KAISER ALUMINUM CORP
Form 10-Q
November 14, 2007

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

Form 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2007

Commission file number 0-52105

KAISER ALUMINUM CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	**94-3030279**
(State of Incorporation)	*(I.R.S. Employer Identification No.)*
27422 PORTOLA PARKWAY, SUITE 350, FOOTHILL RANCH, CALIFORNIA	**92610-2831**
(Address of principal executive offices)	*(Zip Code)*

Registrant s telephone number, including area code:
(949) 614-1740

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, and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

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

Large accelerated filer o Accelerated filer o Non-accelerated filer þ

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

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes þ No o

As of October 31, 2007, there were 20,581,313 shares of the Common Stock of the registrant outstanding.

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES

PART I FINANCIAL INFORMATION

Item 1. ***Financial Statements***

CONSOLIDATED BALANCE SHEETS

	September 30, 2007	December 31, 2006
	(Unaudited) (In millions of dollars, except share amounts)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 101.4	$ 50.0
Receivables:		
Trade, less allowance for doubtful receivables of $2.0 at both September 30, 2007 and December 31, 2006	112.1	98.4
Due from affiliate		1.3
Other	4.8	6.3
Inventories	193.7	188.1
Prepaid expenses and other current assets	13.8	40.8
Total current assets	425.8	384.9
Investment in and advances to unconsolidated affiliate	43.9	18.6
Property, plant, and equipment net	205.9	170.3
Net assets in respect of VEBAs	90.3	40.7
Other assets	39.6	40.9
Total	$ 805.5	$ 655.4
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 65.3	$ 73.2
Accrued salaries, wages, and related expenses	34.6	39.4
Other accrued liabilities	34.0	47.6
Payable to affiliate	19.8	16.2
Total current liabilities	153.7	176.4
Long-term liabilities	68.2	58.3
Long-term debt	50.0	50.0
	271.9	284.7
Commitments and contingencies		
Stockholders equity:		

Common stock, par value $.01, 45,000,000 shares authorized; 20,588,477 shares issued and 20,581,313 shares outstanding at September 30, 2007; 20,525,660 shares issued and outstanding at December 31, 2006		.2		.2
Additional capital		565.6		487.5
Retained earnings		95.4		26.2
Common stock owned by Union VEBA subject to transfer restrictions, at reorganization value, 5,472,665 shares and 6,291,945 shares at September 30, 2007 and December 31, 2006, respectively		(131.4)		(151.1)
Accumulated other comprehensive income		4.4		7.9
Treasury stock, at cost, 7,164 shares at September 30, 2007		(.6)		
Total stockholders equity		533.6		370.7
Total	$	805.5	$	655.4

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

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES

STATEMENTS OF CONSOLIDATED INCOME

	Quarter Ended September 30, 2007	Three Months Ended September 30, 2006 Period from July 1, 2006 through September 30, 2006	Predecessor July 1, 2006	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006 Period from July 1, 2006 through September 30, 2006	Predecessor Period from January 1, 2006 to July 1, 2006
	(Unaudited) (In millions of dollars, except share and per share amounts)					
Net sales	$ 366.7	$ 331.4	$	$ 1,144.0	$ 331.4	$ 689.8
Costs and expenses:						
Cost of products sold	303.3	291.8		954.4	291.8	596.4
Depreciation and amortization	3.0	2.8		8.3	2.8	9.8
Selling, administrative, research and development, and general	17.8	18.0		56.0	18.0	30.3
Other operating (benefits) charges, net	(1.4)	(2.9)		(13.7)	(2.9)	.9
Total costs and expenses	322.7	309.7		1,005.0	309.7	637.4
Operating income	44.0	21.7		139.0	21.7	52.4
Other income (expense):						
Interest expense (excluding unrecorded contractual interest expense of $47.4 for the period from January 1, 2006 to July 1, 2006)	(1.0)			(2.2)		(.8)
Reorganization items			3,105.3			3,090.3
Other net	1.8	.9		4.1	.9	1.2
Income before income taxes and discontinued operations	44.8	22.6	3,105.3	140.9	22.6	3,143.1
Provision for income taxes	(20.0)	(8.3)		(64.3)	(8.3)	(6.2)
Income from continuing operations	24.8	14.3	3,105.3	76.6	14.3	3,136.9
Income from discontinued operations, net of income						4.3

taxes												
Net income	$	24.8	$	14.3	$	3,105.3	$	76.6	$	14.3	$	3,141.2
Earnings per share Basic:												
Income from continuing operations	$	1.24	$	.72	$	38.98	$	3.83	$	.72	$	39.37
Income from discontinued operations	$		$		$		$		$		$	.05
Net income per share	$	1.24	$	.72	$	38.98	$	3.83	$	.72	$	39.42
Earnings per share Diluted (same as basic for Predecessor):												
Income from continuing operations	$	1.22	$	.72			$	3.77	$	.72		
Income from discontinued operations	$		$				$		$			
Net income per share	$	1.22	$	.72			$	3.77	$	.72		
Weighted average number of common shares outstanding (000):												
Basic		20,026		20,002		79,672		20,010		20,002		79,672
Diluted		20,326		20,029		79,672		20,291		20,029		79,672

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

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES

STATEMENTS OF CONSOLIDATED STOCKHOLDERS EQUITY AND COMPREHENSIVE INCOME

	Common Stock	Additional Capital	Retained Earnings (Deficit)	Common Stock Owned by Union VEBA Subject to Transfer Restrictions	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total
			(Unaudited) (In millions of dollars, except share amounts)				
BALANCE, December 31, 2005- Predecessor	$ .8	$ 538.0	$ (3,671.2)	$	$ (8.8)	$	(3,141.2)
Net income (same as Comprehensive income) Predecessor			35.9				35.9
BALANCE, June 30, 2006-Predecessor	.8	538.0	(3,635.3)		(8.8)		(3,105.3)
Cancellation of Predecessor common stock	(.8)	.8					
Issuance of Successor common stock (20,000,000 shares) to creditors	.2	480.2					480.4
Common stock owned by Union VEBA subject to transfer restrictions, at reorganization value, 6,291,945 shares				(151.1)			(151.1)
Plan and fresh start adjustments		(538.8)	3,635.3		8.8		3,105.3
BALANCE, July 1, 2006	.2	480.2		(151.1)			329.3
Net income			26.2				26.2
Benefit plan adjustments not recognized in earnings					7.9		7.9
Comprehensive income							34.1
		.2					.2

Issuance of 4,273 shares of common stock to directors in lieu of annual retainer fees							
Recognition of pre-emergence tax benefits in accordance with fresh start accounting		3.3					3.3
Amortization of unearned equity compensation		3.8					3.8
BALANCE, December 31, 2006	$ .2	$ 487.5	$ 26.2	$ (151.1)	$ 7.9	$	$ 370.7
Net income			76.6				76.6
Foreign currency translation adjustment					(3.5)		(3.5)
Comprehensive income							73.1
Removal of transfer restrictions on 819,280 shares of common stock owned by Union VEBA, net of income taxes of $5.0		23.0		19.7			42.7
Recognition of pre-emergence tax benefits in accordance with fresh start accounting (including tax benefits of $15.9 for the quarter ended September 30, 2007)		48.1					48.1
Equity compensation recognized by an unconsolidated affiliate		.2					.2
Repurchase of 3,862 shares of common stock from former employee and 3,302 shares of common stock from employees on vesting of restricted stock						(.6)	(.6)
Issuance of 3,877 shares of common stock to directors in lieu of annual retainer fees		.3					.3
Common stock cash dividends			(7.4)				(7.4)
Amortization of unearned equity compensation (including unearned equity compensation of $2.3 for the quarter ended September 30, 2007)		6.5					6.5
BALANCE, September 30, 2007	$ .2	$ 565.6	$ 95.4	$ (131.4)	$ 4.4	$ (.6)	$ 533.6

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

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES

STATEMENTS OF CONSOLIDATED CASH FLOWS

	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006: Period from July 1, 2006 to September 30, 2006	Nine Months Ended September 30, 2006: Predecessor Period from Jan 1, 2006 to July 1, 2006
	(Unaudited) (In millions of dollars)		
Cash flows from operating activities:			
Net income	$ 76.6	$ 14.3	$ 3,141.2
Less income from discontinued operations			4.3
Income from continuing operations	76.6	14.3	3,136.9
Adjustments to reconcile income from continuing operations to net cash provided (used) by continuing operations:			
Recognition of pre-emergence tax benefits in accordance with fresh start accounting	48.1		
Depreciation and amortization (including deferred financing costs of $.4, $.1 and $.9, respectively)	8.7	2.9	10.7
Deferred income taxes	.1		(.7)
Non-cash equity compensation	6.8	2.3	
Gain on discharge of pre-petition obligations and fresh start adjustments			(3,110.3)
Payments pursuant to plan of reorganization			(25.3)
Net non-cash (benefits) charges in other operating charges and LIFO charges (benefits)	(13.1)	(3.3)	21.7
Gain on sale of real estate			(1.6)
Equity in income of unconsolidated affiliate, net of distributions	(25.1)	(2.1)	(10.1)
Changes in assets and liabilities:			
Decrease (increase) in trade and other receivables	(10.9)	4.3	(18.3)
Decrease (increase) in inventories, excluding LIFO adjustments	2.6	(6.0)	(29.5)
Decrease (increase) in prepaid expenses and other current assets	26.7	6.0	(14.5)
(Decrease) increase in accounts payable	(8.8)	7.3	5.7
(Decrease) increase in other accrued liabilities	(15.0)	(8.6)	4.7
(Decrease) increase in payable to affiliate	3.6	(13.6)	18.2
(Decrease) increase in accrued income taxes	(.5)	6.3	.2
Net cash impact of changes in long-term assets and liabilities	(10.5)	(6.9)	(8.0)
Net cash provided by discontinued operations			8.5
Other	.1		
Net cash provided (used) by operating activities	89.4	2.9	(11.70)

Cash flows from investing activities:						
Decrease in restricted cash		9.4				
Capital expenditures, net of accounts payable of $.9 in 2007 and $1.6 in both the period from July 1, 2006 to September 30, 2006 and the period from January 1, 2006 to July 1, 2006		(43.1)		(11.6)		(28.1)
Net proceeds from sale of real estate						1.0
Net cash used by investing activities		(33.7)		(11.6)		(27.1)
Cash flows from financing activities:						
Borrowings under Term Loan Facility				50.0		
Financing costs				(.6)		(.2)
Repurchase of common stock		(.6)				
Cash dividend paid to shareholders		(3.7)				
Other						1.5
Net cash (used) provided by financing activities		(4.3)		49.4		1.3
Net increase (decrease) in cash and cash equivalents during the period		51.4		40.7		(37.5)
Cash and cash equivalents at beginning of period		50.0		12.0		49.5
Cash and cash equivalents at end of period	$	101.4	$	52.7	$	12.0
Supplemental disclosure of cash flow information:						
Interest paid, net of capitalized interest of $2.4, $.6 and $1.0, respectively	$	2.3	$		$	
Income taxes paid	$	2.2	$	.4	$	1.2
Supplemental disclosure of non-cash transactions:						
Removal of transfer restrictions on common stock owned by Union VEBA (Note 9)	$	47.7	$		$	
Cash dividend declared and unpaid (Note 13)	$	3.7	$		$	

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

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS
(In millions of dollars, except share and per share amounts)
(Unaudited)

The accompanying financial statements include the financial statements of Kaiser Aluminum Corporation(the Company or Kaiser) both before (the Predecessor) and after (the Successor) its emergence from chapter 11 bankruptcy in July 2006. Financial information related to the Company after emergence is generally referred to throughout this Report as Successor information. Information of the Company before emergence is generally referred to as Predecessor information. The financial information of the Successor is not comparable to that of the Predecessor given the impacts of the Plan (as defined below), implementation of fresh start reporting and other factors as more fully described below.

The Notes to Interim Consolidated Financial Statements are grouped into two categories: (1) those primarily affecting the Successor (Notes 1 through 14) and (2) those primarily affecting the Predecessor (Notes 15 through 18).

SUCCESSOR

1. Summary of Significant Accounting Policies

This Report should be read in conjunction with the Company s Annual Report on Form 10-K for the year ended December 31, 2006.

Principles of Consolidation and Basis of Presentation. The consolidated financial statements include the statements of the Company and its wholly owned subsidiaries. Investments in 50%-or-less-owned entities are accounted for primarily by the equity method. The only such affiliate for the periods covered by this report was Anglesey Aluminium Limited (Anglesey). Intercompany balances and transactions are eliminated.

The Company s emergence from chapter 11 and adoption of fresh start accounting resulted in a new reporting entity for accounting purposes. Although the Company emerged from chapter 11 bankruptcy on July 6, 2006 (Effective Date), the Company adopted fresh start accounting as required by the American Institute of Certified Professional Accountants Statement of Position 90-7 (SOP 90-7), *Financial Reporting by Entities in Reorganization Under the Bankruptcy Code*, effective as of the beginning of business on July 1, 2006. As such, it was assumed that the emergence was completed instantaneously at the beginning of business on July 1, 2006 such that all operating activities during the period from July 1, 2006 through December 31, 2006 are reported as applying to the Successor. The Company believes that this is a reasonable presentation as there were no material transactions between July 1, 2006 and July 6, 2006 that were not related to Kaiser s Second Amended Plan of Reorganization (the Plan). Due to the implementation of the Plan, the application of fresh start accounting and changes in accounting policies and procedures, the financial statements of the Successor are not comparable to those of the Predecessor.

The accompanying unaudited interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and the rules and regulations of the Securities and Exchange Commission. Accordingly, these financial statements do not include all of the disclosures required by GAAP for complete financial statements. In the opinion of management, the unaudited interim consolidated financial statements furnished herein include all adjustments, all of which are of a normal recurring nature unless otherwise noted, necessary for a fair statement of the results for the interim periods presented.

Use of Estimates and Assumptions. The preparation of financial statements in accordance with GAAP requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities known to exist as of the date the financial statements are published, and the reported amounts of revenues and expenses during the reporting period. Uncertainties with respect to such estimates and assumptions are inherent in the preparation of the Company s consolidated financial statements; accordingly, it is possible that the actual results could differ from these estimates and assumptions, which could have a material effect on the reported amounts of the Company s consolidated financial position and results of operation.

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Operating results for the nine months ended September 30, 2007 are not necessarily indicative of the results that may be expected for the year ended December 31, 2007.

Earnings per Share. Basic earnings per share is computed by dividing earnings by the weighted average number of common shares outstanding during the applicable period. The shares owned by a voluntary employee beneficiary association (VEBA) for the benefit of certain union retirees, their surviving spouses and eligible dependents (the Union VEBA) that are subject to transfer restrictions, while treated in the Consolidated Balance Sheets as being similar to treasury stock (i.e., as a reduction in Stockholders equity), are included in the computation of basic shares outstanding in the Statement of Consolidated Income because such shares were irrevocably issued and have full dividend and voting rights.

Diluted earnings per share is computed by dividing earnings by the sum of (a) the weighted average number of common shares outstanding during the period and (b) the dilutive effect of potential common share equivalents consisting of non-vested common shares, restricted stock units and stock options (see Note 13).

Restricted Cash. The Company is required to keep certain amounts on deposit relating to workers compensation, collateral for certain letters of credit and other agreements totaling $15.8 and $25.2 at September 30, 2007 and December 31, 2006, respectively. On July 17, 2007, the State of Washington reduced the amount the Company is required to have on deposit with the State by approximately $9.5. The remaining $7.7 on deposit with the State of Washington represents the deposit required to fund existing workers compensation claims. Of the restricted cash balance at September 30, 2007 and December 31, 2006, $14.4 and $23.5, respectively, is considered long term and is included in Other assets on the balance sheet.

New Accounting Pronouncements. Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* (SFAS No. 157) was issued in September 2006 to increase consistency and comparability in fair value measurements and to expand their disclosures. The new standard includes a definition of fair value as well as a framework for measuring fair value. The provisions of this standard apply to other accounting pronouncements that require or permit fair value measurements. The standard is effective for fiscal periods beginning after November 15, 2007 and should be applied prospectively, except for certain financial instruments where it must be applied retrospectively as a cumulative-effect adjustment to the balance of opening retained earnings in the year of adoption. The Company is still evaluating SFAS No. 157 but does not currently anticipate that the adoption of this standard will have a material impact on its financial statements.

Statement of Financial Accounting Standards No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statement No. 115* (SFAS No. 159) was issued in February 2007 and will become effective for the Company on January 1, 2008. SFAS No. 159 permits entities the option to measure many financial instruments and certain other items at fair value. Unrealized gains and losses in respect of assets and liabilities for which the fair value option has been elected will be reported in earnings. Selection of the fair value option is irrevocable and can be applied on a partial basis, i.e., to some but not all similar financial assets or liabilities. The Company is currently evaluating what impact, if any, this pronouncement will have on its consolidated financial statements.

Significant accounting policies of the Predecessor are discussed in Note 15.

2. Inventories

Inventories are stated at the lower of cost or market value. Finished products, work in process and raw material inventories are stated on the last-in, first-out (LIFO) basis. Other inventories, principally operating supplies and repair and maintenance parts, are stated at average cost. Inventory costs consist of material, labor and manufacturing overhead, including depreciation. Abnormal costs, such as idle facility expenses, freight, handling costs and spoilage, are accounted for as current period charges.

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Inventories consist of the following:

	September 30, 2007	December 31, 2006
Fabricated products		
Finished products	$ 60.1	$ 61.1
Work in process	79.6	72.8
Raw materials	41.2	42.0
Operating supplies and repairs and maintenance parts	12.7	12.1
	193.6	188.0
Commodities Primary aluminum	.1	.1
	$ 193.7	$ 188.1

As stated above, the Company determines cost for substantially all of its product inventories on a LIFO basis. All Predecessor LIFO layers were eliminated in connection with the application of fresh start accounting. The Successor applies LIFO differently than the Predecessor in that the Successor views each quarter on a standalone year to date basis for computing LIFO, whereas the Predecessor recorded LIFO amounts with a view to the entire fiscal year which, with certain exceptions, tended to result in LIFO charges being recorded in the fourth quarter or the second half of the year. The Company recorded a net non-cash LIFO benefit of approximately $10.2 and $8.2 during the quarter and nine month periods ended September 30, 2007, respectively. The Company recorded a non-cash LIFO benefit (charge) of approximately $(21.7) for the period from January 1, 2006 to July 1, 2006 and $3.3 for the period from July 1, 2006 through September 30, 2006. These amounts are primarily a result of changes in metal prices and, in 2007, changes in inventory volumes.

Pursuant to fresh start accounting, as more fully discussed in Note 2 of Notes to Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2006, all inventory amounts at the Effective Date were stated at fair market value. Raw materials and Operating supplies and repairs and maintenance parts were recorded at published market prices including any location premiums. Finished products and Work in process (WIP) were recorded at selling price less cost to sell, cost to complete and a reasonable apportionment of the profit margin associated with the selling and conversion efforts. As a result, as reported in Note 2 of Notes to Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2006, inventories were increased by approximately $48.9 at the Effective Date.

Given the recent strength in demand for many types of fabricated aluminum products and primary aluminum, the Company has a larger volume of raw materials, WIP and finished goods than is its historical average, and the price for such goods that was reflected in the opening inventory balance at the Effective Date, given the application of fresh start accounting, is higher than long term historical averages. As such, with the inevitable ebb and flow of business cycles, non-cash LIFO charges and potential lower of cost and market adjustments will result when inventory levels drop and/or margins compress. Such adjustments could be material to results in future periods.

3. Investment In and Advances To Unconsolidated Affiliate

The Company has a 49% ownership interest in Anglesey, which owns an aluminum smelter at Holyhead, Wales. The Company accounts for its 49% ownership in Anglesey using the equity method. The Company s equity in income before income taxes of Anglesey is treated as a reduction (increase) in Cost of products sold. The income tax effects of the Company s equity in income are included in the Company s income tax provision.

The nuclear plant that supplies power to Anglesey is currently slated for decommissioning in late 2010. For Anglesey to be able to operate past September 2009, when its current power contract expires, Anglesey will have to secure power at prices that make its operation viable. No assurances can be provided that Anglesey will be

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Continued)

successful in this regard. In addition, given the potential for future shutdown and related costs, Anglesey temporarily suspended dividends during the last half of 2006 and the first half of 2007 while it studied future cash requirements. Based on a review of cash available for future cash requirements, Anglesey removed the temporary suspension of dividends and declared a dividend in August 2007. The dividend in respect of the Company s ownership interests in the amount of $4.4 was received in August 2007 resulting in a reduction of Investment in unconsolidated affiliate. Dividends over the past five years have fluctuated substantially depending on various operational and market factors. During the last five years, cash dividends received were as follows: 2006 $11.8, 2005 $9.0, 2004 $4.5, 2003 $4.3 and 2002 $6.0. No assurance can be given that Anglesey will not suspend dividends again in the future.

The following table shows a summary of Anglesey s selected operating results for the quarter and nine months ended September 30, 2007 and 2006:

	Quarter Ended September 30, 2007	Quarter Ended September 30, 2006	Nine Months Ended September 30, 2007	Nine Months Ended September 30, Period from July 1, 2006 through September 30, 2006	Nine Months Ended September 30, Predecessor Period from January 1, 2006 to July 1, 2006
Net sales	$ 108.5	$ 103.1	$ 314.7	$ 103.1	$ 170.1
Gross profit	$ 23.7	$ 30.5	$ 73.9	$ 30.5	$ 38.0
Net income	$ 17.1	$ 21.5	$ 52.8	$ 21.5	$ 26.8
Company s equity income(1)	$ 9.7	$ 13.0	$ 29.7	$ 13.0	$ 11.0

(1) The Company s equity income differs from the summary net income due to equity method accounting adjustments and applying GAAP.

At September 30, 2007 and December 31, 2006, the receivables from Anglesey were none and $1.3, respectively.

As a result of fresh start accounting, the Company decreased its investment in Anglesey at the Effective Date by $11.6 (see Note 2 of Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2006). The $11.6 difference between the Company s share of Anglesey s equity and the investment amount reflected in the Company s balance sheet is being amortized (included in Cost of products sold) over the period from July 2006 to September 2009, the end of the current power contract. The non-cash amortization was approximately $.9 and $2.7 for the quarter and nine month periods ended September 30, 2007, respectively. At September 30, 2007, the remaining unamortized amount was $7.1.

In the nine months ended September 30, 2007, the Company recorded a $.2 charge for share-based equity compensation for employees of Anglesey who participate in the employee share savings plan of its parent (Rio Tinto). The $.2 has been recognized as a reduction in the equity in earnings of Anglesey for the nine months ended September 30, 2007. In accordance with Accounting Principles Board Opinion No. 18, *The Equity Method of Accounting for Investments in Common Stock*, this transaction has been accounted for as a capital transaction of Anglesey. As a result, the Company increased its Additional capital for the nine months ended September 30, 2007 by $.2 rather than adjust its Investment in and advances to unconsolidated affiliate.

4. Conditional Asset Retirement Obligations

The Company has conditional asset retirement obligations (CAROs) at several of its fabricated products facilities. The vast majority of such CAROs consist of incremental costs that would be associated with the removal

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Continued)

and disposal of asbestos (all of which is believed to be fully contained and encapsulated within walls, floors, ceilings or piping) at certain of the older plants if such plants were to undergo major renovation or be demolished. No plans currently exist for any such renovation or demolition of such facilities and the Company s current assessment is that the most probable scenarios are that no such CARO would be triggered for 20 or more years, if at all. Nonetheless, the retroactive application of FASB Interpretation No. 47 (FIN 47), *Accounting for Conditional Assets Retirement Obligations, an interpretation of FASB Statement No. 143* (SFAS No. 143) resulted in the Company recognizing, a Long-term liability of approximately $2.5 at December 31, 2005.

The Company s estimates and judgments that affect the probability weighted estimated future contingent cost amounts did not change during the nine months ended September 30, 2007. The Company s results for the nine month periods ended September 30, 2007 and September 30, 2006, included an incremental accretion of the estimated liability of $.2 and $.1, respectively (recorded in Cost of products sold). The estimated fair value of the CARO at September 30, 2007 was $3.0.

Anglesey (see Note 3) also recorded CARO liabilities of approximately $15.0 and $9.0 in its financial statements as of December 31, 2005 and March 31, 2007, respectively. The treatment applied by Anglesey was not consistent with the principles of SFAS No. 143 or FIN 47. Accordingly, the Company adjusted Anglesey s recording of the CARO to comply with GAAP treatment. The Company adjusted its equity in earnings for Anglesey for the quarters ended September 30, 2007 and September 30, 2006 by $.3 and $.1, respectively, and for the nine month period ended September 30, 2007, periods from January 1, 2006 to July 1, 2006 and from July 1, 2006 through September 30, 2006 by $1.0, $.3 and $.1, respectively, to reflect the impact of applying GAAP with respect to the Anglesey CARO liability.

For purposes of the Company s fair value estimates, a credit adjusted risk free rate of 7.5% was used.

5. Property, Plant and Equipment

The major classes of property, plant, and equipment are as follows:

	September 30, 2007	December 31, 2006
Land and improvements	$ 12.8	$ 12.8
Buildings	20.1	18.6
Machinery and equipment	140.9	92.3
Construction in progress	45.7	51.9
	219.5	175.6
Accumulated depreciation	(13.6)	(5.3)
Property, plant, and equipment, net	$ 205.9	$ 170.3

Approximately $37.2 of the Construction in progress at September 30, 2007, relates to the Company s Spokane, Washington facility (see Note 10).

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Continued)

6. Supplemental Balance Sheet Information

Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets were comprised of the following:

	September 30, 2007	December 31, 2006
Current derivative assets (Note 11)	$ 8.1	$ 29.8
Short term restricted cash	1.4	1.7
Prepaid expenses	4.3	9.3
Total	$ 13.8	$ 40.8

Other Assets

Other assets were comprised of the following:

	September 30, 2007	December 31, 2006
Derivative assets (Note 11)	$ 22.5	$ 13.4
Restricted cash	14.4	23.5
Other	2.7	4.0
Total	$ 39.6	$ 40.9

Other Accrued Liabilities

Other accrued liabilities were comprised of the following:

	September 30, 2007	December 31, 2006
Current derivative liabilities (Note 11)	$ 10.6	$ 25.4
Accrued income taxes, taxes payable and FIN 48 liabilities	4.0	9.8
Accrued bank overdraft see below	9.1	2.8
Dividend payable	3.7	

Other		6.6		9.6
Total	$	34.0	$	47.6

The accrued bank overdraft balance at September 30, 2007 and December 31, 2006 represents uncleared cash disbursements.

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Long-term Liabilities

Long-term liabilities were comprised of the following:

	September 30, 2007	December 31, 2006
Deferred tax and FIN 48 liabilities	$ 35.0	$ 17.1
Workers compensation accruals	17.1	17.4
Environmental accruals	5.8	6.7
Derivative liabilities (Note 11)	3.4	5.4
Asset retirement obligations	3.0	2.9
Other long term liabilities	3.9	8.8
Total	$ 68.2	$ 58.3

7. Secured Debt and Credit Facilities

Long-term debt consisted of the following:

	September 30, 2007	December 31, 2006
Revolving Credit Facility	$	$
Term Loan Facility	50.0	50.0
Total	$ 50.0	$ 50.0

On the Effective Date, the Company and certain subsidiaries of the Company entered into a new Senior Secured Revolving Credit Agreement with a group of lenders providing for a $200.0 revolving credit facility (the Revolving Credit Facility), of which up to a maximum of $60.0 may be utilized for letters of credit. Under the Revolving Credit Facility, the Company is able to borrow (or obtain letters of credit) from time to time in an aggregate amount equal to the lesser of $200.0 and a borrowing base comprised of eligible accounts receivable, eligible inventory and certain eligible machinery, equipment and real estate, reduced by certain reserves, all as specified in the Revolving Credit Facility. The Revolving Credit Facility has a five-year term and matures in July 2011, at which time all principal amounts outstanding thereunder will be due and payable. Borrowings under the Revolving Credit Facility bear interest at a rate equal to either a base prime rate or LIBOR, at the Company s option, plus a specified variable percentage determined by reference to the then remaining borrowing availability under the Revolving Credit Facility. The Revolving Credit Facility may, subject to certain conditions and the agreement of lenders thereunder, be increased up to $275.0 at the request of the Company.

Concurrent with the execution of the Revolving Credit Facility, the Company also entered into a Term Loan and Guaranty Agreement with a group of lenders (the Term Loan Facility). The Term Loan Facility provides for a $50.0 term loan and is guaranteed by the Company and certain of its domestic operating subsidiaries. The Term Loan Facility was fully drawn on August 4, 2006. The Term Loan Facility has a five-year term and matures in July 2011, at which time all principal amounts outstanding thereunder will be due and payable. Borrowings under the Term Loan Facility bear interest at a rate equal to either a premium over a base prime rate or LIBOR, at the Company s option. At September 30, 2007, the average interest rate applicable to borrowings under the Term Loan Facility was 9.7%.

Amounts owed under each of the Revolving Credit Facility and the Term Loan Facility may be accelerated upon the occurrence of various events of default set forth in each such agreement, including, without limitation, the failure to make principal or interest payments when due and breaches of covenants, representations and warranties.

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Revolving Credit Facility is secured by a first priority lien on substantially all of the assets of the Company and certain of its US operating subsidiaries that are also borrowers thereunder. The Term Loan Facility is secured by a second lien on substantially all of the assets of the Company and the Company s US operating subsidiaries that are the borrowers or guarantors thereof.

Both credit facilities place restrictions on the ability of the Company and certain of its subsidiaries to, among other things, incur debt, create liens, make investments, pay dividends, sell assets, undertake transactions with affiliates and enter into unrelated lines of business.

At September 30, 2007, there were no borrowings outstanding under the Revolving Credit Facility, there were approximately $15.5 outstanding letters of credit and there was $50.0 outstanding under the Term Loan Facility.

8. Income Tax Matters

Tax Provision. The (provision) benefit for income taxes for the quarters and nine month periods ended September 30, 2007 and 2006 consisted of:

Quarters ended September 30, 2007 and 2006:

	Quarter Ended September 30, 2007	Three Months Ended September 30, 2006 Period from July 1, 2006 through September 30, 2006	Predecessor July 1, 2006
Domestic	$ (15.0)	$ (2.7)	$
Foreign	(5.0)	(5.6)	
Total	$ (20.0)	$ (8.3)	$

Nine months ended September 30, 2007 and 2006:

	Nine Months Ended September 30, 2006	
		Predecessor
	Period from July 1,	Period from January 1,

	Nine Months Ended September 30, 2007	2006 through September 30, 2006	2006 through July 1, 2006
Domestic	$ (48.5)	$ (2.7)	$ .8
Foreign	(15.8)	(5.6)	(7.0)
Total	$ (64.3)	$ (8.3)	$ (6.2)

The income tax provision for the nine month period ended September 30, 2007 was $64.3, with an effective tax rate of 45.6%. The effective tax rate of 45.6% was impacted by several factors including:

The Company s equity in income before income taxes of Anglesey is treated as a reduction (increase) in Cost of products sold. The income tax effects of the Company s equity in income are included in the tax provision. This resulted in $11.5 being included in the income tax provision, increasing the effective tax rate by approximately 8%.

Benefits associated with any reduction of the valuation allowance are first utilized to reduce intangible assets, with any excess being recorded as an adjustment to Stockholders equity. This resulted in $48.4 being included in the income tax provision, increasing the effective tax rate by approximately 34%.

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The impact on unrecognized tax benefits, including interest and penalties, increased the income tax provision by $2.7 and the effective tax rate by approximately 2%.

The foreign currency impact on unrecognized tax benefits, interest and penalties resulted in a $3.5 currency translation adjustment that was recorded in Accumulated other comprehensive income.

There was a favorable geographical distribution of income.

Deferred Income Taxes. Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The Company had not yet completed the determination of the net operating loss (NOL) carryforwards related to its emergence from chapter 11 bankruptcy and was only able to estimate its NOL carryforwards at December 31, 2006 due to the complexity of the tax analyses. During the quarter ended September 30, 2007, the Company completed its remaining tax analyses for its 2006 federal tax return and ultimately determined that the NOL carryforwards at December 31, 2006 were $890.9. See Note 6 of Notes to Consolidated Financial Statements included in the Company s Annual report on Form 10-K for the year ended December 31, 2006.

Although the Company had approximately $981 of tax attributes, including the NOL carryforwards discussed above, available at December 31, 2006 to offset the impact of future income taxes, the Company does not meet the more likely than not criteria for recognition of such attributes primarily because the Company does not have sufficient history of paying taxes. As such, the Company recorded a full valuation allowance against the amount of tax attributes available and no deferred tax asset was recognized. The benefit associated with any reduction of the valuation allowance is first utilized to reduce intangible assets with any excess being recorded as an adjustment to Stockholders equity rather than as a reduction of income tax expense. Therefore, despite the existence of such tax attributes, the Company expects to record a full statutory tax provision in future periods and, accordingly, the benefit of any tax attributes realized will only affect future balance sheets and statements of cash flows. If the Company ultimately determines that it meets the more likely than not recognition criteria, the amount of NOL carryforwards and other deferred tax assets would be recorded on the balance sheet and would be recorded as an adjustment to Stockholders equity.

Foreign taxes primarily represent Canadian income taxes and United Kingdom income taxes in respect of the Company s ownership in Anglesey. The provision for income tax is based on an assumed effective rate for each applicable period.

Other. The Company and its subsidiaries file income tax returns in the US federal jurisdiction and various states and foreign jurisdictions. The Company s federal income tax return for the 2004 tax year is currently under examination by the Internal Revenue Service. The Company does not expect that the results of this examination will have a material effect on its financial condition or results of operations. The Canada Revenue Agency audited and issued assessment notices for 1998 and 1999 for which Notices of Objection have been filed. The 2000 to 2004 tax years are currently under audit by the Canada Revenue Agency. The Company currently does not expect that the results of these examinations to have a material effect on its financial condition or results of operations. Certain past years are still subject to examination by taxing authorities and the use of NOL carryforwards in future periods could trigger a review of attributes and other tax matters in years that are not otherwise subject to examination.

No US federal or state liability has been recorded for the undistributed earnings of the Company s Canadian subsidiaries at September 30, 2007. These undistributed earnings are considered to be indefinitely reinvested. Accordingly, no provision for US federal and state income taxes or foreign withholding taxes has been provided on such undistributed earnings. Determination of the potential amount of unrecognized deferred US income tax liability and foreign withholding taxes is not practicable because of the complexities associated with its hypothetical calculation.

The Company has unrecognized tax benefits of $17.1 and $14.6 at September 30, 2007 and December 31, 2006, respectively. The change in the nine month period ended September 30, 2007 was primarily due to currency

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Continued)

fluctuations. The Company recognizes interest and penalties related to these unrecognized tax benefits in the income tax provision. During the quarter and nine month periods ended September 30, 2007, the Company recognized approximately $.7 and $2.4, respectively, in interest and penalties. The foreign currency impact on unrecognized tax benefits, interest and penalties resulted in a $3.5 currency translation adjustment that was recorded in Accumulated other comprehensive income. Additionally, the Company had approximately $8.2 and $4.7 accrued at September 30, 2007 and December 31, 2006, respectively, for interest and penalties. The Company does not anticipate that it will have a change in unrecognized tax benefits for the next twelve months that would have a material impact on the Company s earnings.

In connection with the sale of the Company s interests in and related to Queensland Alumina Limited (QAL), the Company made payments totaling approximately $8.5 for alternative minimum tax (AMT) in the United States (approximately $8.0 of Federal AMT and approximately $.5 of state AMT). Such payments were made in the fourth quarter of 2005. Upon completion of the Company s 2005 federal income tax return, the Company determined that approximately $1.0 of AMT was overpaid and was refundable. The Company applied for the refund in the 2005 federal income tax return filed in September 2006 and received the refund in October 2006. The Company believed that the remainder of the United States AMT amounts paid in respect of the sale of interests should, in accordance with the Intercompany Settlement Agreement entered into in connection with the Company s chapter 11 bankruptcy, be reimbursed to the Company from the funds held by the liquidating trustee for the plan of liquidation of two former subsidiaries of the Company (Kaiser Alumina Australia Corporation and Kaiser Finance Corporation). A claim for reimbursement of $7.2 was made in January 2007. In May 2007, the liquidating trust approved the claim and the Company received the $7.2 reimbursement, which amount was recorded as a benefit in Other operating benefits (charges), net in the second quarter of 2007 (see Note 12).

9. Employee Benefit and Incentive Plans

Equity Based Compensation

General. Upon the Company s emergence from chapter 11 bankruptcy, the 2006 Equity and Performance Incentive Plan (the Equity Incentive Plan) became effective. Officers and other key employees of the Company or one or more of its subsidiaries, as well as directors of the Company, are eligible to participate in the Equity Incentive Plan. The Equity Incentive Plan permits the granting of awards in the form of options to purchase common shares, stock appreciation rights, shares of non-vested and vested stock, restricted stock units, performance shares, performance units and other awards. The Equity Incentive Plan will expire on July 6, 2016. No grants will be made after that date, but all grants made on or prior to that date will continue in effect thereafter subject to the terms thereof and of the Equity Incentive Plan. The Company s Board of Directors may, in its discretion, terminate the Equity Incentive Plan at any time. The termination of the Equity Incentive Plan will not affect the rights of participants or their successors under any awards outstanding and not exercised in full on the date of termination.

Subject to certain adjustments that may be required from time to time to prevent dilution or enlargement of the rights of participants under the Equity Incentive Plan, 2,222,222 common shares were reserved for issuance under the Equity Incentive Plan.

Compensation charges related to the Equity Incentive Plan for the quarter ended September 30, 2007, were $2.3, of which $2.2 related to vested and non-vested common shares and restricted stock units and $.1 related to stock options.

During the nine month period ended September 30, 2007, compensation charges related to the Equity Incentive Plan were $6.8, of which $6.6 related to vested and non-vested common shares and restricted stock units and $.2 related to stock options. Compensation charges related to the Equity Incentive Plan for the quarter and nine month period ended September 30, 2006, were $2.3 all of which related to vested and non-vested common shares. The total charges for all periods were included in Selling, administrative, research and development and general expense.

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Continued)

At September 30, 2007, 1,603,649 common shares were available for additional awards under the Equity Incentive Plan.

Non-vested Common Shares and Restricted Stock Units. In April 2007, the Company issued 54,381 non-vested common shares and granted 1,260 restricted stock units to executive officers and other key employees. The shares and the restricted stock units are subject to a three year vesting requirement that lapses on April 3, 2010. The fair value of the shares issued, after assuming a 5% forfeiture rate, of $4.1 is being amortized to expense over a three year period on a ratable basis. The restricted stock units have rights similar to the rights of non-vested common shares and the employee will receive one common share for each restricted stock unit upon the vesting of the restricted stock unit. The restricted stock units vest one third on the first anniversary of the grant date and one third on each of the second and third anniversaries of the date of issuance. The fair value of the restricted stock units issued, after assuming a 5% forfeiture rate, of $.1 is being amortized to expense over the vesting period on a ratable basis.

In June 2007, the Company granted 7,281 non-vested common shares to its non-employee directors. The shares are subject to a one year vesting requirement that lapses on June 6, 2008. The fair value of the shares granted of $.5 is being amortized to expense over a one year period on a ratable basis. An additional 3,877 common shares were issued to non-employee directors electing to receive common shares in lieu of all or a portion of their annual retainer fee. The fair value of the shares of $.3, based on the fair value of the shares at date of issuance, was recognized in earnings in the nine months ended September 30, 2007 as a period expense.

The fair value of the non-vested common shares and restricted stock units is determined based on the closing trading price of the common shares on the grant date. A summary of the activity with respect to non-vested common shares and restricted stock units for the quarter and nine month periods ended September 30, 2007 is as follows:

	Non-Vested Common Shares		**Restricted Stock Units**	
	Shares	**Weighted-Average Grant-Date Fair Value**	**Units**	**Weighed-Average Grant-Date Fair Value**
Quarter				
Outstanding at July 1, 2007	569,841	$ 46.21	4,959	$ 66.58
Granted				
Vested	(16,641)	42.32		
Forfeited	(1,966)	57.30		
Outstanding at September 30, 2007	551,234	$ 46.29	4,959	$ 66.58
Nine Month Period				
Outstanding at January 1, 2007	521,387	$ 42.20	3,699	$ 62.00
Granted	61,662	79.31	1,260	80.01
Vested	(29,093)	42.26		

Forfeited	(2,722)		53.10			
Outstanding at September 30, 2007	551,234	$	46.29	4,959	$	66.58

Under the Equity Incentive Plan, the Company allows participants to elect to have the Company withhold common shares to satisfy minimum statutory tax withholding obligations arising on the vesting of non-vested shares, restricted stock units and stock options. When the Company withholds the shares, it is required to remit to the appropriate taxing authorities the fair value of the shares withheld. During the quarter and nine months ended September 30, 2007, 3,302 and 7,164 shares, respectively, (which are included in vested shares in the above tables) were withheld upon the vesting of common shares. The fair value of the common shares withheld of $.3 and $.6 have

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS (Continued)

been charged to Treasury stock in the quarter and nine months ended September 30, 2007, respectively, as such shares were purchased by the Company and not cancelled at September 30, 2007.

As of September 30, 2007, there was $15.7 of unrecognized compensation cost related to non-vested common shares and restricted stock units. That cost is expected to be recognized over a weighted-average period of 1.8 years.

Stock Options. On April 3, 2007, the Company granted options to purchase 25,137 of its common shares to executive officers and other key employees with a contractual life of ten years.

The fair value of each of the Company s stock option awards is estimated on the date of grant using a Black-Scholes option-pricing model that uses the assumptions noted in the table below. The fair value of the Company s stock option awards, which are subject to graded vesting, is expensed on a straight line basis over the vesting period of the stock options. Due to the Company s short trading history for its common shares since emergence from chapter 11 bankruptcy on July 6, 2006, expected volatility could not be reliably calculated based on the historical volatility of the common shares. As such, the Company has determined volatility for use in the Black-Sholes option-pricing model using the volatility of the stock of a number of similar public companies over a period equal to the expected option life of six years. The risk-free rate for periods within the contractual life of the stock option award is based on the yield curve of a zero-coupon US Treasury bond on the date the stock option is awarded. The Company uses historical data to estimate employee terminations and the simplified method to estimate the expected option life within the valuation model.

The significant weighted average assumptions used in determining the grant date fair value of the option awards granted on April 3, 2007 were as follows:

Dividend yield	%
Volatility rate	45%
Risk-free interest rate	4.59%
Expected option life (years)	6.0

Prior to April 3, 2007, the Company had no outstanding options to purchase common shares. A summary of the Company s stock option activity for the nine months ended September 30, 2007 is as follows:

	Number of Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life (In years)	Aggregate Intrinsic Value (In millions)
Outstanding at April 1, 2007		$		