maximum exposure to loss
Affinity project	$12	$ 3	$ 12
Aspire Defence project	$14	$ 116	$ 14
Ichthys LNG project	$125	$ 46	$ 125
U.K. Road projects	$31	$ 10	$ 31
EBIC Ammonia plant (65% interest)	$34	$ 2	$ 21

	December 31, 2015		
Dollars in millions	Total assets	Total liabilities	Maximum exposure to loss
Aspire Defence project	$17	$ 121	$ 17
Ichthys LNG project	$87	$ 63	$ 87
U.K. Road projects	$34	$ 11	$ 34
EBIC Ammonia plant (65% interest)	$36	$ 2	$ 22

Related Party Transactions

We often provide engineering, construction management and other subcontractor services to our joint ventures and our revenues include amounts related to these services. For the nine months ended September 30, 2016 and 2015, our revenues included $179 million and $223 million, respectively, related to the services we provided to our joint ventures, primarily within our E&C business segment. Under the terms of our transition services agreement ("TSA") with Brown & Root Industrial Services joint venture, we collect cash from customers and make payments to vendors and employees on behalf of the joint venture. For the nine months ended September 30, 2016, we incurred approximately $13 million of reimbursable costs under the TSA. In addition, in 2015, we entered into an alliance agreement with our EPIC joint venture to provide certain pipe fabrication services to KBR. For the nine months ended September 30, 2016, EPIC performed $22 million of services to KBR under the agreement.

Amounts included in our condensed consolidated balance sheets related to services we provided to our unconsolidated joint ventures as of September 30, 2016 and December 31, 2015 are as follows:

Dollars in millions	September 30, 2016	December 31, 2015
Accounts receivable, net of allowance for doubtful accounts (a)	$ 30	$ 7
Costs and estimated earnings in excess of billings on uncompleted contracts (b)	$ 1	$ 5
Billings in excess of costs and estimated earnings on uncompleted contracts (b)	$ 51	$ 55
Accounts payable (c)	$ —	$ 9

(a) Includes a $19 million net receivable from the Brown & Root Industrial Services joint venture at September 30, 2016.
(b) Reflects CIE and BIE primarily related to joint ventures within our E&C business segment as discussed above.
(c) Reflects a $9 million net payable to the Brown & Root Industrial Services joint venture at December 31, 2015.

Consolidated Variable Interest Entities

We consolidate VIEs if we determine we are the primary beneficiary of the project entity because we control the activities that most significantly impact the economic performance of the entity. The following is a summary of the significant VIEs where we are the primary beneficiary:

Dollars in millions	September 30, 2016	
	Total assets	Total liabilities
Gorgon LNG project	$ 29	$ 62
Escravos Gas-to-Liquids project	$ 16	$ 27
Fasttrax Limited project	$ 62	$ 57