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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the quarterly period ended April 3, 2016

or

o **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 001-11499

WATTS WATER TECHNOLOGIES, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	**04-2916536** (I.R.S. Employer Identification No.)
815 Chestnut Street, North Andover, MA (Address of Principal Executive Offices)	**01845** (Zip Code)

Registrant s Telephone Number, Including Area Code: **(978) 688-1811**

(Former Name, Former Address and Former Fiscal year, if changed since last report.)

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

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

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. (Check one):

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

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Class	Outstanding at May 9, 2016
Class A Common Stock, $0.10 par value	27,855,791
Class B Common Stock, $0.10 par value	6,379,290

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WATTS WATER TECHNOLOGIES, INC. AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements

WATTS WATER TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(Amounts in millions, except share information)

(Unaudited)

		April 3, 2016		December 31, 2015
ASSETS				
CURRENT ASSETS:				
Cash and cash equivalents	**$**	**259.4**	$	296.2
Restricted Cash		**18.2**		
Trade accounts receivable, less allowance for doubtful accounts of $11.2 million at April 3, 2016 and $10.1 million at December 31, 2015		**207.7**		186.4
Inventories, net:				
Raw materials		**89.2**		88.5
Work in process		**16.2**		15.2
Finished goods		**159.3**		136.3
Total Inventories		**264.7**		240.0
Prepaid expenses and other assets		**45.2**		46.1
Deferred income taxes		**39.6**		38.4
Assets held for sale		**13.4**		1.9
Total Current Assets		**848.2**		809.0
PROPERTY, PLANT AND EQUIPMENT:				
Property, plant and equipment, at cost		**503.7**		498.6
Accumulated depreciation		**(318.4)**		(314.2)
Property, plant and equipment, net		**185.3**		184.4
OTHER ASSETS:				
Goodwill		**497.6**		489.0
Intangible assets, net		**189.2**		192.8
Deferred income taxes		**3.1**		3.7
Other, net		**11.2**		11.9
TOTAL ASSETS	$	**1,734.6**	$	1,690.8
LIABILITIES AND STOCKHOLDERS EQUITY				
CURRENT LIABILITIES:				
Accounts payable	$	**98.6**	$	101.7
Accrued expenses and other liabilities		**148.1**		145.7
Accrued compensation and benefits		**37.6**		46.5
Current portion of long-term debt		**1.1**		1.1
Total Current Liabilities		**285.4**		295.0
LONG-TERM DEBT, NET OF CURRENT PORTION		**597.1**		574.2
DEFERRED INCOME TAXES		**72.9**		71.8
OTHER NONCURRENT LIABILITIES		**48.1**		44.9
STOCKHOLDERS EQUITY:				
Preferred Stock, $0.10 par value; 5,000,000 shares authorized; no shares issued or outstanding				

Class A Common Stock, $0.10 par value; 80,000,000 shares authorized; 1 vote per share; issued and outstanding 27,887,661 shares at April 3, 2016 and 28,049,908 shares at December 31, 2015		**2.8**		2.8
Class B Common Stock, $0.10 par value; 25,000,000 shares authorized; 10 votes per share; issued and outstanding, 6,379,290 shares at April 3, 2016 and December 31, 2015		**0.6**		0.6
Additional paid-in capital		**516.2**		512.0
Retained earnings		**315.5**		317.7
Accumulated other comprehensive loss		**(104.0)**		(128.2)
Total Stockholders Equity		**731.1**		704.9
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$	**1,734.6**	$	1,690.8

See accompanying notes to consolidated financial statements.

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WATTS WATER TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

(Amounts in millions, except per share information)

(Unaudited)

	First Quarter Ended			
	April 3, 2016		March 29, 2015	
Net sales	$	**344.2**	$	356.2
Cost of goods sold		**209.0**		225.7
GROSS PROFIT		**135.2**		130.5
Selling, general and administrative expenses		**102.6**		105.7
Restructuring and other charges, net		**1.4**		2.0
OPERATING INCOME		**31.2**		22.8
Other (income) expense:				
Interest income		**(0.2)**		(0.2)
Interest expense		**6.7**		5.9
Other income, net		**(2.2)**		(0.2)
Total other expense		**4.3**		5.5
INCOME BEFORE INCOME TAXES		**26.9**		17.3
Provision for income taxes		**10.7**		5.7
NET INCOME	$	**16.2**	$	11.6
BASIC EPS				
NET INCOME PER SHARE	**$**	**0.47**	$	0.33
Weighted average number of shares		**34.4**		35.1
DILUTED EPS				
NET INCOME PER SHARE	**$**	**0.47**	$	0.33
Weighted average number of shares		**34.5**		35.2
Dividends declared per share	**$**	**0.17**	$	0.15

See accompanying notes to consolidated financial statements.

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WATTS WATER TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(Amounts in millions)

(Unaudited)

	First Quarter Ended	
	April 3, 2016	**March 29, 2015**
Net income	**$ 16.2**	$ 11.6
Other comprehensive income (loss):		
Foreign currency translation adjustments	**24.4**	(65.1)
Interest rate swap, net of tax	**(0.2)**	
Defined benefit pension plans amortization of net losses included in net periodic pension cost, net of tax		0.2
Other comprehensive income (loss)	**24.2**	(64.9)
Comprehensive income (loss)	**$ 40.4**	$ (53.3)

See accompanying notes to consolidated financial statements.

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WATTS WATER TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Amounts in millions)

(Unaudited)

	First Quarter Ended April 3, 2016	First Quarter Ended March 29, 2015
OPERATING ACTIVITIES		
Net income	**$ 16.2**	$ 11.6
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Depreciation	**7.3**	7.9
Amortization of intangibles	**5.1**	5.1
Loss on disposal and impairment of property, plant and equipment and other	**0.3**	1.1
Stock-based compensation	**2.8**	2.3
Deferred income tax benefit	**(1.0)**	(1.8)
Gain on acquisition	**(1.7)**	
Changes in operating assets and liabilities, net of effects from business acquisitions and divestures:		
Accounts receivable	**(16.0)**	(21.6)
Inventories	**(19.9)**	(0.4)
Prepaid expenses and other assets	**(2.3)**	0.4
Accounts payable, accrued expenses and other liabilities	**(12.7)**	(3.8)
Net cash (used in) provided by operating activities	**(21.9)**	0.8
INVESTING ACTIVITIES		
Additions to property, plant and equipment	**(9.2)**	(5.6)
Proceeds from sale of property, plant, and equipment	**0.1**	
Restricted cash	**(18.2)**	
Business acquisitions, net of cash acquired	**(2.1)**	
Net cash used in investing activities	**(29.4)**	(5.6)
FINANCING ACTIVITIES		
Proceeds from long-term borrowings	**300.0**	
Payments of long-term debt	**(275.4)**	(0.3)
Payment of capital leases and other	**(0.5)**	(0.8)
Proceeds from share transactions under employee stock plans	**0.6**	0.5
Tax benefit of stock awards exercised		0.1
Payments to repurchase common stock	**(12.5)**	(9.4)
Debt issue costs	**(2.1)**	
Dividends	**(5.9)**	(5.3)
Net cash provided by (used in) financing activities	**4.2**	(15.2)
Effect of exchange rate changes on cash and cash equivalents	**10.3**	(19.3)
DECREASE IN CASH AND CASH EQUIVALENTS	**(36.8)**	(39.3)
Cash and cash equivalents at beginning of year	**296.2**	301.1
CASH AND CASH EQUIVALENTS AT END OF PERIOD	**$ 259.4**	$ 261.8
NON-CASH INVESTING AND FINANCING ACTIVITIES		
Acquisition of businesses:		
Fair value of assets acquired	**5.7**	
Cash paid, net of cash acquired	**2.1**	
Gain on acquisition	**1.7**	
Liabilities assumed	**$ 1.9**	

Issuance of stock under management stock purchase plan	**$**	**0.7**	$	0.3
CASH PAID FOR:				
Interest	**$**	**1.2**	**$**	1.2
Income taxes	**$**	**5.5**	$	5.8

See accompanying notes to consolidated financial statements.

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WATTS WATER TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included in the Watts Water Technologies, Inc. (the Company) Consolidated Balance Sheet as of April 3, 2016, the Consolidated Statements of Operations for the first quarters ended April 3, 2016 and March 29, 2015, the Consolidated Statements of Comprehensive Income (Loss) for the first quarters ended April 3, 2016 and March 29, 2015, and the Consolidated Statements of Cash Flows for the first quarters ended April 3, 2016 and March 29, 2015.

The consolidated balance sheet at December 31, 2015 has been derived from the audited consolidated financial statements at that date. The accounting policies followed by the Company are described in the Company s Annual Report on Form 10-K for the year ended December 31, 2015. The financial statements included in this report should be read in conjunction with the consolidated financial statements and notes included in the Annual Report on Form 10-K for the year ended December 31, 2015. Operating results for the interim periods presented are not necessarily indicative of the results to be expected for the year ending December 31, 2016.

The Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2015-03, Interest-Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs effective for public companies beginning with the first interim period after December 15, 2015. This Update required that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of the debt liability, consistent with debt discounts as opposed to an asset. This is considered a change in accounting principal, and the Company applied the new guidance as of April 3, 2016 and on a retrospective basis. Therefore, we have restated our long-term debt and other asset balances in the Balance Sheet for December 31, 2015 for comparative purposes. Refer to Note 10 below for further details.

The Company operates on a 52-week fiscal year ending on December 31st. Any quarterly data contained in this Quarterly Report on Form 10-Q generally reflect the results of operations for a 13-week period.

2. Accounting Policies

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Goodwill and Long-Lived Assets

The changes in the carrying amount of goodwill by geographic segment are as follows:

	April 3, 2016							
	Gross Balance				Accumulated Impairment Losses			Net Goodwill
	Balance January 1, 2016	Acquired During the Period	Foreign Currency Translation and Other	Balance April 3, 2016	Balance January 1, 2016	Impairment Loss During the Period	Balance April 3, 2016	April 3, 2016
	(in millions)							
Americas	**$ 391.2**	**$**	**$ 0.6**	**$ 391.8**	**$ (24.5)**	**$**	**$ (24.5)**	**$ 367.3**
Europe, Middle East and Africa (EMEA)	**238.6**		**4.4**	**243.0**	**(129.7)**		**(129.7)**	**113.3**
Asia-Pacific	**26.3**	**3.3**	**0.3**	**29.9**	**(12.9)**		**(12.9)**	**17.0**
Total	**$ 656.1**	**$ 3.3**	**$ 5.3**	**$ 664.7**	**$ (167.1)**	**$**	**$ (167.1)**	**$ 497.6**

	December 31, 2015							
	Gross Balance				Accumulated Impairment Losses			Net Goodwill
	Balance January 1, 2015	Acquired During the Period	Foreign Currency Translation and Other	Balance December 31, 2015	Balance January 1, 2015	Impairment Loss During the Period	Balance December 31, 2015	December 31, 2015
	(in millions)							
Americas	$ 398.0	$	$ (6.8)	$ 391.2	$ (24.5)	$	$ (24.5)	$ 366.7
EMEA	265.5		(26.9)	238.6		(129.7)	(129.7)	108.9
Asia-Pacific	12.9	12.9	0.5	26.3	(12.9)		(12.9)	13.4
Total	$ 676.4	$ 12.9	$ (33.2)	$ 656.1	$ (37.4)	$ (129.7)	$ (167.1)	$ 489.0

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Goodwill and indefinite-lived intangible assets are tested for impairment at least annually or more frequently if events or circumstances indicate that it is more likely than not that they might be impaired, such as from a change in business conditions. The Company performs its annual goodwill and indefinite-lived intangible assets impairment assessment in the fourth quarter of each year.

On February 26, 2016, the Company acquired an additional 50% of the outstanding shares of AERCO Korea Co., Ltd., (AERCO Korea) for an aggregate purchase price of approximately $4 million. Prior to February 26, 2016, the Company held a 40% interest in AERCO Korea, which operated as a joint venture. The Company completed a preliminary purchase price allocation that resulted in the recognition of $3.3 million in goodwill and $1.6 million in intangible assets.

In the fourth quarter of 2015, the Company performed a quantitative impairment analysis for the EMEA reporting unit in connection with the annual strategic plan and due to the underperformance to budget, primarily caused by the continued challenging European macroeconomic environment. The Company estimated the fair value of the reporting unit using a weighted calculation of the income approach and the market approach. In the second step of the impairment test, the carrying value of the goodwill exceeded the implied fair value of goodwill, resulting in a pre-tax impairment charge of $129.7 million.

On November 30, 2015, the Company completed the acquisition of 80% of the outstanding shares of Apex Valves Limited (Apex), a New Zealand company, with a commitment to purchase the remaining 20% ownership within three years of closing. The aggregate purchase price was approximately $20.4 million. The Company accounted for the transaction as a business combination. The Company completed a purchase price allocation that resulted in the recognition of $12.9 million in goodwill and $10.1 million in intangible assets.

Intangible assets with estimable lives and other long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset or asset group may not be recoverable. Recoverability of intangible assets with estimable lives and other long-lived assets are measured by a comparison of the carrying amount of an asset or asset group to future net undiscounted pretax cash flows expected to be generated by the asset or asset group. If these comparisons indicate that an asset is not recoverable, the impairment loss recognized is the amount by which the carrying amount of the asset or asset group exceeds the related estimated fair value. Estimated fair value is based on either discounted future pretax operating cash flows or appraised values, depending on the nature of the asset. The Company determines the discount rate for this analysis based on the weighted average cost of capital based on the market and guideline public companies for the related business, and does not allocate interest charges to the asset or asset group being measured. Judgment is required to estimate future operating cash flows.

Intangible assets include the following:

	April 3, 2016			December 31, 2015		
	Gross Carrying Amount	**Accumulated Amortization**	**Net Carrying Amount**	**Gross Carrying Amount**	**Accumulated Amortization**	**Net Carrying Amount**
			(in millions)			
Patents	**$ 16.1**	**$ (14.3)**	**$ 1.8**	$ 16.1	$ (14.1)	$ 2.0
Customer relationships	**215.2**	**(105.8)**	**109.4**	212.5	(102.1)	110.4
Technology	**41.6**	**(16.8)**	**24.8**	41.3	(16.1)	25.2
Trade Names	**22.1**	**(6.8)**	**15.3**	21.9	(6.4)	15.5
Other	**6.9**	**(5.9)**	**1.0**	9.4	(5.9)	3.5

Total amortizable intangibles		**301.9**		**(149.6)**		**152.3**		301.2		(144.6)		156.6
Indefinite-lived intangible assets		**36.9**				**36.9**		36.2				36.2
Total	**$**	**338.8**	**$**	**(149.6)**	**$**	**189.2**	$	337.4	$	(144.6)	$	192.8

The Company acquired $1.6 million in intangible assets as part of the AERCO Korea acquisition, consisting entirely of customer relationships. The amortization period of these customer relationships is 10 years.

Aggregate amortization expense for amortizable intangible assets for both the first quarters of 2016 and 2015 was $5.1 million. Additionally, future amortization expense for the next five years on amortizable intangible assets is expected to be approximately $15.3 million for the remainder of 2016, $19.5 million for 2017, $16.6 million for 2018, $12.6 million for 2019 and $12.2 million for 2020. Amortization expense is recorded on a straight-line basis over the estimated useful lives of the intangible assets. The weighted-average remaining life of total amortizable intangible assets is 11.3 years. Patents, customer relationships, technology, trade names and other amortizable intangibles have weighted-average remaining lives of 3.8 years, 11.3 years, 9.3 years, 14.3 years and 20.6 years, respectively. Indefinite-lived intangible assets primarily include trademarks and trade names.

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Stock-Based Compensation

The Company maintains one stock incentive plan, the Second Amended and Restated 2004 Stock Incentive Plan (the 2004 Stock Incentive Plan). Under this plan, key employees have been granted nonqualified stock options to purchase the Company s Class A common stock. Options typically become exercisable over a four-year period at the rate of 25% per year and expire ten years after the grant date. However, most options granted in 2014 become exercisable over a three-year period at the rate of one-third per year. Options granted under the plan may have exercise prices of not less than 100% of the fair market value of the Class A common stock on the date of grant. The Company s practice has been to grant all options at fair market value on the grant date. Beginning in 2015, the Company stopped granting stock options as part of its annual equity awards to employees and the Company did not issue any stock options in the first three months of 2016 or 2015.

The Company grants shares of restricted stock and deferred shares to key employees and stock awards to non-employee members of the Company s Board of Directors under the 2004 Stock Incentive Plan. Stock awards to non-employee members of the Company s Board of Directors are fully vested upon grant. Employees restricted stock awards and deferred shares typically vest over a three-year period at the rate of one-third per year, except that most restricted stock awards and deferred shares granted in 2014 vest over a two-year period at the rate of 50% per year. The restricted stock awards and deferred shares are amortized to expense on a straight-line basis over the vesting period. In 2016, the Company changed the timing of its annual grant to the first quarter compared to past annual grants in the third quarter. The Company issued 110,295 shares of restricted stock awards and deferred shares in the first three months of 2016 related to the annual grant.

The Company also grants performance stock units to key employees under the 2004 Stock Incentive Plan. Performance stock units vest at the end of the performance period set by the Compensation Committee of our Board of Directors at the time of grant. Upon vesting, the number of shares of the Company s Class A common stock awarded to each performance stock unit recipient will be determined based on the Company s performance relative to certain performance goals set at the time the performance stock units were granted. The recipient of a performance stock unit award may earn from no shares to twice the number of target shares awarded to such recipient. The performance stock units are amortized to expense over the vesting period, and based on the Company s performance relative to the performance goals, may be adjusted. If the performance goals are not met, no awards are earned and previously recognized compensation expense is reversed. The Company granted 106,724 of annual awards for performance stock units during the first three months of 2016 and did not issue any performance stock units in the first three months of 2015.

The Company has a Management Stock Purchase Plan that allows for the purchase of restricted stock units (RSUs) by key employees. On an annual basis, key employees may elect to receive a portion of their annual incentive compensation in RSUs instead of cash. Each RSU represents one share of Class A common stock and is purchased by the employee at 67% of the fair market value of the Company s Class A common stock on the date of grant. Beginning with annual incentive compensation for 2016, the purchase price for RSUs has been increased to 80% of the fair market value of the Company s Class A common stock. RSUs vest either annually over a three-year period from the grant date or upon the third anniversary of the grant date and receipt of the shares underlying RSUs is deferred for a minimum of three years or such greater number of years as is chosen by the employee. An aggregate of 2,000,000 shares of Class A common stock may be issued under the Management Stock Purchase Plan. The Company granted 88,882 RSUs and 59,995 RSUs in the first three months of 2016 and 2015, respectively.

The fair value of each RSU issued under the Management Stock Purchase Plan is estimated on the date of grant using the Black-Scholes-Merton Model based on the following weighted average assumptions:

	2016	**2015**

Expected life (years)	**3.0**	3.0
Expected stock price volatility	**24.8%**	23.4%
Expected dividend yield	**1.3%**	1.2%
Risk-free interest rate	**0.9%**	1.1%

The above assumptions were used to determine the weighted average grant-date fair value of RSUs of $18.15 and $19.04 in 2016 and 2015, respectively.

A more detailed description of each of these plans can be found in Note 13 of the Notes to Consolidated Financial Statements in the Company s Annual Report on Form 10-K for the year ended December 31, 2015.

Shipping and Handling

The Company s shipping and handling costs included in selling, general and administrative expenses were $11.4 million and $14.4 million for the first quarters of 2016 and 2015, respectively.

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Research and Development

Research and development costs included in selling, general and administrative expenses were $6.6 million and $6.4 million for the first quarters of 2016 and 2015, respectively.

Taxes, Other than Income Taxes

Taxes assessed by governmental authorities on sale transactions are recorded on a net basis and excluded from sales in the Company s consolidated statements of operations.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

New Accounting Standards

In April 2016, the FASB issued ASU2016-10, Revenue from Contracts with Customers-Identifying Performance Obligations and Licensing. ASU 2016-10 clarifies the guidance on identifying performance obligations and licensing implementation guidance determined in ASU 2014-09 Revenue from Contracts with Customers (Topic 606), which is not yet affective. The adoption of this guidance is not expected to have a material impact on the Company s financial statements.

In March 2016, the FASB issued ASU 2016-09, Improvements to Employee Share-Based Payment Accounting. ASU 2016-09 simplifies several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as equity or liabilities, forfeitures, and classification on the statement of cash flows. ASU 2016-09 is effective for financial statements issued for annual periods beginning after December 15, 2016 and all interim periods thereafter. Amendments related to the timing of income tax consequences and forfeitures should be applied using a modified retrospective transition method by means of a cumulative-effect adjustment to equity as of the beginning of the period in which the guidance is adopted. Amendments related to the presentation of employee taxes paid on the statement of cash flows when an employer withholds shares to meet the minimum statutory requirement should be applied retrospectively. Amendments requiring recognition of income tax consequences in the income statement should be applied prospectively. The Company is assessing the impact of this standard on the Company s financial statements.

In March 2016, the FASB issued ASU2016-08, Revenue from Contracts with Customers-Principal versus Agent Consideration. ASU 2016-08 clarifies the guidance on principal versus agent considerations determined in ASU 2014-09 Revenue from Contracts with Customers (Topic 606), which is not yet affective. The adoption of this guidance is not expected to have a material impact on the Company s financial statements.

In March 2016, the FASB issued ASU2016-06, Contingent Put and Call Options in Debt Instruments . ASU 2016-06 clarifies the requirements for assessing whether a contingent put (call) options that can accelerate the principal on debt instruments are clearly and closely related to their debt hosts. ASU 2016-06 is effective for financial statements issued for annual periods beginning after December 15, 2016 and all interim periods thereafter. The adoption of this guidance is not expected to have a material impact on the Company s financial statements.

In February 2016, the FASB issued ASU2016-02, Leases (Topic 842) . ASU 2016-02 requires a lessee to recognize in the statement of financial position a liability to make lease payments and a right-of-use asset representing the right to use the underlying asset for the lease term for both finance and operating leases. ASU 2016-02 is effective for financial statements issued for annual periods beginning after December 15, 2018 and all interim periods thereafter. Earlier application is permitted for all entities. The Company is assessing the impact of this standard on the Company s financial statements.

3. Acquisitions

AERCO Korea

On February 26, 2016, the Company acquired an additional 50% of the outstanding shares of AERCO Korea for an aggregate purchase price of approximately $4 million. Prior to February 26, 2016, the Company held a 40% interest in AERCO Korea, which operated as a joint venture. The Company now owns 90% of the outstanding shares of AERCO Korea and as part of the transaction

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committed to purchasing the remaining 10% ownership by December 31, 2017. AERCO Korea sells AERCO U.S. products in Korea, including commercial high-efficiency boilers and water heaters. AERCO Korea strengthens Watts strategic vision to expand solutions sales into Asia-Pacific. The Company accounted for the transaction as a step acquisition within a business combination. The Company recognized a $1.7 million pre-tax gain on the previously held 40% ownership interest in the first quarter of 2016.

The Company completed a purchase price allocation that resulted in the recognition of $3.3 million in goodwill, $1.6 million in intangible assets and $0.8 million as the estimate of the acquisition date fair value on commitment to purchase the remaining 10% ownership by December 31, 2017. The intangible assets acquired consisted entirely of customer relationships. The amortization period of these customer relationships is 10 years. The goodwill is not deductible for tax purposes. The results of AERCO Korea are not material to the Company s consolidated financial statements. The balance sheet and results of operations for AERCO Korea are included in the Company s Asia-Pacific segment since acquisition date.

APEX

On November 30, 2015, the Company completed the acquisition of 80% of the outstanding shares of Apex. Apex specializes in the design and manufacture of control valves for low and high pressure hot water and filtration systems. Apex also produces an extensive range of float and reservoir valves for the agricultural industry. The aggregate purchase price was approximately $20.4 million and the Company recorded a long-term liability of $5.5 million as the estimate of the acquisition date fair value on the contractual call option to purchase the remaining 20% within three years of closing.

The Company accounted for the transaction as a business combination. The Company completed a purchase price allocation that resulted in the recognition of $12.9 million in goodwill and $10.1 million in intangible assets. Intangible assets consist primarily of customer relationships with an estimated life of 10 years and a trade name with an estimated life of 15 years. The goodwill is not deductible for tax purposes. The results of Apex are not material to the Company s consolidated financial statements. The results of operations for Apex are included in the Company s Asia-Pacific segment since acquisition date.

4. Sale of Business

Agreement to Sell a China Operating Entity

On September 22, 2015, the Company signed an agreement to sell an operating entity in China whose manufacturing facility was dedicated to the production of non-core products. As of April 3, 2016, the Company had stopped manufacturing at the facility and met the requirements for held for sale classification on the consolidated balance sheet. The Company reclassified $11.4 million of assets to assets held for sale as of the balance sheet date and the assets primarily relate to land use rights, building and machinery. As of April 3, 2016, the Company had deposited $18.2 million in cash into an escrow account as part of the agreement. The Company classified the $18.2 million deposit as restricted cash on the consolidated balance sheet and statement of cash flows as of April 3, 2016. This cash will be returned to the Company once the sale is completed, which is expected to occur in the second quarter of 2016. The sales price will exceed the carrying value of the assets. The Company currently estimates the pre-tax gain on sale to range from $8 million to $9 million and includes approximately $8 million relating to non-cash cumulative translation adjustments that will be reversed on liquidation of the entity.

5. Financial Instruments and Derivative Instruments

The Company measures certain financial assets and liabilities at fair value on a recurring basis, including deferred compensation plan assets and related liability, and redeemable financial instruments. The fair values of these certain financial assets and liabilities were determined using the following inputs at April 3, 2016 and December 31, 2015:

		Fair Value Measurements at April 3, 2016 Using:		
	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
		(in millions)		
Assets				
Plan asset for deferred compensation(1)	$ 3.0	$ 3.0	$	$
Total assets	$ 3.0	$ 3.0	$	$
Liabilities				
Plan liability for deferred compensation(2)	$ 3.0	$ 3.0	$	$
Redeemable financial instrument(3,4)	6.6			6.6
Total liabilities	$ 9.6	$ 3.0	$	$ 6.6

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	Total	Fair Value Measurements at December 31, 2015 Using: Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
		(in millions)		
Assets				
Plan asset for deferred compensation(1)	$ 3.3	$ 3.3	$	$
Total assets	$ 3.3	$ 3.3	$	$
Liabilities				
Plan liability for deferred compensation(2)	$ 3.3	$ 3.3	$	$
Redeemable financial instrument (3)	5.7			5.7
Total liabilities	$ 9.0	$ 3.3	$	$ 5.7

(1) Included on the Company s consolidated balance sheet in other assets (other, net).

(2) Included on the Company s consolidated balance sheet in accrued compensation and benefits.

(3) Included in the Company s consolidated balance sheet in other noncurrent liabilities as of April 3, 2016 and December 31, 2015 and relates to a mandatorily redeemable equity instrument as part of the Apex acquisition in 2015.

(4) Included in the Company s consolidated balance sheet in other noncurrent liabilities as of April 3, 2016 and relates to a mandatorily redeemable equity instrument as part of the AERCO Korea acquisition.

The table below provides a summary of the changes in fair value of all financial assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the period December 31, 2015 to April 3, 2016.

	Balance December 31, 2015	Settlements	Purchases	Total realized and unrealized (gains) losses included in: Net earnings adjustments	Comprehensive income	Balance April 3, 2016
			(in millions)			
Redeemable financial instrument	$ 5.7		$ 0.8		$ 0.1	$ 6.6

In connection with the acquisition of AERCO Korea in the first quarter of 2016, a liability of $0.8 million was recognized as the estimate of the acquisition date fair value of the mandatorily redeemable equity instrument. This liability is classified as Level 3 under the fair value hierarchy as it is based on the commitment to purchase the remaining 10% of AERCO Korea shares by December 31, 2017, which is not observable in the market.

In connection with the acquisition of Apex in the fourth quarter of 2015, a liability of $5.5 million was recognized as the estimate of the acquisition date fair value of the mandatorily redeemable equity instrument. This liability is classified as Level 3 under the fair value hierarchy as it is based on the commitment to purchase the remaining 20% of Apex shares within the next three years, which is not observable in the market.

The Company uses financial instruments from time to time to enhance its ability to manage risk, including foreign currency, interest rates and commodity pricing exposures, which exist as part of its ongoing business operations. The use of derivatives exposes the Company to counterparty credit risk for nonperformance and to market risk related to changes in currency exchange rates, interest rates and commodity prices. The Company manages its exposure to counterparty credit risk through diversification of counterparties. The Company s counterparties in derivative transactions are substantial commercial banks with significant experience using such derivative instruments. The impact of market risk on the fair value and cash flows of the Company s derivative instruments is monitored and the Company restricts the use of derivative financial instruments to hedging activities. The Company does not enter into contracts for trading purposes nor does the Company enter into any contracts for speculative purposes. The use of derivative instruments is approved by senior management under written guidelines.

Interest Rate Swap

On February 12, 2016, the Company entered into a new Credit Agreement (the Credit Agreement) pursuant to which it received a funding commitment under a Term Loan of $300 million, of which the entire $300 million has been drawn on, and a Revolving

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Commitment (Revolver) of $500 million, none of which was drawn as of April 3, 2016. Both facilities mature on February 12, 2021, five years after the date of the Credit Agreement. For each facility, the Company can choose either an Adjusted LIBOR or Alternative Base Rate (ABR). Upon intended election of Adjusted LIBOR as the interest rate, the Term Loan has quarterly interest payments beginning May 12, 2016 and quarterly principal repayments commencing on March 31, 2017. The Revolver has the same quarterly interest payment dates as the Term Loan, and a balloon payment of principal on maturity date.

Accordingly, the Company s earnings and cash flows are exposed to interest rate risk from changes in Adjusted LIBOR. In order to manage the Company s exposure to changes in cash flows attributable to fluctuations in LIBOR indexed interest payments related to the Term Loan and Revolver, the Company entered into two interest rate swaps. For each interest rate swap, the Company receives the three-month USD-LIBOR subject to a 0% floor, and pays a fixed rate of 1.31375% on a notional amount of $225.0 million. The swaps mature on February 12, 2021. The Company formally documents our hedge relationships at hedge inception to ensure that its interest rate swaps qualify for hedge accounting. On a quarterly basis, the Company assesses whether the interest rate swaps are highly effective in offsetting changes in the cash flow of the hedged item. The Company does not hold or issue interest rate swaps for trading purposes. The swaps are designated as cash flow hedges. For the three months ended April 3, 2016, a loss of $0.2 million was recorded in Accumulated Other Comprehensive Loss to recognize the effective portion of the fair value of interest rate swaps that qualify as a cash flow hedge.

Non-Designated Cash Flow Hedge

The Company has exposure to a number of foreign currency rates, including the Canadian dollar, the euro, the Chinese yuan and the British pound. To manage this risk, the Company generally uses a layering methodology whereby at the end of any quarter, the Company has generally entered into forward exchange contracts which hedge approximately 50% of the projected intercompany purchase transactions for the next twelve months. These forward exchange contracts are not designated as cash flow or fair value hedges. The Company entered into one forward exchange contract to manage the foreign currency rate exposure between the Canadian dollar and the euro regarding an intercompany loan. This forward contract is marked-to-market with changes in the fair value recorded to earnings. The Company recorded a loss of $0.3 million for the first quarter ended April 3, 2016 related to the foreign exchange contract. We did not have any forward contracts in the first three months of 2015.

Fair Value

Cash equivalents consist of instruments with remaining maturities of three months or less at the date of purchase and consist primarily of certificates of deposit and money market funds, for which the carrying amount is a reasonable estimate of fair value. The carrying amounts of cash and cash equivalents, trade receivables and trade payables approximate fair value because of the short maturity of these financial instruments.

The fair value of the Company s 5.85% senior notes due 2016 and 5.05% senior notes due 2020 is based on quoted market prices of similar notes (level 2). The fair value of the Company s borrowings outstanding under the Credit Agreement and the Company s variable rate debt approximates its carrying value. The carrying amount and the estimated fair market value of the Company s long-term debt, including the current portion, are as follows:

	April 3, 2016	December 31, 2015
	(in millions)	
Carrying amount	**$ 598.2**	$ 575.3
Estimated fair value	**$ 605.9**	$ 584.1

6. Restructuring and Other Charges, Net

The Company s Board of Directors approves all major restructuring programs that involve the discontinuance of significant product lines or the shutdown of significant facilities. From time to time, the Company takes additional restructuring actions, including involuntary terminations that are not part of a major program. The Company accounts for these costs in the period that the liability is incurred. These costs are included in restructuring and other charges in the Company s consolidated statements of operations.

A summary of the pre-tax cost by restructuring program is as follows:

	First Quarter Ended	
	April 3, 2016	March 29, 2015
	(in millions)	
Restructuring costs:		
2015 Actions	**$ 1.0**	$ 1.3
2013 Actions		0.5
Other Actions	**0.4**	0.2
Total restructuring and other charges, net	**$ 1.4**	$ 2.0

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The Company recorded pre-tax restructuring and other charges, net in its business segments as follows:

	First Quarter Ended	
	April 3, 2016	March 29, 2015
	(in millions)	
Americas	$ **0.8**	$ 1.3
EMEA	**0.4**	0.8
Asia-Pacific	**0.2**	
Corporate		(0.1)
Total	**$ 1.4**	$ 2.0

2015 Actions

In 2015, the Board of Directors of the Company approved a program relating to the transformation of the Company s Americas and Asia-Pacific businesses. The first phase of the program primarily involved the exit of low-margin, non-core product lines and global sourcing actions. The Company eliminated approximately $165 million of combined Americas and Asia-Pacific net sales primarily within the Company s do-it-yourself (DIY) distribution channel. As part of the rationalization exercise, the Company entered into an agreement to sell an operating entity in China whose manufacturing facility was dedicated exclusively to the manufacturing of products being rationalized. The Company expects to complete the sale in the second quarter of 2016 for approximately $9 million. The second phase of the program involves reducing the square footage of the Company s Americas facilities, which together with phase one, is expected to reduce the Americas net operating footprint by approximately 30%. The second phase is designed to improve the utilization of our remaining facilities, better leverage our cost structure, reduce working capital, and improve execution of customer delivery requirements.

On a combined basis, the total estimated pre-tax cost for the Company s transformation program related to its Americas and Asia-Pacific businesses is $63 million to $68 million, including restructuring costs of $20.4 million, goodwill and intangible asset impairments of $13.4 million and other transformation and deployment costs of $29 million to $34 million. The other transformation and deployment costs include consulting and project management fees, inventory write offs and other associated costs. Costs of the program are expected to be incurred through 2017.

The following table summarizes by type, the total expected, incurred and remaining pre-tax restructuring costs for the Company s transformation program related to its Americas and Asia-Pacific businesses):

	Severance	Legal and consultancy	Asset write-downs	Facility exit and other	Total
			(in millions)		
Costs incurred 2015	$ 8.5	0.7	1.6	2.8	13.6
Costs incurred first quarter 2016	**0.2**	**0.2**	**0.2**	**0.4**	**1.0**
Remaining costs to be incurred	0.3	0.3	0.9	4.3	5.8
Total expected restructuring costs	**$ 9.0**	**$ 1.2**	**$ 2.7**	**$ 7.5**	**$ 20.4**

The following table summarizes total restructuring costs for the period ended April 3, 2016, incurred program to date and expected pre-tax restructuring costs by business segment for the Company s Americas and Asia-Pacific 2015 transformation program:

	Period Ended April 3, 2016	Incurred to Date (in millions)	Total Expected Costs
Asia-Pacific	$ 0.2	$ 4.4	$ 4.7
Americas	0.8	10.2	15.7
Total restructuring costs	**$ 1.0**	**$ 14.6**	**$ 20.4**

Details of the restructuring reserve activity for the Company s Americas and Asia-Pacific 2015 transformation program for the period ended April 3, 2016 are as follows:

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	Severance		Legal and consultancy		Asset write-downs (in millions)		Facility exit and other		Total
Balance at December 31, 2015	$	5.0	$	0.4	$		$	1.0	$	6.4
Net pre-tax restructuring charges		**0.2**		**0.2**		**0.2**		**0.4**		**1.0**
Utilization and foreign currency impact	**$**	**(1.1)**	**$**	**(0.6)**		**(0.2)**		**(0.4)**	**$**	**(2.3)**
Balance at April 3, 2016	**$**	**4.1**	**$**		**$**		**$**	**1.0**	**$**	**5.1**

Other Actions

The Company also periodically initiates other actions which are not part of a major program. In the fourth quarters of 2015 and 2014, management initiated certain restructuring actions and strategic initiatives with respect to the Company s EMEA segment in response to the ongoing economic challenges in Europe and additional product rationalization. The restructuring actions primarily include expected severance benefits and limited costs relating to asset write offs, professional fees and relocation. The 2015 EMEA restructuring action is subject to completion of statutory and labor relations requirements, including consultation with and receipt of advisory opinions from the relevant works councils.

The total pre-tax charge for the 2015 restructuring initiatives is expected to be approximately $10 million, of which approximately $7.0 million was incurred as of April 3, 2016 for the program to date. The remaining expected costs relate to severance, legal and relocation costs and are expected to be completed by the end of the fourth quarter of 2016.

The total pre-tax charge for the 2014 restructuring initiatives is expected to be approximately $8 million, of which approximately $6.7 million was incurred as of April 3, 2016 for the program to date. The remaining costs relate to severance, asset write-offs and relocation costs and are expected to be completed by the end of the fourth quarter of 2016.

The following table summarizes total expected, incurred and remaining pre-tax restructuring costs for the EMEA 2015 restructuring actions:

		Severance		Legal and consultancy (in millions)		Facility exit and other		Total
Costs incurred 2015		6.6				0.3		6.9
Costs incurred first quarter 2016		**0.1**						**0.1**
Remaining costs to be incurred		0.9		2.0		0.1		3.0
Total expected restructuring costs	**$**	**7.6**	**$**	**2.0**	**$**	**0.4**	**$**	**10.0**

Details of the Company s EMEA 2015 restructuring reserve activity for the period ended April 3, 2016 are as follows:

	Severance	Total

		Legal and consultancy	Facility exit and other	
		(in millions)		
Balance at December 31, 2015	$ 6.4	$	$	$ 6.4
Net pre-tax restructuring charges	**0.1**			**0.1**
Utilization and foreign currency impact	**(0.2)**			**(0.2)**
Balance at April 3, 2016	**$ 6.3**	**$**	**$**	**$ 6.3**

The following table summarizes total expected, incurred and remaining pre-tax restructuring costs for the EMEA 2014 restructuring actions:

	Severance	Legal and consultancy	Asset write-downs (in millions)	Facility exit and other	Total
Costs incurred 2014	$ 6.9	$	$	$	$ 6.9
Costs incurred 2015	(1.0)	0.2	0.3		(0.5)
Costs incurred first quarter 2016	**0.2**		**0.1**		**0.3**
Remaining costs to be incurred	0.6		0.6	0.1	1.3
Total expected restructuring costs	**$ 6.7**	**$ 0.2**	**$ 1.0**	**$ 0.1**	**$ 8.0**

Details of the Company s EMEA 2014 restructuring reserve activity for the period ended April 3, 2016 are as follows:

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	Severance	Legal and consultancy	Asset write-downs	Total
		(in millions)		
Balance at December 31, 2015	$ 2.6	$	$	$ 2.6
Net pre-tax restructuring charges	**0.2**		**0.1**	**0.3**
Utilization and foreign currency impact	**(0.9**			