UST INC
Form 10-Q
May 04, 2006

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549-1004
FORM 10-Q

(Mark One)

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

For quarterly period ended March 31, 2006

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 0-17506
UST Inc.
(Exact name of registrant as specified in its charter)

Delaware	06-1193986
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
100 West Putnam Avenue, Greenwich, CT	06830
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code: (203) 661-1100
NONE
(Former name, former address and former fiscal year, if changed since last report.)

Indicate by check mark whether 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 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

Number of Common shares ($.50 par value) outstanding at April 28, 2006 161,394,854

UST Inc.
(Registrant or the Company)
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Part I. FINANCIAL INFORMATION
Item 1. FINANCIAL STATEMENTS
UST Inc.
CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION
(Dollars in thousands, except per share data)

	March 31, 2006 (Unaudited)	December 31, 2005 (Note)
Assets:		
Current assets:		
Cash and cash equivalents	$ 200,072	$ 202,025
Short-term investments		10,000
Accounts receivable	47,064	54,186
Inventories:		
Leaf tobacco	201,292	202,553
Products in process	200,176	203,396
Finished goods	150,552	156,343
Other materials and supplies	23,128	21,115
Total inventories	575,148	583,407
Deferred income taxes	10,150	11,622
Income taxes receivable		2,400
Assets held for sale		3,433
Prepaid expenses and other current assets	25,903	22,481
Total current assets	858,337	889,554
Property, plant and equipment, net	423,829	431,168
Other assets	42,873	46,261
Total assets	$ 1,325,039	$ 1,366,983
Liabilities and Stockholders Equity:		
Current liabilities:		
Accounts payable and accrued expenses	$ 140,864	$ 231,061
Income taxes payable	78,202	12,566
Litigation liability	16,070	15,151
Total current liabilities	235,136	258,778
Long-term debt	840,000	840,000
Postretirement benefits other than pensions	86,437	85,819
Pensions	94,036	92,159
Deferred income taxes	9,212	11,972
Other liabilities	4,187	3,157
Total liabilities	1,269,008	1,291,885
Contingencies (see Note 12)		

Stockholders equity:				
Capital stock[(1)]		103,885		103,810
Additional paid-in capital		952,283		945,466
Retained earnings		521,000		497,389
Accumulated other comprehensive loss		(17,349)		(17,802)
		1,559,819		1,528,863
Less treasury stock 46,293,878 shares in 2006 and 45,049,378 shares in 2005		1,503,788		1,453,765
Total stockholders equity		56,031		75,098
Total liabilities and stockholders equity	$	1,325,039	$	1,366,983

(1) Common Stock par value $.50 per share: Authorized 600 million shares; Issued 207,770,982 shares in 2006 and 207,620,439 shares in 2005. Preferred Stock par value $.10 per share: Authorized 10 million shares; Issued None.

Note: The Condensed Consolidated Statement of Financial Position at December 31, 2005 has been derived from the audited financial statements at that date.

See Notes to Condensed Consolidated Financial Statements.

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UST Inc.
CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS
(In thousands, except per share amounts)
(Unaudited)

	Three Months Ended March 31,	
	2006	2005
Net sales	$ 433,641	$ 440,527
Costs and expenses:		
Cost of products sold	92,191	88,923
Excise taxes	12,019	11,481
Selling, advertising and administrative	131,708	135,807
Antitrust litigation	1,350	
Total costs and expenses	237,268	236,211
Operating income	196,373	204,316
Interest, net	11,470	16,391
Earnings before income taxes	184,903	187,925
Income tax expense	68,990	66,093
Net earnings	$ 115,913	$ 121,832
Net earnings per share:		
Basic	$ .72	$ .74
Diluted	$ .71	$ .73
Dividends per share	$ .57	$ .55
Average number of shares:		
Basic	161,602	164,766
Diluted	162,649	167,022

See Notes to Condensed Consolidated Financial Statements.

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UST Inc.
CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS
(In thousands)
(Unaudited)

	Three Months Ended March 31,	
	2006	2005
Operating Activities:		
Net earnings	$ 115,913	$ 121,832
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	11,346	11,026
Share-based compensation expense	1,860	1,919
Excess tax benefits from share-based compensation	(282)	
(Gain) loss on disposition of property, plant and equipment	(2,372)	339
Deferred income taxes	(1,533)	(3,133)
Changes in operating assets and liabilities:		
Accounts receivable	7,122	(843)
Inventories	8,259	601
Prepaid expenses and other assets	1,148	2,018
Accounts payable, accrued expenses, pensions and other liabilities	(86,049)	(80,174)
Income taxes	68,446	34,746
Litigation liability	919	(2,057)
Net cash provided by operating activities	124,777	86,274
Investing Activities:		
Short-term investments, net	10,000	60,000
Purchases of property, plant and equipment	(4,763)	(13,564)
Proceeds from dispositions of property, plant and equipment	5,957	40
Investment in joint venture	(578)	
Net cash provided by investing activities	10,616	46,476
Financing Activities:		
Repayment of debt		(300,000)
Proceeds from the issuance of stock	4,594	51,130
Excess tax benefits from share-based compensation	282	
Dividends paid	(92,199)	(91,003)
Stock repurchased	(50,023)	(50,000)
Net cash used in financing activities	(137,346)	(389,873)
Decrease in cash and cash equivalents	(1,953)	(257,123)
Cash and cash equivalents at beginning of year	202,025	450,202

Cash and cash equivalents at end of the period	$ 200,072	$ 193,079
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Income taxes	$ 3,948	$ 34,886
Interest	$ 19,875	$ 33,075

See Notes to Condensed Consolidated Financial Statements.

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UST Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2006
(Unaudited)
(In thousands, except per share amounts or where otherwise noted)

1 BASIS OF PRESENTATION

The accompanying unaudited condensed 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 issued by the U.S. Securities and Exchange Commission. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles (GAAP) for complete financial statements. Management believes that all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The condensed consolidated financial statements include the accounts of the Company and all of its subsidiaries after the elimination of intercompany accounts and transactions. Certain prior year amounts on the Condensed Consolidated Statement of Cash Flows have been reclassified to conform to the 2006 financial statement presentation. Operating results for the three month period ended March 31, 2006 are not necessarily indicative of the results that may be expected for the year ended December 31, 2006. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2005 (2005 Form 10-K).

2 RECENT ACCOUNTING PRONOUNCEMENTS

In May 2005, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 154, *Accounting Changes and Error Corrections a replacement of APB Opinion No. 20 and FASB Statement No. 3* (SFAS No. 154). The pronouncement requires that all voluntary changes in accounting principle be reported by retrospectively applying the principle to all prior periods that are presented in the financial statements. The Company adopted the provisions of SFAS No. 154 on January 1, 2006, as required. The adoption of SFAS No. 154 did not have an impact on the Company s consolidated financial statements.

In December 2004, the FASB issued SFAS No. 123(R), *Share-Based* Payment (SFAS No. 123(R)) which is a revision of SFAS No. 123, *Accounting for Stock-Based Compensation*, (SFAS No. 123). SFAS No. 123(R) supersedes Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees* (APB Opinion No. 25), and amends SFAS No. 95, *Statement of Cash Flows*. The Company adopted the provisions of SFAS No. 123(R) on January 1, 2006, as required. See Note 4, Share-Based Compensation for more details.

In November 2004, the FASB issued SFAS No. 151, *Inventory Costs an amendment of ARB No. 43, Chapter 4* (SFAS No. 151). SFAS No. 151 amends the guidance in Accounting Research Bulletin No. 43, Chapter 4, Inventory Pricing, to clarify the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material, or spoilage, and requires these costs be treated as current period charges. In addition, SFAS No. 151 requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. The Company adopted the provisions of SFAS No. 151 on January 1, 2006, as required. The adoption of SFAS No. 151 did not have an impact on the Company s consolidated financial statements.

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UST Inc.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

3 CAPITAL STOCK

The Company repurchased approximately 1.2 million shares of outstanding common stock at a cost of approximately $50 million during the three months ended March 31, 2006. The repurchases were made pursuant to the Company s authorized program, approved in December 2004, to repurchase up to 20 million shares of its outstanding common stock. As of March 31, 2006, approximately 4 million shares have been repurchased at a cost of approximately $167 million under the program.

4 SHARE-BASED COMPENSATION

On January 1, 2006, the Company adopted the provisions of SFAS No. 123(R). The approach in SFAS No. 123(R) is similar to the approach described in SFAS No. 123; however, SFAS No. 123(R) requires all share-based payments issued to acquire goods or services, including grants of employee stock options, to be recognized in the statement of operations based on their fair values, net of estimated forfeitures. SFAS No. 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. In the Company s pro forma disclosure required under SFAS No. 123 for the periods prior to adoption of SFAS No. 123(R), the Company accounted for forfeitures as they occurred. Pro forma disclosure, as allowed under SFAS No. 123, is no longer an alternative. The Company has elected the modified prospective transition method as permitted by SFAS No. 123(R), in which compensation cost is recognized beginning with the effective date based on the requirements of SFAS No. 123(R) for all share-based payments granted after January 1, 2006, and based on the requirements of SFAS No. 123 for all awards granted to employees prior to that date that remained unvested upon adoption of SFAS No. 123(R). Compensation expense related to share-based awards is recognized over the requisite service period, which is generally the vesting period. The amount of incremental compensation expense recognized relating to stock options as a result of the adoption of SFAS No. 123(R) for the three months ended March 31, 2006 was not material.

Prior to the adoption of SFAS No. 123(R), the Company presented all tax benefits for deductions resulting from the exercise of stock options as operating cash flows on its Condensed Consolidated Statement of Cash Flows. SFAS No. 123(R) requires the benefits of tax deductions in excess of recognized compensation expense, or the pro forma compensation expense that would have been recognized under SFAS No. 123 in the case of stock options granted prior to January 1, 2006, to be reported as a financing cash inflow, rather than as an operating cash inflow. This requirement reduces net operating cash flows and increases net financing cash flows. Total cash flow does not differ from what would have been reported under prior accounting guidance.

Prior to the adoption of SFAS No. 123(R), the Company accounted for share-based compensation awards to employees and non-employee directors in accordance with the intrinsic value-based method prescribed by APB Opinion No. 25, as permitted under Statement No. 123. Under the intrinsic value-based method, no share-based compensation expense was reflected in net earnings as a result of stock option grants, as all options granted under these plans had an exercise price equal to the fair market value of the underlying common stock on the date of grant. Compensation expense was recognized in net earnings during the three months ended March 31, 2005 as a result of restricted stock granted to employees and non-employee directors and restricted stock units granted to UST Inc. employees.

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UST Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
4 SHARE-BASED COMPENSATION (Continued)

As the Company did not account for share-based compensation awards under the fair value method prior to January 1, 2006, the following table illustrates the effect of applying the fair value method on net earnings and net earnings per share for the three months ended March 31, 2005 as prescribed in SFAS No. 123:

		Three Months Ended March 31, 2005
Net Earnings:		
As reported	$	121,832
Add: Total share-based employee compensation expense included in reported net income, net of related tax effect		1,282
Deduct: Total share-based employee compensation expense determined under the fair value method for all awards, net of related tax effect		(1,307)
Pro forma	$	121,807
Basic net earnings per share:		
As reported	$	.74
Pro forma	$	.74
Diluted net earnings per share:		
As reported	$	.73
Pro forma	$	.73

Total pre-tax share-based compensation expense for each of the three months ended March 31, 2006 and 2005 was $1.9 million, respectively. Of the total $1.9 million of share-based compensation expense recognized for the three months ended March 31, 2006, approximately $1.8 million was recognized in selling, advertising and administrative (SA&A) expenses, $0.1 million was recognized in cost of goods sold and an inconsequential amount was capitalized as part of inventory. The entire $1.9 million of share-based compensation expense recognized for the three months ended March 31, 2005 was included in SA&A expenses. The income tax benefit related to share-based compensation expense was $0.7 million for each of the three months ended March 31, 2006 and 2005.

The Company maintains the following five equity compensation plans (1) the UST Inc. 2005 Long Term Incentive Plan (2005 LTIP), (2) the UST Inc. Amended and Restated Stock Incentive Plan, (3) the UST Inc. 1992 Stock Option Plan, (4) the Nonemployee Directors Stock Option Plan, and (5) the Nonemployee Directors Restricted Stock Award Plan. In May 2005, the Company authorized that 10 million shares of its common stock be reserved for issuance under the 2005 LTIP, which was approved by stockholders at the Company s Annual Meeting on May 3, 2005. Subsequent to that date, all share-based awards were issued from the 2005 LTIP, as the UST Inc. Amended and Restated Stock Incentive Plan, the Nonemployee Directors Stock Option Plan and the Nonemployee Directors Restricted Stock Award Plan are considered to be inactive. Forfeitures of share-based awards granted from these inactive plans are transferred into the 2005 LTIP as they occur, and are considered available for future issuance under the 2005 LTIP. Share-based awards are generally in the form of common shares, stock options, restricted stock or restricted stock units. Share-based awards granted under the

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UST Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
4 SHARE-BASED COMPENSATION (Continued)

2005 LTIP vest over a period determined by the Compensation Committee of the Board of Directors and in the case of stock option awards, may be exercised up to a maximum of ten years from the date of grant. Under the UST Inc. Amended and Restated Stock Incentive Plan and the UST Inc. 1992 Stock Option Plan, share-based awards vest, in ratable installments or otherwise, over a period of one to five years from the date of grant and, in the case of stock option awards, may be exercised up to a maximum of ten years from the date of grant using various payment methods. Under the Nonemployee Directors Stock Option Plan, options first become exercisable six months from the date of grant and may be exercised up to a maximum of ten years from the date of grant. In certain instances, awards of restricted stock or restricted stock units are subject to performance conditions related to the Company s earnings.

Stock Options

On December 8, 2005, the Board of Directors of the Company, upon the recommendation of its Compensation Committee, approved the acceleration of vesting of all outstanding, unvested stock options previously awarded to the Company s employees and officers, including executive officers, under the UST Inc. Amended and Restated Stock Incentive Plan and the UST Inc. 1992 Stock Option Plan. As a result of the acceleration, stock options to acquire approximately 1.1 million shares of the Company s common stock became exercisable on December 31, 2005. In order to prevent unintended personal benefits to the Company s officers, the accelerated vesting was conditioned on such officers entering into amendments to their original option award agreements providing that such officers will not, subject to limited exceptions, sell, transfer, assign, pledge or otherwise dispose of any shares acquired upon exercising the accelerated portion of the options before the earlier of the date on which that portion of options would have otherwise vested under the original terms of the applicable option agreements or separation from service. All other terms related to these stock options were not affected by this acceleration. As a result of the acceleration of these options, the Company will avoid recognizing approximately $3 million in 2006 and $0.5 million in 2007 in pre-tax incremental compensation expense in its Consolidated Statements of Operations associated with these options.

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UST Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
4 SHARE-BASED COMPENSATION (Continued)

The following table presents a summary of the Company s stock option activity and related information for the three months ended March 31, 2006 (options in thousands):

	Three Months Ended March 31, 2006			
	Number of Options	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2006	6,845.6	$ 32.13		
Granted				
Exercised	148.5	$ 29.65		
Forfeited	1.1	$ 33.25		
Expired				
Outstanding at March 31, 2006	6,696.0	$ 32.19	4.82 years	$62.3 million
Exercisable at March 31, 2006	6,646.0	$ 32.14	4.79 years	$62.2 million

The fair value of each option grant was estimated on the date of grant using the Black-Scholes-Merton option pricing model, which incorporates various assumptions including expected volatility, expected dividend yield, expected life and applicable interest rates. The expected volatility is based upon the historical volatility of the Company s common stock over the most recent period commensurate with the expected life of the applicable stock options, adjusted for the impact of unusual fluctuations not reasonably expected to recur. The expected life of stock options is estimated based upon historical exercise data for previously awarded options, taking into consideration the vesting period and contractual lives of the applicable options. The expected dividend yield is derived from analysis of historical dividend rates, anticipated dividend rate increases and the estimated price of the Company s common stock over the estimated option life. The risk-free rate is based upon the interest rate on U.S. Treasury securities with maturities that best correspond with the expected life of the applicable stock options. The following provides a summary of the weighted-average assumptions used in valuing stock options granted during the three months ended March 31, 2005:

	Three Months Ended March 31, 2005
Expected dividend yield	4.1%
Risk-free interest rate	4.27%
Expected volatility	15.18%
Expected life of the option	6.5 years

The weighted-average grant date fair value of stock options granted during the three months ended March 31, 2005 was $6.43. There were no stock options awards granted during the three months ended March 31, 2006. The total intrinsic value of options exercised during the three months ended March 31, 2006 and 2005 was $1.6 million and $34.8 million, respectively.

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UST Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
4 SHARE-BASED COMPENSATION (Continued)

Cash received from option exercises under all share-based payment arrangements for the three months ended March 31, 2006 and 2005 was $4.6 million and $51.1 million, respectively. The actual tax benefit realized for the tax deductions from stock option exercises totaled $0.4 million and $12 million for the three months ended March 31, 2006 and 2005, respectively.

Restricted Stock/Restricted Stock Units/Common Stock

A summary of the status of restricted stock and restricted stock units as of March 31, 2006, and changes during the three months ended March 31, 2006, is presented below:

	Restricted Stock		Restricted Stock Units	
	Number of Shares	Weighted average grant-date fair value per share	Number of Shares	Weighted average grant-date fair value per share
Nonvested at January 1, 2006	440,528	$ 39.65	171,390	$ 38.68
Granted				
Forfeited			2,546	$ 38.71
Vested	980	$ 28.41	244	$ 39.30
Nonvested at March 31, 2006	439,548	$ 39.68	168,600	$ 38.68

Of the 439,548 shares of restricted stock above, 251,338 shares are subject to certain performance conditions related to the Company s earnings. There were no restricted stock or restricted stock unit awards granted during the three months ended March 31, 2006. The weighted-average grant date fair value of restricted stock granted during the three months ended March 31, 2005 was $48.14.

During the three months ended March 31, 2006, 1,890 shares of common stock were awarded outright to non-employee directors for meeting attendance, resulting in $74 thousand in compensation expense.

As of March 31, 2006, there is $12 million and $4.3 million of total unrecognized pre-tax compensation expense related to nonvested restricted stock and restricted stock units, respectively, granted under the Company incentive plans. This cost is expected to be recognized over a weighted-average period of 2.8 years and 2.1 years for restricted stock and restricted stock units, respectively.

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UST Inc.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

5 EMPLOYEE BENEFIT PLANS

In accordance with SFAS No. 132, *Employers Disclosures about Pensions and Other Postretirement Benefits (Revised 2003)*, the following provides the components of net periodic benefit cost for the three months ended March 31, 2006 and 2005, respectively:

	Pension Plans Three Months Ended March 31,		Postretirement Benefits Other than Pensions Three Months Ended March 31,	
	2006	2005	2006	2005
Service cost	$ 4,989	$ 4,958	$ 1,528	$ 1,445
Interest cost	7,474	7,535	1,295	1,341
Expected return on plan assets	(6,447)	(6,493)		
Amortization of unrecognized transition obligation	(2)	(2)		
Amortization of prior service cost	5	(1)	(1,463)	(537)
Recognized actuarial loss	1,746	1,548	412	287
Net periodic benefit cost	$ 7,765	$ 7,545	$ 1,772	$ 2,536

As previously disclosed in the 2005 Form 10-K, the Company expects to contribute $6.5 million to its non-qualified defined benefit pension plans in 2006.

In October 2005, in light of the prescription drug benefits offered under Medicare Part D, the Company announced that, effective January 1, 2006, its welfare benefit plans will no longer include prescription drug coverage for substantially all Medicare-eligible retirees or their Medicare-eligible spouses or dependents. In accordance with FASB Statement of Position No. 106-2, *Accounting and Disclosure Requirements Related to the Medical Prescription Drug, Improvement and Modernization Act of 2003*, this amendment to reduce coverage to levels that are no longer deemed actuarially equivalent does not impact the actuarial experience gain previously recognized in connection with the subsidy. However, the combined impact of the amendment and the effective elimination of the subsidy are reflected as a credit to prior service cost.

In accordance with SFAS No. 106, *Employers Accounting for Postretirement Benefits Other than Pensions*, the impact of the October 2005 plan amendment effectively eliminating prescription drug benefits, along with the impact of other amendments to retiree health and welfare plans, all communicated in the same October announcement, were recognized beginning in the fourth quarter of 2005. These amendments will continue to impact net periodic postretirement benefit cost over the estimated remaining service period of affected participants.

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UST Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

6 INCOME TAXES

The Company s income tax provision takes into consideration pre-tax income, statutory tax rates and the Company s tax profile in the various jurisdictions in which it operates. The tax bases of the Company s assets and liabilities reflect its best estimate of the future tax benefit and costs it expects to realize when such amounts are included in its tax returns. Quantitative and probability analysis, which incorporates management s judgment, is required in determining the Company s effective tax rate and in evaluating its tax positions. Notwithstanding the fact that all of the Company s tax filing positions are supported by the requisite tax and legal authority, accruals are established in accordance with SFAS No. 5, *Accounting for Contingencies,* when the Company believes that these positions are likely to be subject to challenge by a tax authority.

The Internal Revenue Service (IRS) and other tax authorities audit the Company s income tax returns on a continuous basis. Depending on the tax jurisdiction, a number of years may elapse before a particular matter for which the Company has established an accrual is audited and ultimately resolved. While it is often difficult to predict the timing of tax audits and their final outcome, the Company believes that its accruals reflect the probable outcome of known tax contingencies. However, the final resolution of any such tax audit could result in either a reduction in the Company s accruals or an increase in its income tax provision, both of which could have a significant impact on the results of operations in any given period. The Company continually and regularly evaluates, assesses and adjusts these accruals in light of changing facts and circumstances, which could cause the effective tax rate to fluctuate from period to period.

The Company s effective tax rate increased to 37.3 percent for the quarter ended March 31, 2006 from 35.2 percent for the quarter of March 31, 2005. Income tax expense for the first quarter of 2005 reflects the favorable impact of a net reversal of income tax accruals of $4.7 million, net of federal income tax benefit, which resulted from the settlement of various income tax audits by the IRS and other taxing authorities.

In the first quarter of 2006, the Company approved a cash dividend from the undistributed earnings of one of its foreign subsidiaries. The distribution totaled $19.7 million, of which approximately $18.2 million is currently taxable in the U.S., as $1.5 million constituted previously taxed income. In addition, the distribution was subject to foreign withholding taxes of 5 percent. There was no material impact to income tax expense due to additional foreign tax credits applied against such amounts.

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UST Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

7 SEGMENT INFORMATION

The Company s reportable segments are Smokeless Tobacco and Wine. Those business units that do not meet quantitative reportable thresholds are included in All Other Operations. Included in All Other Operations for both periods are the Company s international operations. Interim segment information is as follows:

	Three Months Ended March 31,	
	2006	2005
Net Sales to Unaffiliated Customers:		
Smokeless Tobacco	$ 366,278	$ 378,719
Wine	56,309	51,591
All Other Operations	11,054	10,217
Net sales	$ 433,641	$ 440,527
Operating Profit:		
Smokeless Tobacco	$ 191,690	$ 200,166
Wine	8,536	7,101
All Other Operations	3,708	3,660
Operating profit	203,934	210,927
Corporate expenses	(7,561)	(6,611)
Interest, net	(11,470)	(16,391)
Earnings before income taxes	$ 184,903	$ 187,925

The Company s identifiable assets by reportable segment as of March 31, 2006 did not change significantly from amounts appearing in the December 31, 2005 Consolidated Segment Information (See the 2005 Form 10-K), with the exception of assets of All Other Operations which reflect a decrease in cash and cash equivalents primarily related to the cash dividend from one of the Company s foreign subsidiaries (See Note 6, Income Taxes for further information).

8 ASSETS HELD FOR SALE

On March 30, 2006, the Company sold a winery property located in California for net proceeds of $5.9 million, resulting in a pre-tax gain of $2.5 million which was recorded as a reduction to SA&A expenses in the Condensed Consolidated Statement of Operations. Prior to this transaction, the property was included as assets held for sale on the December 31, 2005 Consolidated Statement of Financial Position.

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UST Inc.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
9 NET EARNINGS PER SHARE
Basic earnings per share is computed by dividing net earnings by the weighted-average number of shares of common stock outstanding during the period. Diluted earnings per share is computed by dividing net earnings by the weighted-average number of shares of common stock outstanding during the period, increased to include the number of shares of common stock that would have been outstanding had all potentially dilutive shares of common stock been issued. The dilutive effect of outstanding options, restricted stock and restricted stock units is reflected in diluted earnings per share by applying the treasury stock method under SFAS No. 128, *Earnings per Share*. Under the treasury stock method, an increase in the fair value of the Company s common stock can result in a greater dilutive effect from outstanding options, restricted stock and restricted stock units. Furthermore, the exercise of options and the vesting of restricted stock and restricted stock units can result in a greater dilutive effect on earnings per share than that recognized under the treasury stock method.
The following table presents the computation of basic and diluted net earnings per share: