ASHLAND INC.
Form 10-Q
February 08, 2008

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended December 31, 2007

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 1-32532

ASHLAND INC.

(a Kentucky corporation)
I.R.S. No. 20-0865835

50 E. RiverCenter Boulevard
P.O. Box 391
Covington, Kentucky 41012-0391
Telephone Number (859) 815-3333

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 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 þ Accelerated Filer o Non-Accelerated Filer 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 þ

At December 31, 2007, there were 62,902,667 shares of Registrant's Common Stock outstanding.

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ASHLAND INC. AND CONSOLIDATED SUBSIDIARIES
STATEMENTS OF CONSOLIDATED INCOME

(In millions except per share data - unaudited)	Three months ended December 31 2007	2006
SALES AND OPERATING REVENUES	$ 1,905	$ 1,803
COSTS AND EXPENSES		
Cost of sales and operating expenses	1,589	1,489
Selling, general and administrative expenses	281	266
	1,870	1,755
EQUITY AND OTHER INCOME	11	10
OPERATING INCOME	46	58
Net interest and other financing income	12	16
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAXES	58	74
Income taxes - Note H	(20)	(21)
INCOME FROM CONTINUING OPERATIONS	38	53
Loss from discontinued operations (net of income taxes) - Note C	(5)	(4)
NET INCOME	$ 33	$ 49
BASIC EARNINGS PER SHARE - Note I		
Income from continuing operations	$ .61	$ .82
Loss from discontinued operations	(.09)	(.06)
Net income	$ .52	$ .76
DILUTED EARNINGS PER SHARE - Note I		
Income from continuing operations	$ .60	$ .81
Loss from discontinued operations	(.08)	(.06)
Net income	$ .52	$ .75
DIVIDENDS PAID PER COMMON SHARE	$ .275	$ .275

SEE NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.

ASHLAND INC. AND CONSOLIDATED SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

(In millions - unaudited)	December 31 2007	September 30 2007	December 31 2006
ASSETS			
CURRENT ASSETS			
Cash and cash equivalents	$ 681	$ 897	$ 516
Available-for-sale securities	394	155	436
Accounts receivable	1,417	1,508	1,378
Allowance for doubtful accounts	(43)	(41)	(37)
Inventories - Note F	633	610	580
Deferred income taxes	63	69	76
Other current assets	91	78	65
	3,236	3,276	3,014
INVESTMENTS AND OTHER ASSETS			
Goodwill and other intangibles - Note G	380	377	377
Asbestos insurance receivable (noncurrent portion) - Note M	448	458	440
Deferred income taxes	157	157	189
Other noncurrent assets	436	435	443
	1,421	1,427	1,449
PROPERTY, PLANT AND EQUIPMENT			
Cost	2,151	2,125	2,042
Accumulated depreciation and amortization	(1,162)	(1,142)	(1,079)
	989	983	963
	$ 5,646	$ 5,686	$ 5,426
LIABILITIES AND STOCKHOLDERS' EQUITY			
CURRENT LIABILITIES			
Current portion of long-term debt	$ 5	$ 5	$ 7
Trade and other payables	1,036	1,141	1,059
Income taxes	3	6	10
	1,044	1,152	1,076
NONCURRENT LIABILITIES			
Long-term debt (less current portion)	64	64	70
Employee benefit obligations - Note J	262	255	303
Asbestos litigation reserve (noncurrent portion) - Note M	546	560	577
Other noncurrent liabilities and deferred credits	524	501	522
	1,396	1,380	1,472
STOCKHOLDERS' EQUITY	3,206	3,154	2,878
	$ 5,646	$ 5,686	$ 5,426

SEE NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.

ASHLAND INC. AND CONSOLIDATED SUBSIDIARIES
STATEMENTS OF CONSOLIDATED STOCKHOLDERS' EQUITY

(In millions - unaudited)	Common stock	Paid-in capital	Retained earnings	Accumulated other comprehensive income (loss) (a)	Total
BALANCE AT SEPTEMBER 30, 2006	$ 1	$ 240	$ 2,899	$ (44)	$ 3,096
Total comprehensive income (b)			49	11	60
Cash dividends		(1)	(17)		(18)
Issued 492,303 common shares under stock incentive and other plans (c)		28			28
Repurchase of 4,712,000 common shares		(267)	(21)		(288)
BALANCE AT DECEMBER 31, 2006	$ 1	$ -	$ 2,910	$ (33)	$ 2,878
BALANCE AT SEPTEMBER 30, 2007	$ 1	$ 16	$ 3,040	$ 97	$ 3,154
Total comprehensive income (b)			33	36	69
Cash dividends			(17)		(17)
Other			(1)		(1)
Issued 28,662 common shares under stock incentive and other plans (c)		1			1
BALANCE AT DECEMBER 31, 2007	$ 1	$ 17	$ 3,055	$ 133	$ 3,206

(a) At December 31, 2007 and 2006, the accumulated other comprehensive income (after-tax) of $133 million for 2007 and loss (after-tax) of $33 million for 2006 was comprised of pension and postretirement obligations of $55 million for 2007 and a minimum pension liability of $113 million for 2006, net unrealized translation gains of $189 million for 2007 and $81 million for 2006, and net unrealized losses on cash flow hedges of $1 million for 2007 and a net unrealized gain of $1 million for 2006.

(b) Reconciliations of net income to total comprehensive income follow.

(In millions - unaudited)	Three months ended December 31 2007		2006
Net income	$ 33		$ 49
Unrealized translation adjustments	36		9
Related tax benefits	-		1
Net unrealized gains on cash flow hedges	-		1
Total comprehensive income	$ 69		$ 60

(c) Includes income tax benefits resulting from the exercise of stock options of $8 million in fiscal year 2007.

SEE NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.

ASHLAND INC. AND CONSOLIDATED SUBSIDIARIES
STATEMENTS OF CONSOLIDATED CASH FLOWS

(In millions - unaudited)	Three months ended December 31 2007	2006
CASH FLOWS FROM OPERATING ACTIVITIES FROM CONTINUING OPERATIONS		
Net income	$ 33	$ 49
Loss from discontinued operations (net of income taxes)	5	4
Adjustments to reconcile income from continuing operations to cash flows from operating activities		
Depreciation and amortization	34	28
Deferred income taxes	4	11
Equity income from affiliates	(4)	(4)
Distributions from equity affiliates	2	2
Change in operating assets and liabilities (a)	(5)	(212)
	69	(122)
CASH FLOWS FROM FINANCING ACTIVITIES FROM CONTINUING OPERATIONS		
Proceeds from issuance of common stock	2	13
Excess tax benefits related to share-based payments	1	6
Repayment of long-term debt	-	(5)
Repurchase of common stock	-	(288)
Cash dividends paid	(17)	(692)
	(14)	(966)
CASH FLOWS FROM INVESTING ACTIVITIES FROM CONTINUING OPERATIONS		
Additions to property, plant and equipment	(42)	(35)
Purchase of operations - net of cash acquired	(3)	(73)
Purchases of available-for-sale securities	(356)	(286)
Proceeds from sales and maturities of available-for-sale securities	117	207
Other items	16	2
	(268)	(185)
CASH USED BY CONTINUING OPERATIONS	(213)	(1,273)
Cash used by discontinued operations		
Operating cash flows	(3)	(4)
Investing cash flows	-	(27)
DECREASE IN CASH AND CASH EQUIVALENTS	(216)	(1,304)
CASH AND CASH EQUIVALENTS - BEGINNING OF PERIOD	897	1,820
CASH AND CASH EQUIVALENTS - END OF PERIOD	$ 681	$ 516

(a) Excludes changes resulting from operations acquired or sold.

SEE NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS.

ASHLAND INC. AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE A – BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial reporting and Securities and Exchange Commission regulations. In the opinion of management all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. These condensed consolidated financial statements should be read in conjunction with Ashland's Annual Report on Form 10-K for the fiscal year ended September 30, 2007. Results of operations for the period ended December 31, 2007, are not necessarily indicative of results to be expected for the year ending September 30, 2008. Certain prior period data has been reclassified in the condensed consolidated financial statements and accompanying footnotes to conform to current period presentation. Equity and other income, which previously had been classified within the revenue caption of the Statements of Consolidated Income, has been combined and reclassified as a separate caption above operating income within this financial statement.

The preparation of Ashland's condensed consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and the disclosures of contingent assets and liabilities. Significant items that are subject to such estimates and assumptions include, but are not limited to, long-lived assets, employee benefit obligations, income taxes, reserves and associated receivables for asbestos litigation and environmental remediation. Although management bases its estimates on historical experience and various other assumptions that are believed to be reasonable under the circumstances, actual results could differ significantly from the estimates under different assumptions or conditions.

NOTE B – NEW ACCOUNTING STANDARDS

In June 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with Financial Accounting Standard No. 109 (FAS 109), "Accounting for Income Taxes." FIN 48 prescribes a recognition threshold and measurement attributes for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. Ashland adopted the provisions of FIN 48 effective October 1, 2007. The cumulative effect of adoption of FIN 48 resulted in a reduction to the October 1, 2007 opening retained earnings balance of less than $1 million. For additional information on the adoption and implementation of this Interpretation see Note H.

In September 2006, the FASB issued Financial Accounting Standard No. 157 (FAS 157), "Fair Value Measurements," which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements since the FASB has previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. FAS 157 becomes effective for Ashland on October 1, 2008. Ashland is currently in the process of determining the effect, if any, the adoption of FAS 157 will have on the condensed consolidated financial statements.

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ASHLAND INC. AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE C – DISCONTINUED OPERATIONS

On August 28, 2006, Ashland completed the sale of the stock of its wholly owned subsidiary, Ashland Paving And Construction, Inc. (APAC) to Oldcastle Materials, Inc. (Oldcastle) for $1.3 billion. The operating results and assets and liabilities related to APAC have been previously reflected as discontinued operations in the condensed consolidated financial statements. Ashland has made adjustments to the gain on sale of APAC, relating to the tax effects of the sale, during the three months ended December 31, 2007 and 2006. Such adjustments may continue to occur in future periods. Adjustments to the gain are reflected in the period they are determined and recorded in the discontinued operations caption in the Statements of Consolidated Income.

Components of amounts in the Statements of Consolidated Income related to discontinued operations are presented in the following table for the three months ended December 31, 2007 and 2006.

	Three months ended December 31	
(In millions)	2007	2006
Loss on disposal of discontinued operations (net of income taxes)		
APAC	$ (5)	$ (4)

NOTE D – ACQUISITIONS AND DIVESTITURES

Acquisitions

In December 2006, Ashland Specialty Polymers and Adhesives, a business unit of Performance Materials, acquired Northwest Coatings of Oak Creek, Wisconsin, a formulator and manufacturer of adhesives and coatings employing ultraviolet and electron beam (UV/EB) polymerization technologies from Caltius Equity Partners. The transaction, which includes production facilities in Milwaukee, Wisconsin and Greensboro, North Carolina, was valued at $74 million. At the time this purchase transaction was announced, Northwest Coatings had trailing twelve month sales of approximately $40 million.

Divestitures

On August 28, 2006, Ashland completed the sale of the stock of its wholly owned subsidiary, APAC, to Oldcastle. The operating results and assets and liabilities related to APAC have been previously reflected as discontinued operations in the condensed consolidated financial statements. For further information on this transaction see Note C.

As a result of the APAC divestiture certain identified remaining corporate costs that had been previously allocated to this business needed to be eliminated to maintain Ashland's overall competitiveness. Consequently, during fiscal year 2007 Ashland offered an enhanced early retirement or voluntary severance opportunity to administrative and corporate employees. In total, Ashland accepted voluntary severance offers from 172 employees under the program. As a result, a $25 million pretax charge was recorded for severance, pension and other postretirement benefit costs during the March 2007 quarter. This cost was classified in the selling, general and administrative expense caption of the Statements of Consolidated Income and grouped within "Unallocated and other" for segment presentation purposes. The termination dates for employees participating in the program was substantially completed by the end of the December 2007 quarter. As of December 31, 2007, the remaining liability was less than $1 million.

On June 30, 2005, Ashland completed the transfer of its 38% interest in Marathon Ashland Petroleum LLC (MAP) and two other businesses to Marathon Oil Corporation (Marathon) in a transaction valued at approximately $3.7 billion (the "MAP Transaction").

ASHLAND INC. AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE E – DEBT

In April 2007, Ashland replaced its revolving credit agreement with a new five year revolving credit facility which provides for up to $300 million in borrowings. Up to an additional $100 million in borrowings is available with the consent of one or more of the lenders. The borrowing capacity under this new facility was reduced by $101 million for letters of credit outstanding under the credit agreement at December 31, 2007. The revolving credit agreement contains a covenant limiting the total debt Ashland may incur from all sources as a function of Ashland's stockholders' equity. The covenant's terms would have permitted Ashland to borrow $4.7 billion at December 31, 2007, in addition to the actual total debt incurred at that time. Permissible total Ashland debt under the covenant's terms increases (or decreases) by 150% for any increase (or decrease) in stockholders' equity.

In previous periods Ashland entered into in-substance defeasance investments of approximately $57 million to repay current and long-term debt that had a carrying value of $49 million on the Condensed Consolidated Balance Sheet. Because the transactions were not a legal defeasance, the investments have been placed into a trust that is exclusively restricted to future obligations and repayments related to these debt instruments. The investments have been classified on the Condensed Consolidated Balance Sheet as other current assets or other noncurrent assets based on the contractual debt repayment schedule. At December 31, 2007, September 30, 2007 and December 31, 2006, the carrying value of the investments to defease debt was $39 million, $40 million and $45 million, respectively. The carrying value of the debt was $34 million, $34 million and $39 million as of December 31, 2007, September 30, 2007 and December 31, 2006, respectively.

NOTE F – INVENTORIES

Inventories are carried at the lower of cost or market. Certain chemicals, plastics and lubricants are valued at cost using the last-in, first-out (LIFO) method. The remaining inventories are stated at cost using the first-in, first-out (FIFO) method or average cost method (which approximates FIFO). The following table summarizes Ashland's inventories as of the reported Condensed Consolidated Balance Sheet dates.

(In millions)	December 31 2007	September 30 2007	December 31 2006
Chemicals and plastics	$ 663	$ 625	$ 577
Lubricants	89	86	94
Other products and supplies	49	54	53
Excess of replacement costs over LIFO carrying values	(168)	(155)	(144)
	$ 633	$ 610	$ 580

NOTE G – GOODWILL AND OTHER INTANGIBLES

In accordance with Financial Accounting Standard No. 142 (FAS 142), “Goodwill and Other Intangible Assets,” Ashland conducts an annual review for impairment. Impairment is to be examined more frequently if certain indicators are encountered. In accordance with FAS 142, Ashland reviewed goodwill for impairment based on reporting units, which are defined as operating segments or groupings of businesses one level below the operating segment level. Ashland has completed its most recent annual goodwill impairment test required by FAS 142 as of July 1, 2007 and has determined that no impairment exists. The following is a progression of goodwill by segment for the three months ended December 31, 2007 and 2006.

ASHLAND INC. AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE G – GOODWILL AND OTHER INTANGIBLES (continued)

(In millions)	Performance Materials	Distribution	Valvoline	Water Technologies	Total
Balance at September 30, 2007	$ 166	$ 1	$ 30	$ 71	$ 268
Currency translation adjustment	3	-	-	1	4
Balance at December 31, 2007	$ 169	$ 1	$ 30	$ 72	$ 272

(In millions)	Performance Materials	Distribution	Valvoline	Water Technologies	Total
Balance at September 30, 2006	$ 110	$ 1	$ 29	$ 70	$ 210
Acquisitions	47	-	-	1	48
Currency translation adjustment	1	-	-	1	2
Balance at December 31, 2006	$ 158	$ 1	$ 29	$ 72	$ 260

Intangible assets consist of trademarks and trade names, patents and licenses, non-compete agreements, sale contracts, customer lists and intellectual property. Intangibles are amortized on a straight-line basis over their estimated useful lives. The cost of trademarks and trade names is amortized principally over 10 to 25 years, intellectual property over 5 to 17 years and other intangibles over 3 to 30 years. Ashland reviews intangible assets for possible impairment whenever events or changes in circumstances indicate that carrying amounts may not be recoverable.

Intangible assets were comprised of the following as of December 31, 2007 and 2006.

	2007			2006		
(In millions)	Gross carrying amount	Accumulated amortization	Net carrying amount	Gross carrying amount	Accumulated amortization	Net carrying amount
Trademarks and trade names	$ 63	$ (20)	$ 43	$ 62	$ (21)	$ 41
Intellectual property	49	(18)	31	40	(6)	34
Other intangibles	49	(15)	34	52	(10)	42
Total intangible assets	$ 161	$ (53)	$ 108	$ 154	$ (37)	$ 117

Amortization expense recognized on intangible assets for the three months ended December 31 was $3 million for 2007 and $3 million for 2006. As of December 31, 2007, all of Ashland's intangible assets that had a carrying value were being amortized except for certain trademarks and trade names that currently have been determined to have indefinite lives. These assets had a balance of $32 million as of December 31, 2007 and 2006. In accordance with FAS 142, Ashland annually reviews these assets to determine whether events and circumstances continue to support the indefinite useful life. Estimated amortization expense for future periods is $10 million in 2008 (includes three months actual and nine months estimated), $10 million in 2009, $7 million in 2010, $6 million in 2011 and $6 million in 2012.

ASHLAND INC. AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE H – INCOME TAXES

Ashland adopted the provisions of FIN 48 as of October 1, 2007. The cumulative effect of adoption of FIN 48 resulted in a reduction to the October 1, 2007 opening retained earnings balance of less than $1 million. FIN 48 prescribes a recognition threshold and measurement attribute for the accounting and financial statement disclosure of tax positions taken or expected to be taken in a tax return. The evaluation of a tax position is a two-step process. The first step requires Ashland to determine whether it is more likely than not that a tax position will be sustained upon examination based on the technical merits of the position. The second step requires Ashland to recognize in the financial statements each tax position that meets the more likely than not criteria, measured at the largest amount of benefit that has a greater than fifty percent likelihood of being realized. As of October 1, 2007, the amount of unrecognized tax benefits was $57 million, of which $30 million related to discontinued operations. The total amount of unrecognized tax benefits that, if recognized, would affect the effective tax rate is $25 million. The total amount of unrecognized tax benefits that, if recognized, would affect results from discontinued operations is $18 million.

Ashland recognizes interest and penalties related to unrecognized tax benefits as a component of income tax expense in the Statements of Consolidated Income. Ashland had approximately $15 million in interest and penalties related to unrecognized tax benefits accrued as of October 1, 2007.

Ashland or one of its subsidiaries files income tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. Foreign taxing jurisdictions significant to Ashland include Australia, Canada and the Netherlands. Ashland is subject to U.S. federal or state income tax examinations by tax authorities for periods after July 1, 2005. With respect to countries outside of the United States, with certain exceptions, Ashland’s foreign subsidiaries are subject to income tax audits for years after 1999.

It is reasonably possible that the amount of the unrecognized tax benefits may increase or decrease within the next 12 months as the result of settlement of ongoing audits. However, Ashland does not presently anticipate that any increase or decrease in unrecognized tax benefits will be material to the condensed consolidated financial statements.

During the three month period ended December 31, 2007, Ashland increased its liability for unrecognized tax benefits by $5 million attributable to adjustments in the tax basis of previously discontinued operations. There have been no other significant changes to the liability for unrecognized tax benefits or potential interest and penalties recorded during the quarter ended December 31, 2007.

As a result of the structure of the MAP Transaction, Marathon became primarily responsible for certain of Ashland’s federal and state tax obligations for positions taken prior to June 30, 2005. However, pursuant to the terms of the Tax Matters Agreement, Ashland has agreed to indemnify Marathon for any obligations which arise from those positions. Upon adoption of FIN 48, these positions, which were previously accounted for as income tax contingencies by Ashland, are no longer treated in that manner under the provisions of FIN 48. Subsequent adjustments to these liabilities will be recorded as a component of selling, general and administrative expenses within the Statements of Consolidated Income. In accordance with the prospective adoption requirements under the provisions of FIN 48, Ashland did not reclassify prior period expenses relating to these items that would have been classified within the selling, general and administrative caption if FIN 48 was applied retrospectively. For the three months ended December 31, 2007, Ashland recorded $1 million of expense relating to these items that was previously recognized as a component of income tax expense in previous periods.

ASHLAND INC. AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE I – EARNINGS PER SHARE

Following is the computation of basic and diluted earnings per share (EPS) from continuing operations.

(In millions except per share data)	Three months ended December 31 2007	2006
Numerator		
Numerator for basic and diluted EPS – Income from continuing operations	$ 38	$ 53
Denominator		
Denominator for basic EPS – Weighted average common shares outstanding	63	64
Common shares issuable upon exercise of stock options and stock appreciation rights	1	1
Denominator for diluted EPS – Adjusted weighted average shares and assumed conversions	64	65
EPS from continuing operations		
Basic	$ .61	$ .82
Diluted	$ .60	$ .81

NOTE J – EMPLOYEE BENEFIT PLANS

Presently, Ashland anticipates contributing $9 million to its non-U.S. pension plans and does not expect to contribute to its U.S. pension plans during fiscal 2008. As of December 31, 2007, contributions of $1 million have been made to the non-U.S. plans and no contribution has been made to the U.S. plans. The following table details the components of pension and other postretirement benefit costs.

	Pension benefits		Other postretirement benefits	
(In millions)	2007	2006	2007	2006
Three months ended December 31				
Service cost	$ 9	$ 9	$ 2	$ 1
Interest cost	22	19	5	3
Expected return on plan assets	(26)	(21)	-	-
Amortization of prior service credit	-	-	(2)	(1)
Amortization of net actuarial loss (gain)	1	5	(3)	-
	$ 6	$ 12	$ 2	$ 3

NOTE K – CAPITAL STOCK

On September 14, 2006 Ashland's Board of Directors authorized the distribution of a substantial portion of the proceeds of the sale of APAC to the shareholders of Ashland as a one-time special dividend. Each shareholder of record as of October 10, 2006 received $10.20 per share, for a total of $674 million, which was paid on October 25, 2006. Substantially all of the remaining proceeds were directed to be used to repurchase Ashland Common Stock in accordance with the terms authorized by Ashland's Board of Directors and as further described below.

Stock repurchases were made pursuant to two different programs authorized by Ashland's Board of Directors. The first program, originally approved on July 21, 2005, authorized the purchase of $270 million of Ashland Common Stock in the open market. After 3.5 million shares at a cost of $196 million had been purchased under the initial authorization, on January 25, 2006, Ashland's Board of Directors increased the remaining authorization by $176 million to $250 million. As of September 14, 2006, Ashland had completed all repurchases to be made under this program.

ASHLAND INC. AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE K – CAPITAL STOCK (continued)

The second program was authorized by Ashland's Board of Directors on September 14, 2006, employing the remaining after-tax proceeds from the sale of APAC to repurchase up to an additional 7 million shares. To facilitate this repurchase program, Ashland entered into a stock trading plan with Credit Suisse Securities (USA) LLC (Credit Suisse). The stock trading plan, amended and restated on September 20, 2006, allowed Credit Suisse to make daily repurchases of stock starting on October 2, 2006, in accordance with the instructions set forth in the filed plan and within the safe harbor from insider trading liability provided under Exchange Act Rule 10b5-1.

Ashland repurchased 4.7 million shares for $288 million in the December 2006 quarter. Since the inception of the first described share repurchase program on July 21, 2005 through the completion of the second share repurchase program on December 19, 2006, Ashland repurchased a total of 13.2 million shares at a cost of $793 million. These repurchases represented approximately 18% of shares outstanding on June 30, 2005. The stock repurchase actions were consistent with certain representations of intent made to the Internal Revenue Service with respect to the transfer of MAP.

NOTE L – STOCK OPTIONS

Ashland has stock incentive plans under which key employees or directors are granted stock options, stock-settled stock appreciation rights (SARs) or nonvested stock awards. Each program is typically a long-term incentive plan designed to link employee compensation with increased shareholder value over time or reward superior performance and encourage continued employment with Ashland. Ashland began expensing stock awards on October 1, 2002 in accordance with Financial Accounting Standard No. 123 (FAS 123), "Accounting for Stock-Based Compensation" which was subsequently superseded by Financial Accounting Standard No. 123(R) (FAS 123(R)), "Share-Based Payment," and recognizes compensation expense for the grant date fair value of stock-based awards over the applicable vesting period. Stock-based compensation expense was $2 million for each of the three month periods ended December 31, 2007 and 2006, respectively, and is included in the selling, general and administrative expense caption of the Statements of Consolidated Income.

Stock options and SARs

Stock options and SARs are granted to employees or directors at a price equal to the fair market value of the stock on the date of grant and become exercisable over periods of one to three years. Unexercised stock options and SARs lapse ten years after the date of grant. SARs granted for the three months ended December 31, 2007 and 2006 were 0.4 million and 0.5 million, respectively. As of December 31, 2007 there was $11 million of total unrecognized compensation costs related to stock options and SARs. That cost is expected to be recognized over a weighted-average period of 2.2 years. In accordance with FAS 123(R) Ashland estimates the fair value of stock options and SARs granted using the Black-Scholes option-pricing model. This model requires several assumptions, which Ashland has developed and updates based on historical trends and current market observations. The accuracy of these assumptions is critical to the estimate of fair value for these equity instruments.

Nonvested stock awards

Nonvested stock awards are granted to employees or directors at a price equal to the fair market value of the stock on the date of grant and generally vest over a one to seven year period. However, such shares are subject to forfeiture upon termination of service before the vesting period ends. Nonvested stock awards entitle employees or directors to vote the shares and to receive any dividends upon grant. Nonvested stock awards granted for the three months ended December 31, 2007 and 2006 were less than 3,000 shares for each period. As of December 31, 2007 there was $4 million of total unrecognized compensation costs related to nonvested stock awards. That cost is expected to be recognized over a weighted-average period of 2.6 years.

ASHLAND INC. AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE M – LITIGATION, CLAIMS AND CONTINGENCIES

Asbestos-related litigation

Ashland is subject to liabilities from claims alleging personal injury caused by exposure to asbestos. Such claims result primarily from indemnification obligations undertaken in 1990 in connection with the sale of Riley Stoker Corporation (Riley), a former subsidiary. Although Riley was neither a producer nor a manufacturer of asbestos, its industrial boilers contained some asbestos-containing components provided by other companies.

Because claims are frequently filed and settled in large groups, the amount and timing of settlements and number of open claims can fluctuate significantly from period to period. Since October 1, 2004, Riley has been dismissed as a defendant in 88% of the resolved claims. New claims filed for the three months ended December 31, 2007 and 2006 were 589 and 1,077 claims, respectively. A summary of asbestos claims activity follows.

	Three months ended December 31		Years ended September 30		
(In thousands)	2007	2006	2007	2006	2005
Open claims - beginning of period	134	162	162	184	196
New claims filed	1	1	4	6	12
Claims settled	(1)	-	(2)	(3)	(6)
Claims dismissed	(14)	(12)	(30)	(25)	(18)
Open claims - end of period	120	151	134	162	184

A progression of activity in the asbestos reserve is presented in the following table.

	Three months ended December 31		Years ended September 30		
(In millions)	2007	2006	2007	2006	2005
Asbestos reserve - beginning of period	$ 610	$ 635			