SCIOS INC
Form 10-Q
November 09, 2001
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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 September 30, 2001 OR |_| TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the transition period from ________ to ___________ Commission file number: 0-11749

Scios Inc.

(Exact name of Registrant as specified in its charter) Delaware 95-3701481 (State or other jurisdiction of (I.R.S. Employer incorporation or organization) Identification No.) Scios Inc. 820 W. Maude Ave. Sunnyvale, CA 94085 (Address of principal executive offices) (Zip code) (408) 616-8200 (Registrant's telephone number including area code) Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No ____ - Number of shares outstanding of the issuer's common stock, par value $.001 per share, as of September 30, 2001: 45,397,905

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

SCIOS INC.

Consolidated Balance Sheets
(In thousands, except share and per share data)

ASSETS	September 30, 2001 (Unaudited)
Current assets:	
Cash and cash equivalents	$ 69,904
Marketable securities	1,006
Accounts receivable	6,440
Inventory	428
Prepaid expenses and other assets	488
Total current assets	78,266

Marketable securities, non-current	70,666
Property and equipment, net	8,642
Other assets	4,063
TOTAL ASSETS	$ 161,637
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current liabilities:	
Accounts payable	$ 6,879
Other accrued liabilities	12,116
Deferred contract revenues	128
Total current liabilities	19,123
Long-term debt	41,350
Total liabilities	60,473
Stockholders' equity:	
Preferred stock; $.001 par value; 20,000,000 shares authorized; 4,991 shares issued and outstanding	--
Common stock; $.001 par value; 150,000,000 shares authorized; 45,397,905 and 39,166,373 shares issued and outstanding, respectively	45
Treasury stock; 30,000 shares	(445)
Additional paid-in capital	545,930
Notes receivable from stockholders	(446)
Deferred compensation, net	(106)
Accumulated other comprehensive income	1,256
Accumulated deficit	(445,070)
Total stockholders' equity	101,164
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 161,637

The accompanying notes are an integral part of these consolidated financial stat

SCIOS INC.

Consolidated Statements of Operations and Comprehensive Loss
(In thousands, except share and per share data)

	Three months ended September 30,	
	2001	2000
	(Unaudited)	
Revenues:		
Product sales	$ 18,330	$ --
Research and development contracts and royalties	1,284	1,192
Gain on sale of marketing rights	--	--
Psychiatric product sales, co-promotion commissions, net of expenses	--	1,624
	19,614	2,816
Costs and expenses:		
Cost of sales	2,035	--
Research and development	12,101	9,645
Marketing, general and administration	18,347	3,545
Restructuring credits	--	
	32,483	13,190
Loss from operations	(12,869)	(10,37
Other income and expense:		
Interest income	1,929	1,221
Interest expense	(653)	(91
Realized gains (losses) on securities	205	(
Other income (expense), net	221	(41
	1,702	(11
Net loss	(11,167)	(10,484

Other comprehensive income:		
Change in unrealized gain on securities	700	387
Comprehensive loss:	$ (10,467)	$ (10,097
Loss per common share:		
Basic and diluted	$ (0.25)	$ (0.28)
Weighted average number of common shares outstanding used in the calculation of net loss per share:		
Basic and diluted	45,383,394	37,881,42

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

SCIOS INC.

Consolidated Statements of Cash Flows
(In thousands)

	Nine month Septembe 2001
	(Unaudi
Cash flows from operating activities:	
Net loss	$ (33,663)
Adjustments to reconcile net loss to net cash used in operating activities:	
Depreciation and amortization	2,508
Loss on property and equipment retirement	365
Accrued long-term interest payable	2,255
Gain (loss) on sale of securities	594
Amortization of deferred compensation	311
Changes in assets and liabilities:	
Accounts receivable	(1,223)
Accounts payable	2,292
Inventories	(428)
Other accrued liabilities	1,367
Prepaid expenses and other assets	(1,822)
Deferred contract revenue	(16,065)
Restructuring (credits) charges	--
Net cash used in operating activities	(43,508)
Cash flows from investing activities:	
Purchases of property and equipment	

	(2,605)
Sales/maturities of marketable securities	282,340
Purchases of marketable securities	(286,306)
Net cash provided by (used in) investing activities	(6,571)
Cash flows from financing activities:	
Issuance of common stock and collection of notes receivable from stockholders, net	116,949
Purchase of treasury stock	(445)
Payment (issues) of notes receivable	188
Net cash provided by (used in) financing activities	116,692
Net increase (decrease) in cash and cash equivalents	66,613
Cash and cash equivalents, at beginning of period	3,291
Cash and cash equivalents, at end of period	$ 69,904

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

SCIOS INC.

Notes to Consolidated Financial Statements (unaudited)

1. Basis of Presentation

The accompanying unaudited consolidated financial statements of Scios have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not contain all of the information and footnotes required by generally accepted accounting principles in the United States of America for complete financial statements. In the opinion of management, the accompanying unaudited, consolidated financial statements reflect all adjustments (consisting of normal, recurring adjustments) considered necessary for a fair presentation of Scios' interim consolidated financial information. These consolidated financial statements and notes should be read in conjunction with the audited financial statements of Scios included in our Annual Report on Form 10-K for the year ended December 31, 2000. The results of operations for the three and nine months ended September 30, 2001 are not necessarily indicative of the operating results that may be reported for the fiscal year ending December 31, 2001 or for any other future period.

2. New Accounting Pronouncements

Financial Accounting Standards No. 141. In July 2001, the Financial Accounting Standards Board issued SFAS No. 141 "Business Combinations," which establishes financial accounting and reporting for business combinations and supersedes APB Opinion No. 16, Business Combinations, and FASB Statement No. 38, Accounting for Preacquisition Contingencies of Purchased Enterprises. It requires that all business combinations in the scope of this Statement are to be accounted for using one method, the purchase method. The provisions of this Statement apply to all business

combinations initiated after June 30, 2001, and also applies to all business combinations accounted for using the purchase method for which the date of acquisition is July 1, 2001, or later. The adoption of SFAS No. 141 had no material impact on our financial reporting and related disclosures. Financial Accounting Standards No. 142. In July 2001, the Financial Accounting Standards Board issued SFAS No. 142 "Goodwill and Other Intangible Assets," which establishes financial accounting and reporting for acquired goodwill and other intangible assets and supersedes APB Opinion No. 17, Intangible Assets. It addresses how intangible assets that are acquired individually or with a group of other assets (but not those acquired in a business combination) should be accounted for in financial statements upon their acquisition, and after they have been initially recognized in the financial statements. We will adopt SFAS No.142 beginning with the first quarter of fiscal 2002. The adoption of SFAS No. 142 is not expected to have a material impact on our financial reporting and related disclosures. In October 2001, the FASB issued Statement of Financial Accounting Standards No. 144 ("SFAS 144"), "Accounting for the Impairment or Disposal of Long-Lived Assets," which is effective for fiscal years beginning after December 15, 2001 and interim periods within those fiscal periods. This Statement supersedes FASB Statement No. 121and APB 30, however, this Statement retains the requirement of Opinion 30 to report discontinued operations separately from continuing operations and extends that reporting to a component of an entity that either has been disposed of (by sale, by abandonment, or in a distribution to owners) or is classified as held for sale. This Statement addresses financial accounting and reporting for the impairment of certain long-lived assets and for long-lived assets to be disposed of. Management does not expect the adoption of SFAS 144 to have a material impact on the Company's financial position and results of operations.

3. Computation of Loss Per Share

The following table sets forth the computation of the Scios' basic and diluted loss per share (in thousands, except per share amounts):

	Three months ended September 30,		Nine m Sept
	20001	2000	200
Numerator			
Basic and Diluted Net loss	$ 11,167	$10,484	$33,6
Denominator			
Basic and Diluted Weighted average shares	45,383	37,881	41,5
Basic and diluted loss per share	$ 0.25	$ 0.28	$ 0.81

The potentially dilutive effect of outstanding options to purchase common stock would have been anti-dilutive as to the reported losses per share in both 2001 and 2000, and they were therefore excluded from the diluted loss per share calculations for all periods. Further, in the third quarter of 2000, we paid down the Genentech loan by issuing 4,991 shares of preferred stock. The preferred stock converts at a rate of 100:1 of common stock at Genentech's option. Although potentially dilutive, the optional settlement of the Genentech loan through the issuance of preferred stock would have been anti-dilutive in both 2001 and 2000 and was therefore excluded from the calculations. At September 30, 2001, we had 7,310,087 outstanding stock options at prices ranging from $3.81 to $27.60 per share. At September 30, 2000, we had 5,238,021 outstanding stock options at prices ranging from $3.69 to $21.13 per share. 4. Industry and Geographic Segment Information We operate in one business segment, using one measurement of profitability for our business. We receive revenue from product sales and from licensing and development of products from partners in the United States, Europe and Asia Pacific. At September 30, 2001, all long-lived assets were located in the United

States. Revenues for the nine months ended September 30, 2001 were earned in the United States, from Japan for bulk Fibroblast Growth Factor ("FGF") shipments to Kaken Pharmaceuticals Co., Ltd., and royalty income from sales of Fiblast(R)spray by Kaken. All revenues from sales of Natrecor(R)were earned in the United States.

5. Gain on Sale of Marketing Rights

In the first quarter of 2001, the marketing rights for psychiatric product sales were sold to GlaxoSmithKline, or GSK. The marketing rights were originally licensed from GSK under a 1990 licensing agreement. In order to effect the purchase, the licensing agreement was terminated effective March 31, 2001, and we received from GSK $4.0 million in 2001, and will receive $3.0 million in 2002 and $2.5 million in 2003. We recognized a one-time gain on the sale of $9.4 million, which has been classified on the statement of operations under the caption Gain on Sale of Marketing Rights. In addition, we ended the deployment of our Psychiatric Sales Marketing Division sales force and terminated certain full-time support personnel. Severance payments for these personnel amounted to approximately $788,000. 6. Notes Receivable from Officers At September 30, 2001, we had notes receivable from three officers. The first note is in the amount of $179,466 with interest at 6.30% per annum, due and payable on October 31, 2001. The loan was granted in connection with the payment of income taxes for restricted stock granted to the officer. This loan is collateralized by the vested portion of the officer's common stock and is classified with other current assets on the balance sheet at September 30, 2001. This loan was re-paid in November 2001. The second note is in the amount of $280,040 with interest at 5.18% per annum, due and payable on February 28, 2002. The loan was granted in connection with the payment of income taxes for restricted stock granted to the officer. This loan is collateralized by the vested portion of the officer's stock options and is classified with other current assets on the balance sheet at September 30, 2001. The third note is in the amount of $8,333 with interest at 5.82% per annum. This loan will be forgiven in 2002 based on the continued employment of the officer and is collateralized by the officer's residence. The loan was granted in connection with a housing subsidy for the officer to live in California. This note balance is classified with other assets on the balance sheet at September 30, 2001.

7. Equity Financing

During the second quarter of 2001, we raised approximately $113.0 million, net of expenses, through the issuance of 5,750,000 shares of common stock at $21 per share.

8. Lease Commitments

We lease four facilities in Sunnyvale, California with agreements that expire between 2003 and 2008. In addition, we lease a warehouse in Mountain View, California that expires in 2003.

Future minimum payments under these leases are as follows:

	(in thousands)
2002	$ 1,825
2003	$ 2,069
2004	$ 917
2005	$ 948
2006	$ 979
2007	$ 1,010
2008	$ 868

9. Stockholder Approval of Stock Plans

On May 8, 2001, the stockholders approved an amendment to the 1992 Equity Incentive Plan adding 1.5 million shares of common stock to this plan. In addition, an Employee Stock Purchase Plan was approved by the stockholders with an initial allocation of 375,000 shares of common stock.

10. New Accounting Policies

Product Sales Revenue from Natrecor(R)product sales is recognized upon receipt of a purchase order and product shipment, provided no significant obligations remain and collection of the receivables is deemed probable. Provisions for discounts and rebates to customers and returns are provided for in the same period the related sales are recorded. Product sales consist of revenue from Natrecor(R)and from bulk Fibroblast Growth Factor or FGF. The FDA approved Natrecor(R)on August 13, 2001. This was the first quarter in which we recorded sales of Natrecor(R). In the third quarter of 2001, we recorded the last shipment of bulk FGF to Kaken in Japan. Kaken will manufacture future bulk FGF. Inventory Inventories are stated at the lower of cost (first-in, first-out basis) or market. Cost includes material and conversion costs. Prior to FDA approval, materials and the production of Natrecor(R)was expensed and charged in the Statement of Operations to Research and Development.

11. Innovex, PharmBio, and Scios Amended Agreement

On October 24, 2001 Scios, Innovex and Innovex's sister company, PharmaBio, executed a letter of intent to amend the January 10, 2001 agreement in relation to the Natrecor(R)sales force and the infrastructure supporting it. The amendment will enable Scios, at its option, to assume control of the Natrecor(R)sales force in June 2003, one year ahead of schedule. In addition, we eliminated the $5.0 million line of credit provided by PharmaBio to Scios. Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations The following discussion should be read in conjunction with our audited consolidated financial statements, including the related notes, contained in our Annual Report on Form 10-K for the year-ended December 31, 2000. The following discussion also contains forward-looking statements about our plans, objectives and future results. These forward-looking statements are based on our current expectations, and we assume no obligation to update this information. Realization of these plans and results involves risks and uncertainties, and our actual results could differ materially from those discussed here. Factors that could cause or contribute to such differences include those set forth under "Risk Factors" in this Report on Form 10-Q.

Overview

We are a biopharmaceutical company developing novel drugs for the potential treatment of cardiovascular and inflammatory diseases. Our disease-based technology platform integrates expertise in protein biology with computational and medicinal chemistry to identify novel targets and rationally design small molecule compounds for large markets with unmet medical needs. We employ approximately 415 people. Natrecor(R), our treatment for acute Congestive Heart Failure, or acute CHF, was approved by the FDA in the third quarter of 2001 and is currently marketed by our 168-person sales force. SCIO-469, an oral small molecule inhibitor of p38 kinase, is our lead development candidate for the treatment of rheumatoid arthritis. On August 13, 2001, we received final approval from the FDA to market Natrecor(R)for the intravenous treatment of patients with acutely decompensated congestive heart failure. We submitted an amendment to our New Drug Application, or NDA, for Natrecor(R)to the U.S. Food and Drug Administration, or FDA, in January 2001, and the FDA's Cardiovascular and Renal Drugs Advisory Committee reviewed our amended NDA on May 25, 2001. The recommendation of that Committee was for unanimous approval of Natrecor(R). On July 10, 2001, we received from the FDA an approvable letter for Natrecor(R). The approvable letter was issued with two items to be completed: the pre-approval inspection of our facility and the final negotiations on the drug's label. In July 2001, the District Office of the FDA completed the pre-approval inspection and recommended approval of the Natrecor(R)New Drug Application. During August 2001, the final negotiations on the drug's label were completed. During January 2001, we completed a Phase Ia clinical trial with single oral doses of SCIO-469 in healthy volunteers. In February 2001, a Phase Ib clinical trial was initiated with 20 healthy volunteers to evaluate the safety and tolerability of multiple oral doses of SCIO-469 over a two-week period. The Phase Ib trial was completed in April 2001. Based on the results of these trials, we filed an Investigational New Drug application with FDA in November 2001 for a Phase II study with SCIO-469. The study is expected to begin enrollment of Rheumatoid Arthritis patients in January 2002. In March 2001, we initiated the PROACTION (Prospective Randomized Outcomes Study of Acutely Decompensated Congestive Heart Failure Treated Initially in Outpatients

with Natrecor(R)) trial, a pilot study designed to compare the clinical effects, safety profile and economic impact of standard therapy plus Natrecor(R)to standard therapy plus placebo. The PROACTION trial has an enrollment target of 250 acute CHF patients. An interim data analysis of the first 145 patients enrolled was completed in the third quarter of 2001. The early interpretation of the data, which may change based on the final data analysis, suggest that Natrecor(R)can be safely administered in the emergency department setting, and patients treated with Natrecor may be less likely to be admitted to the hospital for heart failure from the emergency department. Final results of the PROACTION study is expected to be reported in the first quarter of 2002. In April 2001, Kaken Pharmaceuticals Co., Ltd. received notice from the Japanese Ministry of Health and Welfare that they have been granted marketing approval for Fiblast(R)Spray for the treatment of recalcitrant dermal ulcers. The active ingredient in Fiblast(R)Spray is recombinant basic Fibroblast Growth Factor, or FGF, which Kaken licensed from us in 1988. Based on this approval, we recognized $15.9 million in revenue during 2001 following shipment of FGF to Kaken in Japan. For the quarters ended June 30, 2001 and September 30, 2001, we recorded product sales of $2.1 million and $13.8 million, respectively . Additionally, in the third quarter, we received royalty payments of $0.2 million from sales of Fiblast(R). In May 2001, we expanded our research collaboration with Medtronic, Inc. to study the effects of Natrecor(R)in combination with Medtronic's heart failure devices and implantable infusion systems. In the first of a planned program of pilot clinical studies, we will evaluate the hemodynamic and clinical effects of Natrecor(R), including the effects on spontaneous activity and controlled exercise tolerance, using information collected by Medtronic's Chronicle(R)Implantable Hemodynamic Monitor (IHM) both during and after infusions of Natrecor(R). The pilot feasibility study began in the third quarter of 2001 at the Karolinska Hospital in Stockholm. The Chronicle IHM is an implanted system designed to measure and record hemodynamic variables over time such as right ventricular systolic and diastolic pressures, estimated pulmonary artery diastolic pressure, heart rate and activity. The Chronicle IHM is not yet approved for marketing in the United States or Europe. During the second quarter of 2001, we raised approximately $113.0 million, net of expenses, through the issuance of 5,750,000 shares of common stock. This equity financing significantly strengthened our financial position and gave us the financial flexibility to launch and market Natrecor(R)while developing our promising pipeline, most importantly our p38 kinase inhibitor for rheumatoid arthritis. On October 24, 2001 Scios, Innovex and Innovex's sister company, PharmaBio, executed a letter of intent to amend the January 10, 2001 agreement in relation to the Natrecor(R)sales force and the infrastructure supporting it. The amendment will enable Scios, at its option, to assume control of the Natrecor(R)sales force in June 2003, one year ahead of schedule. In addition, we eliminated the $5.0 million line of credit provided by PharmaBio to Scios.

Results of Operations

Three Months Ended September 30, 2001 and 2000 Revenues Product Sales. Product sales for the three months ended September 30, 2001 were $18.3 million versus none for the three months ended September 30, 2000. The increase was due to sales of bulk FGF to Kaken and our sales of Natrecor(R). During the third quarter of 2001, we recorded $13.8 million of bulk FGF product sales to Kaken in Japan. Further, Natrecor(R)received FDA approval on August 13, 2001, and we recorded $4.5 million in Natrecor(R)product sales this quarter. Research and Development Contract Revenues and Royalties Research and development contract revenues and royalties were $1.3 million for the three months ended September 30, 2001 and $1.2 million for the three months ended September 30, 2000. These contract revenues reflect our research collaboration agreements with Eli Lilly and Company, DuPont Pharmaceutical Company, and other licensing fees and royalties. The research collaboration agreement with Dupont Pharmaceutical Company ended effective December 2000. Psychiatric Product Sales and Co-Promotion Commissions. Psychiatric product sales and co-promotion commissions for the three months ended September 30, 2001 were none versus $1.6 million for the three months ended September 30, 2000. Scios no longer sells or co-promote the psychiatric products after March 31, 2001. Costs and Expenses Cost of Sales. Cost of sales were $2.0 million and none for the three months ended September 30, 2001 and 2000, respectively. The increase in expenses were mainly due to the cost to manufacture and distribute Natrecor(R), royalty payments to the Biotechnology Research Partners, LTD. on revenues generated from the sales of bulk FGF to Kaken, and cost of shipping bulk FGF to Kaken in Japan. Prior to FDA approval, materials and the cost of production of Natrecor(R)were expensed and charged to Research and Development. Research and Development. Research and development expenses were $12.1 million and $9.6 million

for the three months ended September 30, 2001 and 2000, respectively. The increase in expenses of $2.5 million in expenses were mainly attributable to clinical expenses related to Natrecor(R), research expenses related to our p38 kinase inhibitor program, associated expenses to develop the Acute Decompensated Heart Failure National Registry (ADHERE) database, and hiring of 13 Scientific Affairs Managers to support the launch of Natrecor(R). Marketing, General and Administrative. Marketing, general and administrative expenses were $18.3 million and $3.5 million for the three months ended September 30, 2001 and 2000, respectively. The increase of $14.8 million in expenses for the 2001 quarter is largely attributable to the costs associated with the commercialization of Natrecor(R). These expenses consist of the building of a marketing and sales force infrastructure that includes the recruiting of Cardiovascular Sales Representatives, Area Business Directors, and Area Business Managers. Other costs included launch activities, developing and producing promotional materials, and obtaining and analyzing marketing research data. Other Income (Expense), net Net other income (expense) was $1.7 million and $(0.1) million for the three months ended September 30, 2001 and 2000, respectively. The increase of $1.8 million in other income and expense was principally due to the $0.7 million increase in interest income due to the higher cash balances from quarter to quarter, lower interest expense of $0.2 million due to lower rates, and realized gains on marketable securities of $0.2 million. Nine Months Ended September 30, 2001 and 2000 Revenues Product Sales. Product sales for the nine months ended September 30, 2001 were $20.4 million versus none for the nine months ended September 30, 2000. The increase was due to sales of bulk FGF to Kaken and our sales of Natrecor(R). Based on the product approval of Fiblast(R)Spray in Japan, we recorded $15.9 million of bulk FGF product sales to Kaken in Japan during the second and third quarters of 2001. In addition, we recorded Natrecor(R)sales of $4.5 million in the third quarter following FDA approval on August 13, 2001. Research and Development Contract Revenues and Royalties. Research and development contract revenues and royalties were $3.9 million for the nine months ended September 30, 2001 and $4.6 million for the nine months ended September 30, 2000. These contract revenues reflect our research collaboration agreements with Eli Lilly and Company, DuPont Pharmaceutical Company, and other licensing fees and royalties. The decrease of $0.7 million is primarily due to the fact that the collaborative research phase of our research collaboration agreement with DuPont Pharmaceutical Company ended in December 2000. Gain on Sale of Marketing Rights. In the first quarter of 2001, we sold our marketing rights for certain psychiatric products licensed to GSK. The marketing rights were originally licensed from GSK under a 1990 licensing agreement. In order to effect the purchase, we terminated the licensing agreement effective March 31, 2001, and we received from GSK $4.0 million in 2001, and will receive $3.0 million in 2002, and $2.5 million in 2003. We recognized a one-time gain of $9.4 million related to the sale. Psychiatric Product Sales and Co-Promotion Commissions. Psychiatric product sales and co-promotion commissions for the nine months ended September 30, 2001 were $3.1 million versus $4.5 million for the nine months ended September 30, 2000. The $3.1 million represents final co-promotion commissions as we no longer sell or co-promote psychiatric products after March 31, 2001. Costs and Expenses Cost of Sales. Cost of sales were $2.0 million and none for the nine months ended September 30, 2001 and 2000, respectively. The increases in expenses were mainly due to the cost to manufacture and distribute Natrecor(R), royalty payments to the Biotechnology Research Partners, LTD. on revenues generated from the sales of bulk FGF to Kaken, and cost of shipping bulk FGF to Kaken in Japan. Prior to FDA approval, materials and the cost of production of Natrecor(R)were expensed and charged to Research and Development. Research and Development. Research and development expenses were $34.7 million and $30.2 million for the nine months ended September 30, 2001 and 2000, respectively. The increase in expenses were mainly attributable to clinical expenses related to Natrecor(R), research expenses related to our p38 kinase inhibitor program, associated expenses to develop the Acute Decompensated Heart Failure National Registry (ADHERE) database, hiring of 13 Scientific Affairs Managers to support the Natrecor(R)launch, and materials and cost of production of Natrecor(R)prior to FDA approval. Marketing, General and Administrative. Marketing, general and administrative expenses were $35.1 million and $9.8 million for the nine months ended September 30, 2001 and 2000, respectively. The increase of $25.3 million in expenses in 2001 is largely attributable to the costs associated with the pre-commercialization of Natrecor(R). These expenses include the building of a marketing and sales force infrastructure, which consist of the recruiting of Cardiovascular Sales Representatives, Area Business Directors, and Area Business Managers. In addition, other expenses reflect the development and production of promotional materials, and obtaining and analyzing marketing research data. Restructuring charges (credits). On completion of our 1999 corporate restructuring, we recorded a $1.0 million credit in 2000 relating to the unused portion of the restructuring reserve. Other Income (Expense), net Net other expense was $1.3 million and $(0.4) million for the nine

months ended September 30, 2001 and 2000, respectively. The increase of $1.7 million in other income and expense was principally due lower interest expense of $0.7 million, and realized gains on marketable securities of $0.8 million.

Liquidity and Capital Resources

To date, our operations and capital requirements have been financed primarily with the proceeds of public and private sales of common stock and preferred stock, research and development partnerships, collaborative agreements with pharmaceutical firms, product sales and investment income. During the second quarter of 2001, we raised approximately $113.0 million, net of expenses, through a public offering of 5,750,000 shares of common stock, which significantly strengthened our financial position. At September 30, 2001, our combined cash, cash equivalents and marketable securities (both current and non-current) totaled $141.6 million. In the first quarter of 2001 we entered into a sales and marketing alliance with Innovex, a subsidiary of Quintiles Transnational Corp. As part of the three and half year agreement, PharmaBio Development, Inc., an affiliate of Innovex, agreed to fund $30.0 million of our costs to launch Natrecor(R)over the first 24 months of the commercialization of Natrecor(R)' and to loan us up to $5.0 million. Of the $30.0 million, $10.0 million is expected to be paid to us in the 4th quarter of 2001 and $20.0 million in 2002 and 2003. Under the agreement, Innovex will identify, hire, train and deploy a dedicated cardiology and emergency medicine sales force to launch and market Natrecor(R). On October 24, 2001 Scios, Innovex and Innovex's sister company, PharmaBio, executed a letter of intent to amend the January 10, 2001 agreement in relation to the Natrecor(R)sales force and the infrastructure supporting it. The amendment will enable Scios, at its option, to assume control of the Natrecor(R)sales force in June 2003, one year ahead of schedule. In addition, we eliminated the $5.0 million line of credit provided by PharmaBio to Scios. During September 2001, we announced today that the Board of Directors authorized the repurchase of up to $10.0 million of Scios common stock. The repurchases are to be made through open-market transactions at the discretion of management and as market conditions warrant. During the third quarter of 2001, we re-purchased $445,000 or 30,000 common stocks. Net cash used in operating activities of $44.1 million in the nine months ended September 30, 2001 was primarily attributable to the loss of $33.7 million and decreases in operating assets and liabilities of $15.8 million, partially offset by non-cash expenses of $5.4 million. Net cash used by investing activities of $6.0 million in the nine months ended September 30, 2001 consisted of net purchases of marketable securities of $3.4 million and purchases of property and equipment of $2.6 million. Net cash provided by financing activities of $116.7 million in the nine months ended September 30, 2001 was due to the net proceeds from the issuance of common stock and collection of notes receivable of $116.9 million; offset in part by the repurchase of 30,000 shares of Scios common stock. The stock was recorded as treasury stock of $0.5 million. We anticipate that our existing cash, cash equivalents and marketable securities and proceeds from proceeds from product sales, existing collaborations, including our agreement with Innovex and PharmaBio, and future expected sales of our products will enable us to maintain our current and planned operations for the next twenty-four months. In the long-term, we may need to arrange additional financing for the operation of our business, including the commercialization of our products currently under development. We will consider collaborative arrangements and additional public or private financing, including additional equity financing. Factors influencing the availability of additional financing include our progress in product development, investor perception of our prospects and the general conditions of the financial markets. New Accounting Pronouncements Financial Accounting Standards No. 141. In July 2001, the Financial Accounting Standards Board issued SFAS No. 141 "Business Combinations," which establishes financial accounting and reporting for business combinations and supersedes APB Opinion No. 16, Business Combinations, and FASB Statement No. 38, Accounting for Preacquisition Contingencies of Purchased Enterprises. It requires that all business combinations in the scope of this Statement are to be accounted for using one method, the purchase method. The provisions of this Statement apply to all business combinations initiated after June 30, 2001, and also applies to all business combinations accounted for using the purchase method for which the date of acquisition is July 1, 2001, or later. The adoption of SFAS No. 141 had no material impact on our financial reporting and related disclosures. Financial Accounting Standards No. 142. In July 2001, the Financial Accounting Standards Board issued SFAS No. 142 "Goodwill and Other Intangible Assets," which establishes financial accounting and reporting for acquired goodwill and other intangible assets and supersedes APB Opinion No. 17, Intangible Assets. It addresses how intangible assets that are acquired individually or with a group of other assets (but not those acquired in a business combination) should be accounted for in financial statements upon their acquisition, and after they have

been initially recognized in the financial statements. We will adopt SFAS No.142 beginning with the first quarter of fiscal 2002. The adoption of SFAS No. 142 is not expected to have a material impact on our financial reporting and related disclosures. In October 2001, the FASB issued Statement of Financial Accounting Standards No. 144 ("SFAS 144"), "Accounting for the Impairment or Disposal of Long-Lived Assets," which is effective for fiscal years beginning after December 15, 2001 and interim periods within those fiscal periods. This Statement supersedes FASB Statement No. 121and APB 30, however, this Statement retains the requirement of Opinion 30 to report discontinued operations separately from continuing operations and extends that reporting to a component of an entity that either has been disposed of (by sale, by abandonment, or in a distribution to owners) or is classified as held for sale. This Statement addresses financial accounting and reporting for the impairment of certain long-lived assets and for long-lived assets to be disposed of. Management does not expect the adoption of SFAS 144 to have a material impact on the Company's financial position and results of operations.

Risk Factors

You should carefully consider the risks described below before making an investment decision. Our business, financial condition or results of operations could be harmed by any of these risks. The risks described below are not the only ones facing our company. Additional risks not presently known to us or that we currently deem immaterial may also impair our business operations. This document also contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of the risks faced by us, including those described below and elsewhere in this document.

Risks Related to Natrecor® (nesiritide)

If Natrecor(R)does not gain market acceptance, our business will suffer. Natrecor(R)may not gain market acceptance among physicians, patients, healthcare payors and the medical community. We will need to educate doctors and other healthcare advisors of the safety and clinical efficacy of Natrecor(R)and its potential advantages over other treatments. The degree of market acceptance of Natrecor(R)will also depend on a number of factors, including: |X| the degree of clinical efficacy and safety; |X| cost-effectiveness of Natrecor(R); |X| its advantage over alternative treatment methods; and |X| reimbursement policies of government and third party payors. To the extent market acceptance of Natrecor(R)is limited, our revenues may suffer.

If the FDA determines that our third-party manufacturing facilities are not adequate, we may lose the ability to manufacture and sell Natrecor®.

Periodically, the FDA is likely to inspect each of the facilities involved in manufacturing Natrecor(R). Natrecor(R)is manufactured for us by Biochemie GmbH, a subsidiary of Novartis, in Austria and is shipped in powder form to Abbott Laboratories in McPherson, Kansas where it is blended, filled and packaged for shipment. Although each facility has previously passed FDA inspections, future inspections may find deficiencies in the facilities or processes that may delay or prevent the manufacture or sale of Natrecor(R). If deficiencies are identified, we may lose the ability to supply and sell Natrecor(R)extended periods of time.

We rely on third-party manufacturers, and if they experience any difficulties with their manufacturing processes, we may not obtain sufficient quantities of Natrecor® to assure availability.

We rely on third parties for the manufacture of bulk drug substances and final drug product for clinical and commercial purposes relating to Natrecor(R). Biochemie GmbH is responsible for manufacturing Natrecor(R)in bulk quantities and Abbott Laboratories is responsible for blending, filling and packaging Natrecor(R), and if they encounter problems in these processes, our revenues from future sales of Natrecor(R)could decrease. Natrecor(R)is manufactured using industry-accepted recombinant manufacturing techniques, which must be conducted under strict controls and tight timelines. Natrecor(R)is subject to strict quality control testing during all phases of production and prior to its release to the market. Any quality control testing failures could lead to a reduction in the available supply of Natrecor(R). Biochemie depends on outside vendors for the timely supply of raw materials used to produce our

products, including Natrecor(R). Once a supplier's materials have been selected for use in Biochemie's manufacturing process, the supplier in effect becomes a sole or limited source of that raw material due to regulatory compliance procedures. We depend on these third parties to perform their obligations effectively and on a timely basis. If these third parties fail to perform as required, our ability to deliver Natrecor(R)on a timely basis would be impaired. In addition, in the event of a natural disaster, equipment failure, power failure, strike or other difficulty, we may be unable to replace our third party manufacturers in a timely manner and would be unable to manufacture Natrecor(R)to meet market needs. The success of Natrecor(R)is highly dependent on our partner, Innovex L.P., a division of Quintiles Transnational Corp., for marketing, promotion and sales activities. We believe that for Natrecor(R)to be widely adopted, the efforts of an experienced sales force are needed. We have limited experience in managing or operating a marketing organization. Accordingly, we have entered into an exclusive agreement with Innovex to co-promote and sell Natrecor(R)in the United States. As part of our agreement with Innovex, we have hired a sales force of approximately 170 people solely dedicated to the sale of Natrecor(R). If Innovex and we fail to devote appropriate resources to promote, sell and distribute Natrecor(R), sales of Natrecor(R)could be reduced. If Innovex breaches or terminates its agreement with us or otherwise fails to conduct its Natrecor(R)-related activities in a timely manner or if there is a dispute about its obligations, we may need to seek another partner. In that event, we cannot assure you that we will be able to obtain another partner on favorable terms, if at all.

The failure of PharmaBio Development, Inc., an affiliate of Innovex, to fulfill its obligation to partially fund the commercialization of Natrecor® may affect our ability to successfully market Natrecor®.

PharmaBio has agreed to fund $30.0 million of our costs to launch Natrecor(R)over the first 24 months of Natrecor(R)'s commercialization. Of the $30.0 million, we anticipate that $10.0 million will be paid to us in 2001. If PharmaBio breaches or terminates its agreement with us or otherwise fails to fulfill its financial obligations under the agreement and we are unable to secure alternative funding, we may lose our ability to successfully market Natrecor(R). In the area of acute CHF, we face competition from companies with substantial financial, technical and marketing resources, which could limit our future revenues from Natrecor(R). Many therapeutic options are available for patients with acute CHF. Currently used drugs fall into three main categories: vasodilators, inotropes, and diuretics. Natrecor(R)would compete against both vasodilators and inotropes in the acute CHF market. Many of these drugs are available in generic formulation with an associated low cost. In addition, milrinone, an inotrope, is currently promoted by Sanofi-Synthelabo Inc. We may not be able to compete effectively with these long-standing current forms of therapy. In addition, Natrecor(R)costs more than many of these existing drugs, which may harm our competitive position relative to these drugs. New drugs in development for the treatment of acute CHF would also compete with Natrecor(R)if approved by the FDA or other regulatory agencies. Tezosentan(R), a non-selective endothelin receptor antagonist, is being developed by Actelion LTD. and has been evaluated in Phase III clinical trials as a vasodilator for the treatment of acute CHF. In addition, Abbott had previously submitted an NDA for Simdax(R), a calcium sensitizer described as an inotrope, but withdrew the application in 2000. To our knowledge, Abbott has not announced its intent to refile an NDA for Simdax(R). If any such new drug in development is approved by the FDA or other regulatory agencies, we may not be able to compete effectively with these new forms of therapy. If we fail to gain approval for Natrecor(R)and our other product candidates in international markets, our market opportunities will be limited. We have not yet filed for marketing clearance for the use of Natrecor(R)or any other product candidates in foreign countries, and we may not be able to obtain any international regulatory approvals for Natrecor(R)or any other product we develop. If we fail to obtain those approvals or if such approvals are delayed, the geographic market for Natrecor(R)or our other product candidates would be limited.

We will require a partner to market and commercialize Natrecor® and our other product candidates in international markets.

We plan to partner with other companies for the sale of Natrecor(R)and our other product candidates outside of the United States. We cannot assure you that we will be able to enter into such arrangements on favorable terms or at all. In addition, partnering arrangements could result in lower levels of income to us than if we marketed our products entirely on our own. In the event that we are unable to enter into a partnering arrangement for Natrecor(R)or our other product candidates in international markets, we cannot assure you we will be able to develop an effective international

sales force to successfully market and commercialize those products. If we fail to enter into partnering arrangements for our products and are unable to develop an effective international sales force, our revenues would be limited.

If we fail to obtain additional marketing approvals from the FDA for the use of Natrecor® for additional therapeutic indications or if after approval such approval is subsequently revoked, our revenues from Natrecor® will suffer.

In order to expand the medical uses, or therapeutic indications, for which we may market Natrecor(R), we must successfully complete additional clinical trials, which could be lengthy and expensive and will require the allocation of both substantial management and financial resources. Thereafter, we will have to apply separately to the FDA for clearance to market Natrecor(R)for other indications. We cannot assure you that we will be able to successfully complete the required clinical trials or that the FDA will approve Natrecor(R)for any additional indications. In addition, even if Natrecor(R)is approved by the FDA, we cannot exclude the possibility that serious adverse events related to the use of Natrecor(R)might occur in the future, which could either limit its use or cause the FDA to revoke our approval to market Natrecor(R).

Other Risks Related to Scios

We have a history of losses, expect to operate at a loss for the foreseeable future and may never be profitable.

We may not be able to achieve or earn a profit in the future. We began operations in December 1981, and since that time, with the sole exception of 1983, we have not earned a profit on a full-year basis. Our losses have historically resulted primarily from our investments in research and development. As of September 30, 2001, we had an accumulated deficit of approximately $445.1 million. To date, nearly all of our revenues have come from: |X| sales of Natrecor beginning in August 2001; |X| sales of bulk FGF and royalties from Fiblast(R)Spray sales to Kaken in Japan; |X| one-time signing fees from our corporate partners under agreements supporting the research, development and commercialization of our product candidates; |X| one-time payments from our corporate partners when we achieved regulatory or development milestones; |X| research funding from our corporate partners; and |X| our psychiatric sales and marketing division. We expect that our research, development and clinical trial activities and regulatory approvals, together with future general and administrative activities and the costs associated with launching and commercializing our product candidates and launching and commercializing Natrecor(R)in the United States, will result in significant expenses for the foreseeable future. Our operating results are subject to fluctuations that may cause our stock price to decline. Our revenues and expenses have fluctuated significantly in the past. This fluctuation has in turn caused our operating results to vary significantly from quarter to quarter and year to year. We expect the fluctuations in our revenues and expenses to continue, and thus, our operating results should also continue to vary significantly. These fluctuations may be due to a variety of factors including: |X| our success in selling Natrecor(R); |X| the timing and realization of milestone and other payments from our corporate partners; |X| the timing and amount of expenses relating to our research and development, product development and manufacturing activities; and

|X| the extent and timing of costs related to our activities to obtain patents on our inventions and to extend, enforce and/or defend our patents and other rights to our intellectual property.

Because of these fluctuations, it is possible that our operating results for a particular quarter or quarters will not meet the expectations of public market analysts and investors, causing the market price of our common stock to decline. We believe that period-to-period comparisons of our operating results are not a good indication of our future performance, and you should not rely on those comparisons to predict our future operating or share price performance.

We depend on our key personnel and we must continue to attract and retain key employees and consultants.

We depend on our key scientific and management personnel. Our ability to pursue the development of our current and future product candidates depends largely on retaining the services of our existing personnel and hiring additional qualified scientific personnel to perform research and development. We also rely on personnel with expertise in clinical testing, government regulation, manufacturing and marketing. Attracting and retaining qualified personnel

will be critical to our success. We may not be able to attract and retain personnel on acceptable terms given the competition for such personnel among biotechnology, pharmaceutical and healthcare companies, universities and non-profit research institutions. Failure to retain our key scientific and management personnel or to attract additional highly qualified personnel could delay the development of our product candidates and harm our business.

Other than Natrecor®, our product candidates are at early stages of development, and if we are unable to develop and commercialize these product candidates successfully, we will not generate revenues from these products.

We face the risk of failure normally found in developing biotechnology products based on new technologies. Successfully developing, manufacturing, introducing and marketing our early-stage product candidates will require several years and substantial additional capital.

Our operations depend on compliance with complex FDA and comparable international regulations. If we fail to obtain approvals on a timely basis or to achieve continued compliance, the commercialization of our products could be delayed.

We cannot assure you that we will receive the regulatory approvals necessary to commercialize our product candidates, which could cause our business to fail. Our product candidates are subject to extensive and rigorous government regulation by the FDA and comparable agencies in other countries. The FDA regulates, among other things, the development, testing, manufacture, safety, efficacy, record keeping, labeling, storage, approval, advertising, promotion, sale and distribution of biopharmaceutical products. If our potential products are marketed abroad, they will also be subject to extensive regulation by foreign governments. In addition, we have only limited experience in filing and pursuing applications necessary to gain regulatory approvals, which may impede our ability to obtain such approvals. The results of preclinical studies and clinical trials of our products may not be favorable. In order to obtain regulatory approval for the commercial sale of any of our product candidates, we must conduct both preclinical studies and human clinical trials. These studies and trials must demonstrate that the product is safe and effective for the clinical use for which we are seeking approval. We are currently planning to conduct Phase II clinical trials of our lead p38 kinase inhibitor small molecule compound. The results of these or other clinical trials that we may conduct in the future may not be successful. Adverse results from our current or any future trials would harm our business. We also face the risk that we will not be permitted to undertake or continue clinical trials for any of our product candidates in the future. Even if we are able to conduct such trials, we may not be able to satisfactorily demonstrate that the products are safe and effective and thus qualify for the regulatory approvals needed to market and sell them. Results from preclinical studies and early clinical trials are often not accurate indicators of results of later-stage clinical trials that involve larger human populations.

Our products use novel alternative technologies and therapeutic approaches, which have not been widely studied.

Many of our product development efforts focus on novel alternative therapeutic approaches and new technologies that have not been widely studied. These approaches and technologies may not be successful. We are applying these approaches and technologies in our attempt to discover new treatments for conditions that are also the subject of research and development efforts of many other companies.

Rapid changes in technology and industry standards could render our potential products unmarketable.

We are engaged in a field characterized by extensive research efforts and rapid technological development. New drug discoveries and developments in our field and other drug discovery technologies are accelerating. Our competitors may develop technologies and products that are more effective than any we develop or that render our technology and potential products obsolete or noncompetitive. In addition, our potential products could become unmarketable if new industry standards emerge. To be successful, we will need to enhance our product candidates and design, develop and market new product candidates that keep pace with new technological and industry developments. Many other companies are targeting the same diseases and conditions as we are. Competitive products from other companies could significantly reduce the market acceptance of our products. The markets in which we compete are well established and intensely competitive. We may be unable to compete successfully against our current and future

competitors. Our failure to compete successfully may result in pricing reductions, reduced gross margins and failure to achieve market acceptance for our potential products. Our competitors include pharmaceutical companies, biotechnology companies, chemical companies, academic and research institutions and government agencies. For example, many pharmaceutical and biotechnology companies have initiated research programs similar to ours. Many of these organizations have substantially more experience and more capital, research and development, regulatory, manufacturing, sales, marketing, human and other resources than we do. As a result, they may: |X| develop products that are safer or more effective than our product candidates;

|X| obtain FDA and other regulatory approvals or reach the market with their products more rapidly than we can, reducing the potential sales of our product candidates;

|X| devote greater resources to market or sell their products; |X| adapt more quickly to new technologies and scientific advances; |X| initiate or withstand substantial price competition more successfully than we can; |X| have greater success in recruiting skilled scientific workers from the limited pool of available talent; |X| more effectively negotiate third-party licensing and collaboration arrangements; and |X| take advantage of acquisition or other opportunities more readily than we can. In addition, our product candidates, if approved and commercialized, will compete against well-established existing therapeutic products that are currently reimbursed by government health administration authorities, private health insurers and health maintenance organizations. We face and will continue to face intense competition from other companies for collaborative arrangements with pharmaceutical and biotechnology companies, for relationships with academic and research institutions and for licenses to proprietary technology. In addition, we anticipate that we will face increased competition in the future as new companies enter our markets and as scientific developments continue to expand the understanding of various diseases. While we will seek to expand our technological capabilities to remain competitive, research and development by others may render our technology or product candidates obsolete or noncompetitive or result in treatments or cures superior to any therapy developed by us.

If we are unable to protect our intellectual property rights adequately, the value of our potential products could be diminished.

Our success is dependent in part on obtaining, maintaining and enforcing our patents and other proprietary rights. Patent law relating to the scope of claims in the biotechnology field in which we operate is still evolving and surrounded by a great deal of uncertainty. Accordingly, we cannot assure you that our pending patent applications will result in issued patents. Because certain U.S. patent applications may be maintained in secrecy until a patent issues, we cannot assure you that others have not filed patent applications for technology covered by our pending applications or that we were the first to invent the technology. Other companies, universities and research institutions have or may obtain patents and patent applications that could limit our ability to use, manufacture, market or sell our product candidates or impair our competitive position. As a result, we may have to obtain licenses from other parties before we could continue using, manufacturing, marketing or selling our potential products. Any such licenses may not be available on commercially acceptable terms, if at all. If we do not obtain required licenses, we may not be able to market our potential products at all or we may encounter significant delays in product development while we redesign potentially infringing products or methods. In addition, although we own a number of patents, including issued patents and patent applications relating to Natrecor(R)and certain of our p38 kinase inhibitors, the issuance of a patent is not conclusive as to its validity or enforceability, and third parties may challenge the validity or enforceability of our patents. We cannot assure you how much protection, if any, will be given to our patents if we attempt to enforce them and they are challenged in court or in other proceedings. It is possible that a competitor may successfully challenge our patents or that challenges will result in limitations of their coverage. In addition, the cost of litigation to uphold the validity of patents can be substantial. If we are unsuccessful in such litigation, third parties may be able to use our patented technologies without paying licensing fees or royalties to us. Moreover, competitors may infringe our patents or successfully avoid them through design innovation. To prevent infringement or unauthorized use, we may need to file infringement claims, which are expensive and time- consuming. In addition, in an infringement proceeding, a court may decide that a patent of ours is not valid or may refuse to stop the other party from using the technology at issue on the grounds that its technology is not covered by our patents. Policing unauthorized use of our intellectual

property is difficult, and we cannot assure you that we will be able to prevent misappropriation of our proprietary rights, particularly in countries where the laws may not protect such rights as fully as in the United States. In addition to our patented technology, we also rely on unpatented technology, trade secrets and confidential information. We may not be able to effectively protect our rights to this technology or information. Other parties may independently develop substantially equivalent information and techniques or otherwise gain access to or disclose our technology. We require each of our employees, consultants and corporate partners to execute a confidentiality agreement at the commencement of an employment, consulting or collaborative relationship with us. However, these agreements may not provide effective protection of our technology or information or, in the event of unauthorized use or disclosure, they may not provide adequate remedies. If we fail to negotiate or maintain successful arrangements with third parties, our development and marketing activities may be delayed or reduced. We have entered into, and we expect to enter into in the future, arrangements with third parties to perform research, development, regulatory compliance, manufacturing or marketing activities relating to some or all of our product candidates. If we fail to secure or maintain successful collaborative arrangements, our development and marketing activities may be delayed or reduced. We may be unable to negotiate favorable collaborative arrangements that, if necessary, modify our existing arrangements on acceptable terms. Most of our agreements can be terminated under certain conditions by our partners. In addition, our partners may separately pursue competing products, therapeutic approaches or technologies to develop treatments for the diseases targeted by us or our efforts. Even if our partners continue their contributions to the collaborative arrangements, they may nevertheless determine not to actively pursue the development or commercialization of any resulting products. Also, our partners may fail to perform their obligations under the collaborative arrangements or may be slow in performing their obligations. In these circumstances, our ability to develop and market potential products could be severely limited.

Risks Related to our Industry

We face uncertainties over reimbursement and healthcare reform. In both domestic and foreign markets, future sales of our potential products, if any, will depend in part on the availability of reimbursement from third-party payors such as government health administration authorities, private health insurers and other organizations. Third-party payors are increasingly challenging the price and cost- effectiveness of medical products and services. Significant uncertainty exists as to the reimbursement status of newly-approved health care products. Even if we were to obtain regulatory approval, our product candidates may not be considered cost-effective and adequate third-party reimbursement may not be available to enable us to maintain price levels sufficient to realize an appropriate return on our investments in product development. Legislation and regulations affecting the pricing of pharmaceuticals may change before any of our product candidates is approved for marketing. Adoption of such legislation and regulations could further limit reimbursement for medical products and services. If the government and third party payors fail to provide adequate coverage and reimbursement rates for our potential products, the market acceptance of our products may be adversely affected.

We may be required to defend lawsuits or pay damages in connection with the alleged or actual harm caused by our product candidates.

We face an inherent business risk of exposure to product liability claims in the event that the use of our product candidates is alleged to have resulted in harm to others. This risk exists in clinical trials as well as in commercial distribution. In addition, the pharmaceutical and biotechnology industries in general have been subject to significant medical malpractice litigation. We may incur significant liability if product liability or malpractice lawsuits against us are successful. Although we maintain product liability insurance, we cannot be sure that this coverage is adequate or that it will continue to be available to us on acceptable terms.

We use hazardous materials in our business, and any claims relating to improper handling storage or disposal of these materials could harm our business.

Our research and development activities involve the controlled use of hazardous materials, chemicals, biological agents and radioactive compounds. We are subject to federal, state and local laws and regulations governing the use,

manufacture, storage, handling and disposal of such materials and certain waste products. Although we believe that our safety procedures for handling and disposing of such materials comply with the standards prescribed by such laws and regulations, the risk of accidental contamination or injury from these materials cannot be completely eliminated. In the event of such an accident, we could be held liable for any resulting damages, and any such liability could exceed our resources. We may be required to incur significant costs to comply with these laws in the future. Failure to comply with these laws could result in fines and the revocation of permits, which could prevent us from conducting our business.

Our stock price continues to experience large fluctuations, and you could lose some or all of your investment.

The market price of our stock has been and is likely to continue to be highly volatile. These price fluctuations have been rapid and severe. The market price of our common stock may fluctuate significantly in response to the following factors, most of which are beyond our control: |X| variations in our quarterly operating results; |X| changes in securities analysts' estimates of our financial performance; |X| changes in market valuations of similar companies; |X| announcements by us or our competitors of significant contracts, acquisitions, strategic partnerships, joint ventures or capital commitments; |X| additions or departures of key personnel; |X| future sales of common stock; |X| announcements by us or our competitors of technological innovations of new therapeutic products, clinical trial results and developments in patent or other proprietary rights; |X| announcements regarding government regulations, public concern as to the safety of drugs developed by us or others or changes in reimbursement policies; and

|X| fluctuations in stock market price and volume, which are particularly common among securities of biopharmaceutical companies.

We are at risk of securities class action litigation. In the past, securities class action litigation has often been brought against a company following a decline in the market price of its securities. This risk is especially relevant for us because biotechnology companies have experienced greater than average stock price volatility in recent years. Several years ago, we were the subject of a securities class action lawsuit, which was eventually dismissed with a determination that the plaintiffs had no basis for their claim. If we face such litigation in the future, it could result in substantial costs and a diversion of management's attention and resources, which could harm our business. We have implemented provisions in our charter documents that may ultimately delay, discourage or prevent a change in our management or control of us. Our certificate of incorporation and bylaws contain provisions that could make it more difficult for our stockholders to replace or remove our directors or to effect any other corporate action. These provisions include those which: |X| prohibit holders of less than ten percent of our outstanding capital stock from calling special meetings of stockholders; |X| prohibit stockholder action by written consent, thereby requiring stockholder actions to be taken at a meeting of our stockholders; and

|X| establish advance notice requirements for nominations for election to the board of directors or for proposing matters than can be acted upon by stockholders at stockholder meetings.

Moreover, our certificate of incorporation does not provide for cumulative voting in the election of directors, which would otherwise allow less than a majority of stockholders to elect director candidates. Some of the above provisions may also have possible anti-takeover effects, which may make an acquisition of us by a third party more difficult, even if such an acquisition could be beneficial to our stockholders. In addition, our certificate of incorporation also authorizes us to issue up to 20,000,000 shares of preferred stock in one or more different series with terms to be determined by our board of directors at time of issuance. As of September 30, 2001, an aggregate of 71,053 shares of preferred stock had been designated for issuance as Series A or Series B preferred stock by the board of directors and 4,991 shares of Series B preferred stock were issued and outstanding. Issuance of other shares of preferred stock could also be used as an anti-takeover device.

Item 3. Quantitative and Qualitative Disclosure About Market Risk

We are exposed to a variety of risks, including changes in interest rates affecting the return on our investments and foreign currency fluctuations. In the normal course of our business, we employ established policies and procedures to manage our exposure to fluctuations in interest rates and foreign currency values. Our exposure to market rate risk for changes in interest rates relate primarily to our investment portfolio. We attempt to place our investments with high quality issuers and, by policy, limit the amount of credit exposure to any one issuer and do not use derivative financial instruments in our investment portfolio. We maintain an investment portfolio of various issuers, types and maturities, which consist of both fixed and variable rate financial instruments. These securities are classified as available-for-sale, and consequently, are recorded on the balance sheet at fair value with unrealized gains or losses reported as a separate component in stockholders' equity, net of applicable taxes. At any time, sharp changes in interest rates can affect the value of our investment portfolio and its interest earnings. Currently, we do not hedge these interest rate exposures. However, through our money manager, we maintain management control systems to monitor interest rate risk. The risk management control systems use analytical techniques as well as other procedures to review interest rate risk. Assuming a hypothetical interest rate increase of 10%, the fair value of our total investment portfolio as of September 30, 2001 would have potentially incurred a loss of $263,000. Our exposure to foreign currency fluctuations is currently limited to our supply contract for Natrecor(R), which is denominated in German Marks. Changes in the exchange rate between German Marks and the U.S. dollar could adversely affect our manufacturing costs. All of our other contracts are denominated in U.S. dollars. Exposure to foreign currency exchange rate risk may change over time as our business evolves and our products are introduced into international markets. Currently, we do not hedge against any foreign currencies and, as a result, could incur unanticipated gains or losses.

PART II. OTHER INFORMATION

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits 10.48 First Amendment dated May 28, 2001 to Sublease Agreement dated May 24, 1999 for premises located at 749 North Mary Ave, Sunnyvale, California. 10.49 Amendment No. 5 dated July 24, 2001 to Lease Agreement dated January 22, 1993 for premises located at 820 Maude Avenue, Sunnyvale, California. 10.50 Letter dated June 10, 2001 to Extend Leases for premises located at 820 Maude Avenue, Sunnyvale, California. (b) Reports on Form 8-K

> Report on Form 8-K Filed on July 13, 2001. On July 10, 2001, Scios Inc., announced that it received a letter from the U.S. Food and Drug Administration stating that the Natrecor® (nesiritide) New Drug Application was approvable.
>
> Report on Form 8-K Filed on August 13, 2001. On August 13, 2001, Scios Inc. announced that it has received final approval from the U.S. Food and Drug Administration (FDA) to market Natrecor® (nesiritide) for the intravenous treatment of patients with acutely decompensated congestive heart failure who have shortness of breath (i.e., dyspnea) at rest or with minimal activity.
>
> Report on Form 8-K Filed on September 20, 2001. On September 20, 2001, Scios Inc. announced that, effective immediately, its Board of Directors authorized the repurchase of up to $10 million of Scios common stock.

Exhibit 10.48

First Amendment to Sublease Agreement Sublandlord: Trimble Navigation Limited Date: May 28, 2001 Subtenant: Scios Inc. Subject Properties 749 N. Mary Avenue, Sunnyvale, CA 94086 THIS FIRST AMENDMENT TO SUBLEASE ("Amendment") is made as of May 28, 2001 by and between Trimble Navigation Limited ("Trimble") and Scios Inc. ("Scios"). RECITALS A. Trimble and Scios have previously entered into that certain Sublease Agreement dated March 25, 1999 which Sublease covers certain Premises commonly known as 749 N. Mary Avenue, Sunnyvale, CA 94086 (the "749 N. Mary Sublease").

B. Under the terms of Section 7.2 of the parties aforesaid 749 N. Mary Sublease, Scios may exercise an option to extend the Sublease Term for one period of eleven (11) months from February 1, 2002 through December 31, 2002 (Option Term). Scios now wishes to exercise such option.

C. In addition, Scios wishes to further extend its sublease of the Premises for an additional twelve- (12) month period from January 1, 2003 through December 31, 2003 (extended Sublease Term). Trimble is willing to agree to such additional extended sublease period.

AGREEMENT NOW THEREFORE, in consideration for the agreements of Trimble and Scios contained herein and other valuable consideration, Trimble and Scios hereby amend their 749 N. Mary Sublease as follows: 1. Extended Sublease Term. The term of the 749 N. Mary Sublease shall be extended for the period commencing on February 1, 2002 and terminating on December 31, 2003 ("Extended Sublease Term"). 2. Extended Sublease Term Base Rent. Base Rent due and payable by Subtenant to Sublandlord during the Extended Sublease Term shall be as follows: Dates Base Rental Rate Monthly Rent ----- ---------------- ------------- February 1,2002- $1.95/SF/Mo $65,520.00/Mo December 31,2002 January 1, 2002- $2.20/SF/Mo $73,920.00/Mo December 31, 2003

3. Extension Condition; Cross Default. Sublandlord s agreement to extend the term of the 749 N. Mary Sublease from January 1, 2003 through December 31, 2003 under the terms of this First Amendment to Sublease is conditioned upon Subtenant s execution of that certain Sublease Agreement with respect to premises located at 617 N. Mary Ave., Sunnyvale, CA. (the 617 N. Mary Sublease) concurrently herewith. Subtenant hereby agrees that a default beyond any applicable cure period by Subtenant under the terms of the 617 N. Mary Sublease as amended shall be a default under the Sublease entitling the Sublandlord immediately to exercise its remedies thereunder.

4. Master Landlord Consent; Deemed exercise of Extension Option in Absence of Master Landlord s Consent. Subtenant acknowledges and agrees that Sublandlord s ability to extend the period of the 749 N. Mary Sublease from January 1, 2003 through December 31, 2003 is conditioned on the prior written consent of Master Landlord as provided in the Master Lease. Should Master Landlord refuse its consent to such extension of the term of the 749 N. Mary Sublease from January 1, 2003 through December 31, 2003 on terms acceptable to Sublandlord, this Amendment shall be deemed to be amended by the exclusion of the extension of the term from January 1, 2003 through December 31, 2003. In the event of such refusal to consent (1) Sublandlord shall not be responsible to Subtenant for any other costs or expenses Subtenant may have incurred by reason of its entering into this Amendment, and (2) Subtenant shall be deemed to have effectively exercised it option to extent the term of the Sublease in accordance with Section 7.2 of the 749 N. Mary Sublease, and the new expiration date of the term of the 749 N. Mary Sublease shall be December 31, 2002.

5. Entire Agreement. This Amendment contains the entire agreement of the parties

hereto with respect to its subject matter, and no representations, inducements, promises or agreements, oral or otherwise, between the parties, not embodied herein shall be of any force and effect.

5. Full Force and Effect. The parties acknowledge and agree that all other terms and conditions of the 749 N. Mary Sublease shall remain unchanged and in full force and effect. WITH INTENT TO BE BOUND, Trimble and Scios have signed this First Amendment to Sublease Agreement on the date set forth below. Trimble Navigation Limited By____/S/ Mary Ellen Genovese Date:___05/25/02_____________ ---------------------------- ------------------------- Mary Ellen Genovese Address for Notice: ------------------- Chief Financial Officer -- Trimble Navigation Limited Real Estate Dept. P.O. Box 3642 Sunnyvale, CA. 94088-3642 Scios Inc. By /S/ David W. Gryska Date:05/25/01 -----------------------------------

__________ David W. Gryska Address for Notice: ------------------ Chief Financial Officer - Scios Inc. 820 West Maude Avenue Sunnyvale, CA 94086

Exhibit 10.49

June 10, 2001 By Certified Mail John Arrillaga, Trustee Richard T. Peery, Trustee Perry/Arrillaga 2560 Mission College Blvd. Suite 101 Santa Clara, Ca. 95054 Re: Exercise of Options to Extend Through August 31, 2008; 810 and 820 West Maude Avenue, Sunnyvale, CA. Gentlemen: Scios Inc, (formerly known as Scios Nova Inc.) hereby exercises its right to extend the terms of the following two leases (collectively, the "Leases"): a) Lease Agreement dated January 22, 1993 regarding the premises located at 810 West Maude Avenue, Sunnyvale, CA (the address of which was changed to 820 West Maude Avenue as reflected in the Amendment No. 2), as amended by Amendment

No. 1 dated September 1, 1993, Amendment No. 2 dated December 27, 1993, Amendment No. 3 dated March 1, 1994, Landlords Consent to Assignment dated March 20, 1995, and Amendment No. 4 dated December 7, 1995: and

b) Lease Agreement dated November 17, 1995 regarding the premises located at 810 West Maude Avenue, Sunnyvale, CA.

As a Consequence of such exercise, the term of each of the Leases is hereby extended to August 31, 2008, in accordance with the terms of each Lease.

Sincerely, Scios Inc. By___/S/David W. Gryska --------------------------------- Name: David W. Gryska Title: Chief Financial Officer cc: Anna B. Pope, Esq.

Exhibit 10.50

AMENDMENT NO. 5

TO LEASE

THIS AMENDMENT NO. 5 is made and entered into this 15th day of June, 2001, by and between JOHN ARRILLAGA, Trustee, of his Successor Trustee UTA dated 7/20/77 (JOHN ARRILLAGA SURVIVOR'S TRUST) (previously known as the "John Arrillaga Separate Property Trust") as amended, and RICHARD T. PEERY, Trustee, or his Successor Trustee UTA dated 7/20/77 (RICHARD T. PEERY SEPARATE PROPERTY TRUST) as amended, collectively as LANDLORD, and SCIOS INC., a Delaware corporation, as TENANT. RECITALS

A. WHEREAS, by Lease Agreement dated January 22, 1993 Landlord leased to Alpha 1 Biomedicals, Inc., a Delaware corporation 15,018 ± square feet of that certain 51,680 ± square foot building located at 810 W. Maude Ave., Sunnyvale, California, the details of which are more particularly set forth in said January 22, 1993 Lease Agreement, and B. WHEREAS, said Lease was amended by Amendment No. 1 dated September 1, 1993 by changing the classification of parking spaces as set forth in Paragraph 45 of said Lease Agreement from sixty-four (64) nonexclusive parking spaces to eight (8) exclusive parking spaces and fifty-six (56) nonexclusive parking spaces, and, C. WHEREAS, said Lease was amended by Amendment No. 2 dated December 27, 1993 which: (i) changed the street address of Tenant s Leased Premises to 820 West Maude Avenue, (ii) increased the total square footage leased by 11,902 ± square feet or from 15,018 ± 26,920 ± square feet, (iii) extended the Lease Term for three (3) years five (5) months commencing on September 1, 1998 and ending on January 31, 2002, (iv) amended the Basic Rent schedule to reflect the increase in square footage and Term, (v) deleted Paragraph 46 (FIRST OPTION TO EXTENT LEASE FOR FIVE (5) YEARS) in its entirety and, (vi) replaced Paragraph 47 (SECOND OPTION TO EXTEND LEASE FOR FIVE (5) YEARS), and, D. WHEREAS, said Lease was amended by Amendment No. 3 dated March 1, 1994 which changed the effective date of the increase in square footage from February 1, 1994 to March 1, 1994 and amended the Basic Rent and Aggregate Rent accordingly, and, E. WHEREAS, said Lease was amended by Landlord s Consent to Assignment dated March 20, 1995 which was acknowledged the assignment of said Lease from Alpha 1 Biomedicals, Inc., to Scios Nova, Inc., and F. WHEREAS, said Lease was amended by Amendment No. 4 dated December 7, 1995 which added a Lease Co-Terminous Paragraph and a Cross Default Paragraph, and, G. WHEREAS, said Lease was amended by Letter Agreement dated September 17, 1996 whereby Landlord acknowledged Tenant s name change from Scios Nova, Inc. , a Delaware corporation to Scios Inc. , a Delaware corporation, effective March 26, 1996, and, H. WHEREAS, it is now the desire of the parties hereto amend the Lease by (i) extending the Term for six (6) years, seven (7) months, changing the Termination Date from January 31, 2002 to August 31, 2008, (ii) amending the Basic Rent schedule and Aggregate Rent accordingly, (iii) increasing the Security Deposit required under the Lease, (iv) amending Lease Paragraphs 9 (Taxes), and 12 (Property Insurance), (v) replacing Lease Paragraphs 10 (Liability Insurance), and 36 (Limitation of Liability), and (vi) adding paragraph (Authority to Execute) to said Lease Agreement as hereinafter set forth.

AGREEMENT NOW THEREFORE, for the valuable consideration, receipt of which is hereby acknowledged, and in consideration of the hereinafter mutual promises, the parties hereto do agree as follows: 1. TERM OF LEASE: Pursuant to Paragraph 8 of Amendment No. 2, Tenant has exercised its Option to Extend. Therefore it is ------------ agreed between the parties that the Term of said Lease Agreement shall be extended for an additional six (6) year, seven (7) month period, and the Lease Termination Date shall be changed from January 31, 2002 to August 31, 2008. 2. BASIC RENTAL FOR EXTENDED TERM OF LEASE: The monthly Basic Rental for the Extended Term of Lease shall be as follows: -------------------------------------- On February 1, 2002, the sum of THIRTY THREE THOUSAND SIX HUNDRED FIFTY AND NO/100 DOLLARS ($33,650.00) shall be due, and a like sum due on the first day of each month thereafter through and including August 1, 2002. On September 1, 2002, the sum of THIRTY FOUR THOUSAND NINE HUNDRED NINETY SIX AND NO/100 DOLLARS ($34,996.00) shall be due, and a like sum due on the first day of each month thereafter through and including August 1, 2003. On September 1, 2003,

the sum of THIRTY SIX THOUSAND THREE HUNDRED FORTY TWO AND NO/100 DOLLARS ($36,342.00) shall be due, and a like sum due on the first day of each month thereafter through and including August 1, 2004. On September 1, 2004, the sum of THIRTY SEVEN THOUSAND SIX HUNDRED EIGHTY EIGHT AND NO/100 DOLLARS ($37,688.00) shall be due, and a like sum due on the first day of each month thereafter through and including August 1, 2005. On September 1, 2005, the sum of THIRTY NINE THOUSAND THIRTY FOUR AND NO/100 DOLLARS ($39,034.00) shall be due, and a like sum due on the first day of each month thereafter through and including August 1, 2006. On September 1, 2006, the sum of FORTY THOUSAND THREE HUNDRED EIGHTY AND NO/100 DOLLARS ($40,380.00) shall be due, and a like sum due on the first day of each month thereafter through and including August 1, 2007. On September 1, 2007, the sum of FORTY ONE THOUSAND SEVEN HUNDRED TWENTY SIX AND NO/100 DOLLARS ($41,726.00) shall be due, and a like sum due on the first day of each month thereafter through and including August 1, 2008. The Aggregate Basic Rent for the Lease shall be increased by $2,997,542.00 or from $2,756.477.80 to $5,754,019.80. 3. SECURITY DEPOSIT: Tenant's Security Deposit shall be increased by $5,384.00, or from $67,300.00 to $72,684.00, payable upon ---------------- Tenant's execution of this Amendment No. 5. 4. TAXES: Lease Paragraph 9 ("Taxes") shall be amended to include the following language: -----

> The term Real Estate Taxes shall also include supplemental taxes related to the period of Tenant s Lease Term whenever levied, including any such taxes that may be levied after the Lease Term has expired .

5. PROPERTY INSURANCE: Lease Paragraph 12 ("Property Insurance") is hereby amended to include the following: "Tenant ------------------ acknowledges that as part of the cost of insurance policies for the Premises, Tenant is responsible for the payment of insurance deductibles on insurance claims as they relate to the Premises". 6. LIABILITY INSURANCE: Lease Paragraph 10 ("Liability Insurance") shall be deleted and replaced in its entirety by the ------------------- following: "10. LIABILITY INSURANCE: Tenant, at Tenant's expense, agrees to keep in force during the Team of this Lease a ------------------- policy of commercial general liability insurance with combined single limit coverage of not less than Two Million Dollars ($2,000,000) per occurrence for bodily injury and property damage occurring in, on or about the Premises, including parking and landscaped areas. Such insurance shall be primary and noncontributory as respects any insurance carried by Landlord. The policy or polices effecting such insurance shall name Landlord as additional insureds, and shall insure any liability of Landlord, contingent or otherwise, as respects acts or omissions of Tenant, its agents, employees or invitees or otherwise by any conduct or transactions of any of said persons in or about or concerning the Premises, including any failure of Tenant to observe or perform any of its obligations hereunder; shall be issued by an insurance company admitted to transact business in the State of California; and shall provide that the insurance effected thereby shall not be canceled, except upon thirty (30) days' prior written notice to Landlord. A certificate of insurance of said policy shall be delivered to Landlord. If, during the Term of this Lease, in the considered opinion of Landlord's Lender, insurance advisor, or counsel, the amount of insurance described in this Paragraph is not adequate, Tenant agrees to increase said coverage to such reasonable amount as Landlord's Lender, insurance advisor, or counsel shall deem adequate." 7. LIMITATION OF LIABILITY: Lease Paragraph 36 ("Limitations of Liability") shall be deleted and replaced in its entirety by the following: "36. LIMITATION OF LIABILITY: In consideration of the benefits accruing hereunder, Tenant and all successors and ---------------------- assigns covenant and agree that, in the event of any actual or alleged failure, breach or default hereunder by Landlord: (i) the sole and exclusive remedy shall be against Landlord's interest in the Premises leased herein; (ii) no partner of Landlord shall be sued or named as a party in any suit or action (except as may be necessary to secure jurisdiction of the partnership); (iii) no service of process shall be made against any partner of Landlord (except as may be necessary to secure jurisdiction of the partnership); (iv) no partner of Landlord shall be required to answer or otherwise plead to any service of process; (v) no judgement will be taken against any partner of Landlord; (vi) any judgement taken against any partner of Landlord may be vacated and set aside at any time without hearing; (vii) no writ of execution will ever be levied against the assets of any partner of Landlord; (viii) these covenants and agreements are enforceable both by Landlord and also by any partner of Landlord.

> Tenant agrees that each of the foregoing covenants and agreements shall be applicable to any covenant or agreement either expressly contained in this Lease or imposed by statute or at common law.

8. AUTHORITY TO EXECUTE. The parties executing this Agreement hereby warrant and represent that they are properly authorized to execute this Agreement and bind the parties on behalf of whom they execute this Agreement and to all of the terms, covenants and conditions of this Agreement as they relate to the respective parties hereto.

EXCEPT AS MODIFIED HEREIN, all other terms, covenants, and conditions of said January 22, 1993 Lease Agreement shall remain in full force and effect. IN WITNESS WHEREOF, Landlord and Tenant have executed this Amendment No. 5 to Lease as of the day and year least written below. LANDLORD: TENANT: JOHN ARRILLAGA SURVIVOR'S SCIOS INC., TRUST a Delaware corporation By/s/ John Arrillaga By/s/ David W. Gryska ------------------------------ ---------------------------------- John Arrillaga, Trustee Date: 7/24/01 David W. Gryska ------------------------- ------------------------------------ Print or Type Name RICHARD T. PERRY SEPARATE Title: CFO ------------------------------ PROPERTY TRUST By/s/ Richard T. Peery Date: 7/20/01 ------------------------------ ------------------------------- Richard T. Peery, Trustee Date: 7/24/01 --------------------------- SIGNATURES Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized. SCIOS INC. November 8, 2001 By: /s/ Richard B. Brewer ---------------------- Richard B. Brewer, President and CEO November 8, 2001 By: /s/ David W. Gryska -------------------- David W. Gryska, Senior Vice President and CFO 2
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575,485

606,835

Total liabilities and equity

$
2,383,529

$
2,441,748

See accompanying notes to unaudited condensed consolidated financial statements.

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HARSCO CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

	Three Months Ended June 30		Six Months Ended June 30	
(In thousands, except per share amounts)	2014	2013	2014	2013
Revenues from continuing operations:				
Service revenues	$361,199	$584,908	$712,209	$1,136,063
Product revenues	173,378	174,828	335,067	339,068
Total revenues	534,577	759,736	1,047,276	1,475,131
Costs and expenses from continuing operations:				
Cost of services sold	296,801	460,305	590,800	903,701
Cost of products sold	120,657	116,849	236,123	237,711
Selling, general and administrative expenses	77,969	125,623	144,763	250,321
Research and development expenses	1,983	2,184	4,602	4,380
Loss on disposal of the Harsco Infrastructure Segment and transaction costs	3,415	—	5,553	—
Other expenses	27,516	3,928	26,860	2,386
Total costs and expenses	528,341	708,889	1,008,701	1,398,499
Operating income from continuing operations	6,236	50,847	38,575	76,632
Interest income	410	830	707	1,236
Interest expense	(11,958)	(12,855)	(23,379)	(24,598)
Change in fair value to the unit adjustment liability	(2,473)	—	(5,019)	—
Income (loss) from continuing operations before income taxes and equity income (loss)	(7,785)	38,822	10,884	53,270
Income tax expense	(4,258)	(11,508)	(8,753)	(16,473)
Equity in income (loss) of unconsolidated entities, net	(3,008)	595	(4,238)	581
Income (loss) from continuing operations	(15,051)	27,909	(2,107)	37,378
Discontinued operations:				
Income (loss) on disposal of discontinued business	1,732	(863)	1,092	(1,505)
Income tax (expense) benefit related to discontinued business	(642)	330	(405)	575
Income (loss) from discontinued operations	1,090	(533)	687	(930)
Net income (loss)	(13,961)	27,376	(1,420)	36,448
Less: Net income attributable to noncontrolling interests	(14)	(3,578)	(1,416)	(5,405)
Net income (loss) attributable to Harsco Corporation	$(13,975)	$23,798	$(2,836)	$31,043
Amounts attributable to Harsco Corporation common stockholders:				
Income (loss) from continuing operations, net of tax	$(15,065)	$24,331	$(3,523)	$31,973
Income (loss) from discontinued operations, net of tax	1,090	(533)	687	(930)
Net income (loss) attributable to Harsco Corporation common stockholders	$(13,975)	$23,798	$(2,836)	$31,043
Weighted-average shares of common stock outstanding	80,885	80,760	80,850	80,733
Basic earnings (loss) per common share attributable to Harsco Corporation common stockholders:				
Continuing operations	$(0.19)	$0.30	$(0.04)	$0.40
Discontinued operations	0.01	(0.01)	0.01	(0.01)
Basic earnings (loss) per share attributable to Harsco Corporation common stockholders	$(0.17) (a)	$0.29	$(0.04) (a)	$0.39

Diluted weighted-average shares of common stock outstanding	80,885	81,004	80,850	80,967
Diluted earnings (loss) per common share attributable to Harsco Corporation common stockholders:				
Continuing operations	$(0.19)	$0.30	$(0.04)	$0.39
Discontinued operations	0.01	(0.01)	0.01	(0.01)
Diluted earnings (loss) per share attributable to Harsco Corporation common stockholders	$(0.17) (a)	$0.29	$(0.04) (a)	$0.38
Cash dividends declared per common share	$0.205	$0.205	$0.41	$0.41

(a) Does not total due to rounding

See accompanying notes to unaudited condensed consolidated financial statements.

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HARSCO CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (Unaudited)

	Three Months Ended June 30	
(In thousands)	2014	2013
Net income (loss)	$(13,961)	$27,376
Other comprehensive income (loss):		
Foreign currency translation adjustments, net of deferred income taxes of $(359) and $(1,500) in 2014 and 2013, respectively	3,017	(34,539)
Net gain (loss) on cash flow hedging instruments, net of deferred income taxes of $282 and $1,206 in 2014 and 2013, respectively	2,096	(1,525)
Pension liability adjustments, net of deferred income taxes of $333 and $(457) in 2014 and 2013, respectively	(3,005)	3,220
Unrealized gain on marketable securities, net of deferred income taxes of $(5) in 2014	9	—
Total other comprehensive income (loss)	2,117	(32,844)
Total comprehensive loss	(11,844)	(5,468)
Less: Comprehensive (income) loss attributable to noncontrolling interests	100	(2,946)
Comprehensive loss attributable to Harsco Corporation	$(11,744)	$(8,414)

	Six Months Ended June 30	
(In thousands)	2014	2013
Net income (loss)	$(1,420)	$36,448
Other comprehensive income (loss):		
Foreign currency translation adjustments, net of deferred income taxes of $(460) and 7,555 in 2014 and 2013, respectively	1,747	(46,555)
Net gain (loss) on cash flow hedging instruments, net of deferred income taxes of $668 and $769 in 2014 and 2013, respectively	(1,867)	536
Pension liability adjustments, net of deferred income taxes of $(73) and $(4,548) in 2014 and 2013, respectively	676	31,223
Unrealized gain on marketable securities, net of deferred income taxes of $(2) and $(5) in 2014 and 2013, respectively	4	8
Total other comprehensive income (loss)	560	(14,788)
Total comprehensive income (loss)	(860)	21,660
Less: Comprehensive income attributable to noncontrolling interests	(1,002)	(4,595)
Comprehensive income (loss) attributable to Harsco Corporation	$(1,862)	$17,065

See accompanying notes to unaudited condensed consolidated financial statements.

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HARSCO CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

	Six Months Ended June 30	
(In thousands)	2014	2013
Cash flows from operating activities:		
Net income (loss)	$(1,420)	$36,448
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation	84,333	121,640
Amortization	6,046	8,847
Change in fair value to the unit adjustment liability	5,019	—
Deferred income tax expense (benefit)	2,274	(2,528)
Equity in (income) loss of unconsolidated entities, net	4,238	(581)
Loss on disposal of Harsco Infrastructure Segment	3,865	—
Other, net	16,926	(2,157)
Changes in assets and liabilities:		
Accounts receivable	(30,945)	(47,398)
Inventories	(12,884)	(13,363)
Accounts payable	(7,172)	9,949
Accrued interest payable	704	566
Accrued compensation	2,072	(14,782)
Advances on contracts	32,870	(9,063)
Harsco Infrastructure Segment 2010 Restructuring Program accrual	—	(295)
Harsco 2011/2012 Restructuring Program accrual	(2,198)	(10,950)
Other assets and liabilities	(29,279)	(19,964)
Net cash provided by operating activities	74,449	56,369
Cash flows from investing activities:		
Purchases of property, plant and equipment	(81,615)	(120,191)
Proceeds from the Infrastructure Transaction	15,699	—
Proceeds from sales of assets	6,120	14,853
Purchases of businesses, net of cash acquired	(26,046)	—
Payment of unit adjustment liability	(11,160)	—
Other investing activities, net	(1,926)	(2,400)
Net cash used by investing activities	(98,928)	(107,738)
Cash flows from financing activities:		
Short-term borrowings, net	(1,570)	4,188
Current maturities and long-term debt:		
Additions	108,431	127,395
Reductions	(62,595)	(51,277)
Cash dividends paid on common stock	(33,146)	(33,093)
Dividends paid to noncontrolling interests	(1,586)	(2,655)
Contributions from noncontrolling interests	—	4,502
Purchase of noncontrolling interests	—	(166)
Common stock issued - options	—	371
Other financing activities, net	(2)	—
Net cash provided by financing activities	9,532	49,265

Effect of exchange rate changes on cash	(1,191)	(4,145)
Net decrease in cash and cash equivalents	(16,138)	(6,249)
Cash and cash equivalents at beginning of period	93,605	95,250
Cash and cash equivalents at end of period	$77,467	$89,001

See accompanying notes to unaudited condensed consolidated financial statements.

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HARSCO CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF EQUITY (Unaudited)

	Harsco Corporation Stockholders' Equity						
	Common Stock						
(In thousands, except share and per share amounts)	Issued	Treasury	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Noncontrolling Interests	Total
Balances, January 1, 2013	$140,080	$(745,205)	$152,645	$1,675,490	$(411,168)	$49,782	$861,624
Net income				31,043		5,405	36,448
Cash dividends declared:							
Common @ $0.41 per share				(33,110)			(33,110)
Noncontrolling interests						(2,655)	(2,655)
Total other comprehensive loss, net of deferred income taxes of $3,771					(13,978)	(810)	(14,788)
Contributions from noncontrolling interests						4,502	4,502
Purchase of subsidiary shares from noncontrolling interest			(292)			107	(185)
Stock options exercised, net 20,000 shares	25		362				387
Vesting of restricted stock units and other stock grants, net 60,674 shares	117	(840)	2,059				1,336
Amortization of unearned portion of stock-based compensation, net of forfeitures			2,185				2,185
Balances, June 30, 2013	$140,222	$(746,045)	$156,959	$1,673,423	$(425,146)	$56,331	$855,744

	Harsco Corporation Stockholders' Equity						
	Common Stock						
(In thousands, except share and per share amounts)	Issued	Treasury	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Noncontrolling Interests	Total
Balances, January 1, 2014	$140,248	$(746,237)	$159,025	$1,381,321	$(370,615)	$43,093	$606,835
Net income (loss)				(2,836)		1,416	(1,420)
Cash dividends declared:							
Common @ $0.41 per share				(33,174)			(33,174)
Noncontrolling interests						(1,719)	(1,719)
Total other comprehensive income (loss), net of deferred income taxes of $130					974	(414)	560
Contributions from noncontrolling interests						1,560	1,560
Noncontrolling interests transferred in the Infrastructure Transaction.						(905)	(905)
Vesting of restricted stock units and other stock grants, net 124,532 shares	187	(693)	1,933				1,427

Amortization of unearned portion of stock-based compensation, net of forfeitures			2,321				2,321
Balances, June 30, 2014	$140,435	$(746,930)	$163,279	$1,345,311	$(369,641)	$43,031	$575,485

See accompanying notes to unaudited condensed consolidated financial statements.

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HARSCO CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. Basis of Presentation

Harsco Corporation (the "Company") has prepared these unaudited condensed consolidated financial statements based on Securities and Exchange Commission rules that permit reduced disclosure for interim periods. In the opinion of management, all adjustments (all of which are of a normal recurring nature) that are necessary for a fair presentation are reflected in the unaudited condensed consolidated financial statements. The December 31, 2013 Condensed Consolidated Balance Sheet information contained in this Quarterly Report on Form 10-Q was derived from the 2013 audited consolidated financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America ("U.S. GAAP") for an annual report. The unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements, including the notes thereto, included in the Company's Annual Report on Form 10-K for the year ended December 31, 2013.

Operating results and cash flows for the three and six months ended June 30, 2014 are not indicative of the results that may be expected for the year ending December 31, 2014.

During the second quarter of 2014, the Company recorded out-of-period adjustments that had the net effect of decreasing after-tax income by $1.7 million, or $0.02 per diluted share, for the second quarter of 2014. The adjustments are primarily the result of correcting expenses that should not have been capitalized in accordance with the Company's policies and revenue that should not have been recorded in accordance with a customer contract. The Company assessed the individual and aggregate impact of these adjustments on the current year and all prior periods and determined that the cumulative effect of the adjustments was not material to the expected full-year 2014 results, and did not result in a material misstatement to any previously issued annual or quarterly financial statements. Consequently, the Company recorded the $1.7 million net adjustment in the second quarter of 2014 and has not revised any previously issued annual financial statements or interim financial data.

2. Recently Adopted and Recently Issued Accounting Standards

The following accounting standards have been adopted in 2014:

On January 1, 2014, the Company adopted Financial Accounting Standards Board ("FASB") issued changes related to a parent's accounting for the cumulative translation adjustment upon derecognition of certain subsidiaries or groups of assets within a foreign entity or of an investment in a foreign entity. The changes resolve diversity in practice related to these matters. The adoption of these changes did not have a material impact on the Company's consolidated financial statements.

On January 1, 2014, the Company adopted FASB issued changes related to financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists that could be used to offset the liability for an uncertain tax position. The changes resolve diversity in practice related to these matters. The adoption of these changes did not have a material impact on the Company's consolidated financial statements.

The following accounting standards have been issued and become effective for the Company at a future date:

In April 2014, the FASB issued changes related to reporting discontinued operations and disclosure of disposals of components of an entity. The changes modify the criteria related to what transactions constitute discontinued operations and expands disclosure requirements. The changes become effective for the Company, prospectively, on January 1, 2015. Management has determined that these changes will not have a material impact on the Company's consolidated financial statements.

In May 2014, the FASB issued changes related to the recognition of revenue from contracts with customers. The changes clarify the principles for recognizing revenue and develop a common revenue standard. The core principle of the changes is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The changes also require additional disclosures related to revenue recognition. The changes become

effective for the Company on January 1, 2017. Management is currently evaluating these changes.

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3. Acquisitions and Dispositions

Acquisitions
In January 2014, the Company acquired Hammco Corporation ("Hammco"), a U.S. manufacturer of high specification air-cooled heat exchangers for the natural gas and petrochemical processing markets. Hammco has been included in the results of the Harsco Industrial Segment. Inclusion of pro forma financial information for this transaction is not necessary due to the immaterial size of the acquisition. The purchase price allocation is not yet final for this acquisition.

Dispositions
In November 2013, the Company consummated the previously announced transaction to sell the Company's Harsco Infrastructure Segment into a strategic venture with Clayton, Dubilier & Rice ("CD&R") as part of a transaction that combines the Harsco Infrastructure Segment with Brand Energy & Infrastructure Services, Inc., which CD&R simultaneously acquired (the "Infrastructure Transaction"). The Company has contributed substantially all of the Company's equity interest in, and the net assets of, the Harsco Infrastructure Segment to the strategic venture in exchange for $300 million, subject to working capital and other adjustments, and an approximate 29% equity interest in the resulting entity (the "Infrastructure strategic venture" or "Brand"). The Company's equity interest in the Infrastructure strategic venture is accounted for under the equity method of accounting as prescribed by U.S. GAAP. See Note 5, Equity Method Investments, for additional information on equity method investments.

As a result of the Infrastructure Transaction, the Company recorded an estimated loss on disposal of the Harsco Infrastructure Segment of $271.3 million during 2013 and recorded an additional loss of $3.2 million and $3.9 million during the three and six months ended June 30, 2014, respectively. The Company does not anticipate any further adjustments to the loss on disposal of the Harsco Infrastructure Segment. See Note 1, Summary of Significant Accounting Policies, and Note 3, Acquisitions and Dispositions, to the Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2013 for additional information on the Company's policy on impairment of long-lived assets (other than goodwill) and the loss on disposal of the Harsco Infrastructure Segment.

Additionally, the Company incurred $0.2 million and $1.7 million of transaction costs during the three and six months ended June 30, 2014, respectively, in conjunction with the Infrastructure Transaction.

4. Accounts Receivable and Inventories
Accounts receivable consist of the following:

(In thousands)	June 30 2014	December 31 2013
Trade accounts receivable	$398,471	$359,819
Less: Allowance for doubtful accounts	(13,837)	(6,638)
Trade accounts receivable, net	$384,634	$353,181
Other receivables (a)	$33,604	$46,470

(a) Other receivables include insurance claim receivables, employee receivables, tax claim receivables, receivables from affiliates and other miscellaneous receivables not included in Trade accounts receivable, net.
The provision for doubtful accounts related to trade accounts receivable was as follows:

	Three Months Ended June 30		Six Months Ended June 30	
(In thousands)	2014	2013	2014	2013

Provision for doubtful accounts related to trade accounts receivable	$7,364	$2,621	$7,345	$4,838

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The increase in the Allowance for doubtful accounts since December 31, 2013 and the Provision for doubtful accounts related to trade accounts receivable for both the three and six months ended June 30, 2014 relate to two European customers in the Harsco Metals & Minerals Segment.
Inventories consist of the following:

(In thousands)	June 30 2014	December 31 2013
Finished goods	$25,130	$23,112
Work-in-process	33,022	25,623
Raw materials and purchased parts	85,731	72,118
Stores and supplies	32,465	34,836
Inventories	$176,348	$155,689

5. Equity Method Investments

As a result of the Infrastructure Transaction, the Company possessed an approximate 29% equity interest in Brand at June 30, 2014. See Note 3, Acquisitions and Dispositions, for additional information related to the Infrastructure Transaction.

Brand is a leading provider of specialized services to the global energy, industrial and infrastructure markets that combines a global footprint, broad service offerings and rigorous operating processes to support customer required facility maintenance and turnaround needs and capital driven upgrade and expansion plans. Brand's range of services includes work access, corrosion management, atmospheric and immersion coatings, insulation services, fireproofing and refractory, mechanical services, forming and shoring and other complementary specialty services. Brand delivers services through a global network of strategically located branches in six continents with a particular focus on major hydrocarbon and power generation markets globally. In addition, Brand has co-located branches at energy-related customer facilities providing a consistent presence for required maintenance work.

The book value of the Company's investment in Brand at June 30, 2014 was $289.7 million. The Company records the Company's proportionate share of Brand's net income or loss one quarter in arrears. Brand's results of operations for the three month period ended March 31, 2014 and the period from November 27, 2013 through March 31, 2014 are summarized as follows:

(In thousands)	Three Months Ended March 31 2014	Period From November 27 2013 Through March 31 2014 (a)
Summarized Statement of Operations Information of Brand:		
Net revenues	$741,763	$977,857
Gross profit	147,805	196,637
Net loss attributable to Brand Energy & Infrastructure Services, Inc. and Subsidiaries	(10,366)	(14,607)
Harsco's equity in loss of Brand	(3,009)	(4,239)

(a) The Company's equity method investment in Brand began on November 26, 2013; accordingly, there is only approximately four months of related equity loss. The results of the Harsco Infrastructure Segment from January 1, 2013 through the date of closing are reported in the Company's results of operations for 2013.

As part of the Infrastructure Transaction, the Company is required to make a quarterly payment to the Company's partner in the Infrastructure strategic venture, either (at the Company's election) (i) in cash, with total payments to equal approximately $22 million per year on a pre-tax basis (approximately $15 million per year after-tax), or (ii) in kind through the transfer of approximately 2.5% of the Company's ownership interest in the Infrastructure strategic venture on an annual basis (the "unit adjustment liability"). The resulting liability is reflected in the caption, Unit adjustment liability, on the Company's Condensed Consolidated Balance Sheets. The Company will recognize the change in fair value to the unit adjustment liability each period until the Company is no longer required to make these payments or chooses not to make these payments. The change in fair value to the unit adjustment liability is a non-cash expense. For the three and six months ended June 30, 2014, the Company recognized $2.5 million and $5.0 million, respectively, of change in fair value to the unit adjustment liability.

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The Company's obligation to make a quarterly payment will cease upon the earlier of (i) Brand achieving $487.0 million in last twelve months' earnings before interest, taxes, depreciation and amortization for three quarters, which need not be consecutive, or (ii) eight years after the closing of the Infrastructure Transaction. In addition, upon the initial public offering of Brand, the Company's quarterly payment obligation will decrease by the portion of CD&R's ownership interest sold or eliminated completely once CD&R's ownership interest in Brand falls below 20%. In the event of a liquidation of Brand, CD&R is entitled to a liquidation preference of approximately $336 million, plus any quarterly payments that had been paid in kind.

The Condensed Consolidated Balance Sheets as of June 30, 2014 and December 31, 2013 include balances related to the unit adjustment liability of $100.2 million and $106.3 million, respectively, in the current and non-current captions, Unit adjustment liability.

The Company intends to make these quarterly payments in cash and will continue to evaluate the implications of making payments in cash or in kind based upon performance of the Infrastructure strategic venture. In the future, should the Company decide not to make the cash payment, the value of both the equity method investment in Brand and the related unit adjustment liability may be impacted, and the change may be reflected in earnings in that period.

Within Brand's equity structure, there exists the ability for the issuance of equity incentive compensation for certain executive employees, which has the potential of diluting the Company's ownership interest in Brand by approximately 2.9% if all such awards are issued and vested.

Balances related to transactions between the Company and Brand are as follows:

(In thousands)	June 30 2014	December 31 2013
Balances due from Brand	$8,872	$85,908
Balances due to Brand	41,306	149,325

These balances between the Company and Brand relate primarily to the finalization of the Infrastructure Transaction, including transition services and the funding of certain transferred defined benefit pension plan obligations through 2018. There is not expected to be any significant level of revenue or expense between the Company and Brand on an ongoing basis once all aspects of the Infrastructure Transaction have been finalized.

No instances of impairment were noted on the Company's equity method investments as of June 30, 2014.

6. Property, Plant and Equipment

Property, plant and equipment consists of the following:

(In thousands)	June 30 2014	December 31 2013
Land	$18,796	$16,652
Land improvements	14,245	13,615
Buildings and improvements	214,169	192,346
Machinery and equipment	2,003,319	1,969,493
Uncompleted construction	86,959	86,508
Gross property, plant and equipment	2,337,488	2,278,614
Less: Accumulated depreciation	(1,628,877)	(1,567,268)
Property, plant and equipment, net	$708,611	$711,346

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7. Goodwill and Other Intangible Assets

The following table reflects the changes in carrying amounts of goodwill by segment for the six months ended June 30, 2014:

(In thousands)	Harsco Metals & Minerals Segment	Harsco Industrial Segment	Harsco Rail Segment	Consolidated Totals
Balance at December 31, 2013	$421,955	$—	$9,310	$431,265
Changes to goodwill (a)	—	6,717	—	6,717
Foreign currency translation	2,186	—	—	2,186
Balance at June 30, 2014	$424,141	$6,717	$9,310	$440,168

(a) Changes to goodwill relate to the initial acquisition of Hammco and related purchase price adjustments in accordance with U.S. GAAP occurring during the measurement period. See Note 3, Acquisitions and Dispositions.

The Company tests for goodwill impairment annually or more frequently if indicators of impairment exist or if a decision is made to dispose of a business. The Company performs its annual goodwill impairment test as of October 1 and monitors for triggering events on an ongoing basis. The Company determined that, as of June 30, 2014, no interim goodwill impairment testing was necessary. There can be no assurance that the Company’s annual goodwill impairment testing will not result in a charge to earnings. Any impairment could result in the write-down of the carrying value of goodwill to its implied fair value.

Intangible assets consist of the following:

	June 30, 2014		December 31, 2013	
(In thousands)	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Customer related	$165,842	$114,799	$150,307	$110,889
Non-compete agreements	1,125	1,040	1,126	1,024
Patents	6,285	5,441	6,211	5,273
Technology related	27,151	20,311	27,185	18,931
Trade names	7,759	3,356	4,113	2,969
Other	7,589	4,368	7,753	4,348
Total	$215,751	$149,315	$196,695	$143,434

Amortization expense for intangible assets was as follows:

	Three Months Ended June 30		Six Months Ended June 30	
(In thousands)	2014	2013	2014	2013
Amortization expense for intangible assets	$2,593	$3,904	$5,146	$7,852

The estimated amortization expense for the next five fiscal years based on current intangible assets is as follows:

(In thousands)	2014	2015	2016	2017	2018
Estimated amortization expense (b)	$10,000	$8,750	$8,250	$5,250	$5,000

(b) These estimated amortization expense amounts do not reflect the potential effect of future foreign currency exchange fluctuations.

8. Employee Benefit Plans

Three Months Ended
June 30

Defined Benefit Pension Plans Net Periodic Pension Cost	U. S. Plans		International Plans	
(In thousands)	2014	2013	2014	2013
Service cost	$558	$642	$411	$900
Interest cost	3,217	2,944	11,012	10,762
Expected return on plan assets	(4,196)	(3,913)	(12,708)	(11,800)
Recognized prior service costs	22	35	47	94
Recognized loss	838	1,264	3,583	4,149
Settlement/curtailment (gains) losses	—	—	56	(289)
Defined benefit pension plans net periodic pension cost	$439	$972	$2,401	$3,816

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Defined Benefit Pension Plans Net Periodic Pension Cost (In thousands)	Six Months Ended June 30 U. S. Plans 2014	2013	International Plans 2014	2013
Service cost	$1,116	$1,283	$818	$1,808
Interest cost	6,434	5,884	21,924	21,545
Expected return on plan assets	(8,392)	(7,822)	(25,296)	(23,619)
Recognized prior service costs	44	72	93	184
Recognized loss	1,676	2,526	7,136	8,300
Settlement/curtailment (gains) losses	—	—	56	(289)
Defined benefit pension plans net periodic pension cost	$878	$1,943	$4,731	$7,929

Company Contributions (In thousands)	Three Months Ended June 30 2014	2013	Six Months Ended June 30 2014	2013
Defined benefit pension plans:				
United States	$582	$565	$1,148	$1,048
International	4,316	3,320	21,737	20,956
Multiemployer pension plans	966	5,699	1,667	8,515
Defined contribution pension plans	2,930	4,070	6,999	8,821

The Company currently anticipates contributing approximately $9 million and $10 million to the U.S. and international defined benefit pension plans, respectively, during the remainder of 2014.

9. Income Taxes

The effective income tax rate related to continuing operations for the three and six months ended June 30, 2014 was (54.7)% and 80.4%, respectively, compared with 29.6% and 30.9% for the three and six months ended June 30, 2013, respectively. The effective income tax rate related to continuing operations and income tax expense from continuing operations changed primarily due to the change in income (loss) from continuing operations and changes in losses generated in certain jurisdictions where no tax benefit can be recognized for both the three and six months ended June 30, 2014 compared with the three and six months ended June 30, 2013.

An income tax benefit from an uncertain tax position may be recognized when it is more likely than not that the position will be sustained upon examination, based on technical merits, including resolutions of any related appeals or litigation processes. The unrecognized income tax benefit at June 30, 2014 was $18.5 million, including interest and penalties. Within the next twelve months, it is reasonably possible that up to $0.7 million of unrecognized income tax benefits will be recognized upon settlement of tax examinations and the expiration of various statutes of limitations.

The U.S. Internal Revenue Service completed its audit of the Company's 2010 income tax return in July 2014 and made no changes to the reported tax.

10. Commitments and Contingencies

Environmental

The Company is involved in a number of environmental remediation investigations and cleanups and, along with other companies, has been identified as a “potentially responsible party” for certain waste disposal sites. While each of these

matters is subject to various uncertainties, it is probable that the Company will agree to make payments toward funding certain of these activities and it is possible that some of these matters will be decided unfavorably to the Company. The Company has evaluated its potential liability, and its financial exposure is dependent upon such factors as the continuing evolution of environmental laws and regulatory requirements, the availability and application of technology, the allocation of cost among potentially responsible parties, the years of remedial activity required and the remediation methods selected. The Condensed Consolidated Balance Sheets as of June 30, 2014 and December 31, 2013 include accruals in Other current liabilities of $1.3 million and $1.2 million, respectively, for environmental matters. The amounts charged against Income (loss) from continuing operations before income taxes and equity income (loss) related to environmental matters totaled $0.7 million and $1.3 million for the three and six months ended June 30, 2014, respectively. The amounts charged against pre-tax income related to environmental matters totaled $0.3 million and $0.6 million for the three and six months ended June 30, 2013, respectively.

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The Company evaluates its liability for future environmental remediation costs on a quarterly basis. Although actual costs to be incurred at identified sites in future periods may vary from the estimates (given inherent uncertainties in evaluating environmental exposures), the Company does not expect that any costs that are reasonably possible to be incurred by the Company in connection with environmental matters in excess of the amounts accrued would have a material adverse effect on the Company's financial condition, results of operations or cash flows.

Brazilian Tax Disputes

The Company is involved in a number of tax disputes with federal, state and municipal tax authorities in Brazil. These disputes are at various stages of the legal process, including the administrative review phase and the collection action phase, and include assessments of fixed amounts of principal and penalties, plus interest charges that increase at statutorily determined amounts per month and are assessed on the aggregate amount of the principal and penalties. In addition, the losing party at the collection action or court of appeals phase could be subject to a charge to cover statutorily mandated legal fees, which are generally calculated as a percentage of the total assessed amounts due, inclusive of penalty and interest. A large number of the claims relate to value-added ("ICMS") services and social security ("INSS") tax disputes. The largest proportion of the assessed amounts relate to ICMS claims filed by the State Revenue Authorities from the State of São Paulo, Brazil (the "SPRA"), encompassing the period from January 2002 to May 2005.

In October 2009, the Company received notification of the SPRA's final administrative decision regarding the levying of ICMS in the State of São Paulo in relation to services provided to a customer in the State between January 2004 and May 2005. As of June 30, 2014, the principal amount of the tax assessment from the SPRA with regard to this case was approximately $3 million, with penalty, interest and fees assessed to date increasing such amount by an additional $29 million. Any change in the aggregate amount since the Company's Annual Report on Form 10-K for the year ended December 31, 2013 reflects an increase in assessed interest and statutorily mandated legal fees for the period and includes the effect of foreign currency translation.

Another ICMS tax case involving the SPRA refers to the tax period from January 2002 to December 2003. This case is still pending at the administrative phase, where the aggregate amount assessed by the tax authorities in August 2005 was$11.5 million (the amounts with regard to this claim are valued as of the date of the assessment since it has not yet reached the collection phase), composed of a principal amount of $2.7 million, with penalty and interest assessed through that date increasing such amount by an additional $8.8 million. All such amounts include the effect of foreign currency translation.

The Company continues to believe it is not probable that it will incur a loss for these assessments by the SPRA. The Company also continues to believe that sufficient coverage for these claims exists as a result of the Company's customer's indemnification obligations and such customer's pledge of assets in connection with the October 2009 notice, as required by Brazilian procedure.

The Company intends to continue its practice of vigorously defending itself against these tax claims under various alternatives, including judicial appeal. The Company will continue to evaluate its potential liability with regard to these claims on a quarterly basis; however, it is not possible to predict the ultimate outcome of these tax-related disputes in Brazil. No loss provision has been recorded in the Company's consolidated financial statements because the loss contingency is not deemed probable, and the Company does not expect that any costs that are reasonably possible to be incurred by the Company in connection with Brazilian tax disputes would have a material adverse effect on the Company's financial condition, results of operations or cash flows.

Customer Disputes

The Company, through its Harsco Metals & Minerals Segment, provides services to ArcelorMittal and/or various of its subsidiaries and affiliates (collectively, "ArcelorMittal") through long-term service contracts on a number of sites worldwide. Currently, ArcelorMittal and the Company are involved in several commercial disputes, some of which may result in legal or other action. Both the Company and ArcelorMittal are working to resolve these matters. Furthermore, the Company, through its Harsco Metals & Minerals Segment, may become involved in commercial disputes with other customers. Although results of operations and cash flows for a given period could be adversely affected by a negative outcome in these or other lawsuits, claims and proceedings, management believes that the

ultimate outcome of these matters will not have a material adverse effect on the Company's financial condition, results of operations or cash flows.

Other

In the United States, the Company has been named as one of many defendants (approximately 90 or more in most cases) in legal actions alleging personal injury from exposure to airborne asbestos over the past several decades. In their suits, the plaintiffs have named as defendants, among others, many manufacturers, distributors and installers of numerous types of equipment or products that allegedly contained asbestos.

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The Company believes that the claims against it are without merit. The Company has never been a producer, manufacturer or processor of asbestos fibers. Any component within a Company product that may have contained asbestos would have been purchased from a supplier. Based on scientific and medical evidence, the Company believes that any asbestos exposure arising from normal use of any Company product never presented any harmful levels of airborne asbestos exposure, and, moreover, the type of asbestos contained in any component that was used in those products was protectively encapsulated in other materials and is not associated with the types of injuries alleged in the pending suits. Finally, in most of the depositions taken of plaintiffs to date in the litigation against the Company, plaintiffs have failed to specifically identify any Company products as the source of their asbestos exposure.

The majority of the asbestos complaints pending against the Company have been filed in New York. Almost all of the New York complaints contain a standard claim for damages of $20 million or $25 million against the approximately 90 defendants, regardless of the individual plaintiff's alleged medical condition, and without specifically identifying any Company product as the source of plaintiff's asbestos exposure.

As of June 30, 2014, there are 17,458 pending asbestos personal injury claims filed against the Company. Of these cases, 17,108 are pending in the New York Supreme Court for New York County in New York State. The other claims, totaling 350, are filed in various counties in a number of state courts, and in certain Federal District Courts (including New York), and those complaints generally assert lesser amounts of damages than the New York State court cases or do not state any amount claimed.

As of June 30, 2014, the Company has obtained dismissal by stipulation, or summary judgment prior to trial, in 27,386 cases.

In view of the persistence of asbestos litigation nationwide, the Company expects to continue to receive additional claims. However, there have been developments during the past several years, both by certain state legislatures and by certain state courts, which could favorably affect the Company's ability to defend these asbestos claims in those jurisdictions. These developments include procedural changes, docketing changes, proof of damage requirements and other changes that require plaintiffs to follow specific procedures in bringing their claims and to show proof of damages before they can proceed with their claim. An example is the action taken by the New York Supreme Court (a trial court), which is responsible for managing all asbestos cases pending within New York County in the State of New York. This Court issued an order in December 2002 that created a Deferred or Inactive Docket for all pending and future asbestos claims filed by plaintiffs who cannot demonstrate that they have a malignant condition or discernible physical impairment, and an Active or In Extremis Docket for plaintiffs who are able to show such medical condition. As a result of this order, the majority of the asbestos cases filed against the Company in New York County have been moved to the Inactive Docket until such time as the plaintiffs can show that they have incurred a physical impairment. As of June 30, 2014, the Company has been listed as a defendant in 214 Active or In Extremis asbestos cases in New York County. The Court's Order has been challenged by some plaintiffs.

Except with regard to the legal costs in a few limited, exceptional cases, the Company's insurance carrier has paid all legal and settlement costs and expenses to date related to the Company's U.S. asbestos cases. The Company has liability insurance coverage under various primary and excess policies that the Company believes will be available, if necessary, to substantially cover any liability that might ultimately be incurred on these claims.

The Company intends to continue its practice of vigorously defending these claims and cases. It is not possible to predict the ultimate outcome of asbestos-related lawsuits, claims and proceedings due to the unpredictable nature of personal injury litigation, and no loss provision has been recorded in the Company's consolidated financial statements because a loss contingency is not deemed probable or estimable. Despite this uncertainty, and although results of operations and cash flows for a given period could be adversely affected by asbestos-related lawsuits, claims and proceedings, the Company does not expect that any costs that are reasonably possible to be incurred by the Company in connection with asbestos litigation would have a material adverse effect on the Company's financial condition, results of operations or cash flows.

The Company is subject to various other claims and legal proceedings covering a wide range of matters that arose in the ordinary course of business. In the opinion of management, all such matters are adequately covered by insurance or by established reserves, and, if not so covered, are without merit or are of such kind, or involve such amounts, as

would not have a material adverse effect on the financial position, results of operations or cash flows of the Company.

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Insurance liabilities are recorded when it is probable that a liability has been incurred for a particular event and the amount of loss associated with the event can be reasonably estimated. Insurance reserves have been estimated based primarily upon actuarial calculations and reflect the undiscounted estimated liabilities for ultimate losses, including claims incurred but not reported. Inherent in these estimates are assumptions that are based on the Company's history of claims and losses, a detailed analysis of existing claims with respect to potential value, and current legal and legislative trends. If actual claims differ from those projected by management, changes (either increases or decreases) to insurance reserves may be required and would be recorded through income in the period the change was determined. When a recognized liability is covered by third-party insurance, the Company records an insurance claim receivable to reflect the covered liability. Insurance claim receivables are included in Other receivables on the Company's Condensed Consolidated Balance Sheets. See Note 1, Summary of Significant Accounting Policies, to the Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2013 for additional information on Accrued Insurance and Loss Reserves.

11. Reconciliation of Basic and Diluted Shares

	Three Months Ended June 30		Six Months Ended June 30	
(In thousands, except per share amounts)	2014	2013	2014	2013
Income (loss) from continuing operations attributable to Harsco Corporation common stockholders	$(15,065)	$24,331	$(3,523)	$31,973
Weighted-average shares outstanding - basic	80,885	80,760	80,850	80,733
Dilutive effect of stock-based compensation	—	244	—	234
Weighted-average shares outstanding - diluted	$80,885	$81,004	$80,850	$80,967

Earnings (loss) from continuing operations per common share, attributable to Harsco Corporation common stockholders:

Basic	$(0.19)	$0.30	$(0.04)	$0.40
Diluted	$(0.19)	$0.30	$(0.04)	$0.39

The following average outstanding stock-based compensation units were not included in the three and six months ended computation of diluted earnings per share because the effect was antidilutive:

	Three Months Ended June 30		Six Months Ended June 30	
(In thousands)	2014	2013	2014	2013
Restricted stock units	311	—	311	—
Stock options	215	304	215	304
Stock appreciation rights	968	190	968	95
Performance share units	97	—	97	—

12. Derivative Instruments, Hedging Activities and Fair Value

Derivative Instruments and Hedging Activities

The Company uses derivative instruments, including foreign currency forward exchange contracts, cross-currency interest rate swaps and, at times, commodity contracts, to manage certain foreign currency, interest rate and commodity price exposures. Derivative instruments are viewed as risk management tools by the Company and are not

used for trading or speculative purposes.

All derivative instruments are recorded on the Condensed Consolidated Balance Sheets at fair value. Changes in the fair value of derivatives used to hedge foreign currency denominated balance sheet items are reported directly in earnings, along with offsetting transaction gains and losses on the items being hedged. Derivatives used to hedge forecasted cash flows associated with foreign currency commitments or forecasted commodity purchases may be accounted for as cash flow hedges, as deemed appropriate and if the criteria for hedge accounting are met. Gains and losses on derivatives designated as cash flow hedges are deferred as a separate component of equity and reclassified to earnings in a manner that matches the timing of the earnings impact of the hedged transactions. Generally, at June 30, 2014, these deferred gains and losses are reclassified to earnings over 10 to 15 years from the balance sheet date. The ineffective portion of all hedges, if any, is recognized currently in earnings.

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The fair values of outstanding derivative contracts recorded as assets and liabilities on the Condensed Consolidated Balance Sheets at June 30, 2014 and December 31, 2013 were as follows:

	Asset Derivatives		Liability Derivatives	
(In thousands)	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
June 30, 2014				
Derivatives designated as hedging instruments:				
Foreign currency forward exchange contracts	Other current assets	$41	Other current liabilities	$36
Cross-currency interest rate swaps	Other assets	24,473	Other liabilities	19,939
Total derivatives designated as hedging instruments		$24,514		$19,975
Derivatives not designated as hedging instruments:				
Foreign currency forward exchange contracts	Other current assets	$2,300	Other current liabilities	$1,460

	Asset Derivatives		Liability Derivatives	
(In thousands)	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
December 31, 2013				
Derivatives designated as hedging instruments:				
Foreign currency forward exchange contracts	Other current assets	$40	Other current liabilities	$17
Cross-currency interest rate swaps	Other assets	26,001	Other liabilities	13,410
Total derivatives designated as hedging instruments		$26,041		$13,427
Derivatives not designated as hedging instruments:				
Foreign currency forward exchange contracts	Other current assets	$1,216	Other current liabilities	$3,267

All of the Company's derivatives are recorded in the Condensed Consolidated Balance Sheets at gross amounts and not offset. All of the Company's cross-currency interest rate swaps and certain foreign currency forward exchange contracts are transacted under International Swaps and Derivatives Association ("ISDA") documentation. Each ISDA master agreement permits the net settlement of amounts owed in the event of default. The Company's derivative assets and liabilities subject to enforceable master netting arrangements resulted in a $0.1 million net liability at both June 30, 2014 and December 31, 2013.

The effect of derivative instruments on the Condensed Consolidated Statements of Operations and the Condensed Consolidated Statements of Comprehensive Income (Loss) for the three and six months ended June 30, 2014 and 2013 was as follows:

Derivatives Designated as Hedging Instruments

(In thousands)	Amount of Gain (Loss) Recognized in Other Comprehensive Income (“OCI”) on Derivative - Effective Portion	Location of Gain (Loss) Reclassified from Accumulated OCI into Income - Effective Portion	Amount of Gain (Loss) Reclassified from Accumulated OCI into Income - Effective Portion	Location of Gain (Loss) Recognized in Income on Derivative - Ineffective Portion and Amount Excluded from Effectiveness Testing	Amount of Gain (Loss) Recognized in Income on Derivative - Ineffective Portion and Amount Excluded from

				Effectiveness Testing	
Three Months Ended June 30, 2014:					
Foreign currency forward exchange contracts	$ 9	$—		$—	
Cross-currency interest rate swaps	1,805	—	Cost of services and products sold	(3,801	) (a)
	$ 1,814	$—		$ (3,801	)
Three Months Ended June 30, 2013:					
Cross-currency interest rate swaps	$ (2,731)	$—	Cost of services and products sold	$ (3,583	) (a)

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(In thousands)	Amount of Gain (Loss)Recognized in Other Comprehensive Income ("OCI") on Derivative - Effective Portion	Location of Gain (Loss) Reclassified from Accumulated OCI into Income - Effective Portion	Amount of Gain (Loss) Reclassified from Accumulated OCI into Income - Effective Portion	Location of Gain (Loss) Recognized in Income on Derivative - Ineffective Portion and Amount Excluded from Effectiveness Testing	Amount of Gain (Loss) Recognized in Income on Derivative - Ineffective Portion and Amount Excluded from Effectiveness Testing
Six Months Ended June 30, 2014:					
Foreign currency forward exchange contracts	$ 20	Cost of services and products sold	$ (2)		$ —
Cross currency interest rate swaps	(2,555)		—	Cost of services and products sold	(5,375) (a)
	$ (2,535)		$ (2)		$ (5,375)
Six Months Ended June 30, 2013:					
Cross currency interest rate swaps	$ (233)		$ —	Cost of services and products sold	$ 16,870 (a)

(a) These gains (losses) offset foreign currency fluctuation effects on the debt principal.

Derivatives Not Designated as Hedging Instruments

(In thousands)	Location of Gain (Loss) Recognized in Income on Derivative	Amount of Gain (Loss) Recognized in Income on Derivative for the Three Months Ended June 30 (a)	
		2014	2013
Foreign currency forward exchange contracts	Cost of services and products sold	$ (1,135)	$ (4,108)

(In thousands)	Location of Gain (Loss) Recognized in Income on Derivative	Amount of Gain (Loss) Recognized in Income on Derivative for the Six Months Ended June 30 (a)	
		2014	2013
Foreign currency forward exchange contracts	Cost of services and products sold	$ 421	$ (2,049)

(a) These gains (losses) offset amounts recognized in cost of services and products sold principally as a result of intercompany or third party foreign currency exposures.

Foreign Currency Forward Exchange Contracts

The Company conducts business in multiple currencies and, accordingly, is subject to the inherent risks associated with foreign exchange rate movements. The financial position and results of operations of substantially all of the Company's foreign subsidiaries are measured using the local currency as the functional currency. Foreign currency-denominated assets and liabilities are translated into U.S. dollars at the exchange rates existing at the respective balance sheet dates. Income and expense items are translated at the average exchange rates during the respective periods. The aggregate effects of translating the balance sheets of these subsidiaries are deferred and

recorded in Accumulated other comprehensive loss, which is a separate component of equity.

The Company uses derivative instruments to hedge cash flows related to foreign currency fluctuations. Foreign currency forward exchange contracts outstanding are part of a worldwide program to minimize foreign currency exchange operating income and balance sheet exposure by offsetting foreign currency exposures of certain future payments between the Company and its various subsidiaries, suppliers or customers. These unsecured contracts are with major financial institutions. The Company may be exposed to credit loss in the event of non-performance by the contract counterparties. The Company evaluates the creditworthiness of the counterparties and does not expect default by them. Foreign currency forward exchange contracts are used to hedge commitments, such as foreign currency debt, firm purchase commitments and foreign currency cash flows for certain export sales transactions.

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The following tables summarize, by major currency, the contractual amounts of the Company's foreign currency forward exchange contracts in U.S. dollars at June 30, 2014 and December 31, 2013. The "Buy" amounts represent the U.S. dollar equivalent of commitments to purchase foreign currencies, and the "Sell" amounts represent the U.S. dollar equivalent of commitments to sell foreign currencies. The recognized gains and losses offset amounts recognized in cost of services and products sold principally as a result of intercompany or third party foreign currency exposures.
Contracted Amounts of Foreign Currency Forward Exchange Contracts Outstanding at June 30, 2014:

(In thousands)	Type	U.S. Dollar Equivalent	Maturity	Recognized Gain (Loss)	
British pounds sterling	Sell	$24,902	July 2014	$(57	)
British pounds sterling	Buy	7,165	July 2014	15	
Euros	Sell	263,296	July 2014	818	
Euros	Buy	259,010	July 2014 through September 2014	12	
Other currencies	Sell	35,751	July 2014 through December 2015	(16	)
Other currencies	Buy	10,133	July 2014 through August 2014	73	
Total		$600,257		$845	

Included in the contracted amounts of foreign currency exchange forward contracts outstanding at June 30, 2014 are $132.2 million of foreign currency exchange forward contracts entered into by the Company under the Transition Services Agreement with Brand. The Company has recognized a $0.6 million mark-to-market asset associated with these foreign currency exchange forward contracts.

Contracted Amounts of Foreign Currency Forward Exchange Contracts Outstanding at December 31, 2013:

(In thousands)	Type	U.S. Dollar Equivalent	Maturity	Recognized Gain (Loss)	
British pounds sterling	Sell	$26,931	January 2014	$(277	)
British pounds sterling	Buy	1,976	January 2014	15	
Euros	Sell	248,943	January 2014 through July 2014	(335	)
Euros	Buy	242,385	January 2014 through March 2014	(1,335	)
Other currencies	Sell	12,708	January 2014 through July 2014	(134	)
Other currencies	Buy	8,907	January 2014 through August 2014	38	
Total		$541,850		$(2,028	)

Included in the contracted amounts of foreign currency exchange forward contracts outstanding at December 31, 2013 are $121.2 million of foreign currency exchange forward contracts entered into by the Company under the Transition Services Agreement with Brand. The Company has recognized a $0.7 million mark-to-market liability associated with these foreign currency exchange forward contracts.
In addition to foreign currency forward exchange contracts, the Company designates certain loans as hedges of net investments in international subsidiaries. The Company recorded pre-tax net gains of $4.6 million and $4.9 million during the three and six months ended June 30, 2014, respectively, and pre-tax net losses of $4.9 million and $3.2 million during the three and six months ended June 30, 2013, respectively, into Accumulated other comprehensive loss.
Cross-Currency Interest Rate Swaps
The Company uses cross-currency interest rate swaps in conjunction with certain debt issuances in order to secure a fixed local currency interest rate. Under these cross-currency interest rate swaps, the Company receives interest based on a fixed or floating U.S. dollar rate and pays interest on a fixed local currency rate based on the contractual amounts in dollars and the local currency, respectively. The cross-currency interest rate swaps are recorded on the Condensed Consolidated Balance Sheets at fair value, with changes in value attributed to the effect of the swaps' interest spread recorded in Accumulated other comprehensive loss. Changes in value attributed to the effect of foreign currency fluctuations are recorded in the statements of operations and offset currency fluctuation effects on the debt principal.

The following table indicates the contractual amounts of the Company's cross-currency interest rate swaps at June 30, 2014:

		Interest Rates	
(In millions)	Contractual Amount	Receive	Pay
Maturing 2018	$ 250.0	Fixed U.S. dollar rate	Fixed euro rate
Maturing 2020	220.0	Fixed U.S. dollar rate	Fixed British pound sterling rate
Maturing 2016 through 2017	9.8	Floating U.S. dollar rate	Fixed rupee rate

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Fair Value of Derivative Assets and Liabilities and Other Financial Instruments

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (an exit price). The Company utilizes market data or assumptions that the Company believes market participants would use in valuing the asset or liability, including assumptions about risk and the risks inherent in the inputs to the valuation technique.

The fair value hierarchy distinguishes between (1) market participant assumptions developed based on market data obtained from independent sources (observable inputs), and (2) an entity's own assumptions about market participant assumptions based on the best information available in the circumstances (unobservable inputs). The fair value hierarchy consists of three broad levels, which give the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy are described below:

- Level 1—Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

- Level 2—Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, including quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; inputs other than quoted prices that are observable for the asset or liability (e.g., interest rates); and inputs that are derived principally from or corroborated by observable market data by correlation or other means.

- Level 3—Inputs that are both significant to the fair value measurement and unobservable.

In instances in which multiple levels of inputs are used to measure fair value, hierarchy classification is based on the lowest level input that is significant to the fair value measurement in its entirety. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the asset or liability.

The following table indicates the fair value hierarchy of the financial instruments of the Company at June 30, 2014 and December 31, 2013:

Level 2 Fair Value Measurements (In thousands)	June 30 2014	December 31 2013
Assets		
Foreign currency forward exchange contracts	$2,341	$1,256
Cross-currency interest rate swaps	24,473	26,001
Liabilities		
Foreign currency forward exchange contracts	1,496	3,284
Cross-currency interest rate swaps	19,939	13,410

The following table reconciles the beginning and ending balances for liabilities measured on a recurring basis using unobservable inputs (Level 3) for the six months ended June 30, 2014:

Level 3 Liabilities—Unit Adjustment Liability (a) for the Six Months Ended June 30 (b) (In thousands)	Consolidated Totals
Balance at December 31, 2013	$106,343
Payments	(11,160)
Change in fair value to the unit adjustment liability	5,019
Balance at June 30, 2014	$100,201

(a) See Note 5, Equity Method Investments, for additional information related to the unit adjustment liability.

(b) Does not total due to rounding.

The Company primarily applies the market approach for recurring fair value measurements and endeavors to utilize the best available information. Accordingly, the Company utilizes valuation techniques that maximize the use of observable inputs, such as forward rates, interest rates, the Company's credit risk and counterparties' credit risks, and which minimize the use of unobservable inputs. The Company is able to classify fair value balances based on the

ability to observe those inputs. Commodity derivatives, foreign currency forward exchange contracts and cross-currency interest rate swaps are classified as Level 2 fair value based upon pricing models using market-based inputs. Model inputs can be verified, and valuation techniques do not involve significant management judgment.

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The carrying amounts of cash and cash equivalents, accounts receivable, accounts payable, accrued liabilities and short-term borrowings approximate fair value due to the short-term maturities of these assets and liabilities. At June 30, 2014 and December 31, 2013, the total fair value of long-term debt, including current maturities, was $898.2 million and $832.6 million, respectively, compared with a carrying value of $855.8 million and $803.4 million, respectively, at June 30, 2014 and December 31, 2013, respectively. Fair values for debt are based on quoted market prices (Level 1) for the same or similar issues, or on the current rates offered to the Company for debt of the same remaining maturities.

13. Review of Operations by Segment

The Company has reclassified segment operating results for the three and six months ended June 30, 2013 to conform to the revised manner in which the Company now allocates corporate expenses to operating segments as a result of changes in organizational structure resulting from the Infrastructure Transaction. The changes do not impact the Company's previously reported consolidated revenues from continuing operations, operating income from continuing operations or income from continuing operations before income taxes and equity income (loss).

	Three Months Ended June 30		Six Months Ended June 30	
(In thousands)	2014	2013	2014	2013
Revenues From Continuing Operations				
Harsco Metals & Minerals	$360,994	$336,146	$714,032	$673,470
Harsco Infrastructure	—	251,172	—	467,231
Harsco Industrial	103,005	93,772	205,105	184,218
Harsco Rail	70,578	78,646	128,139	150,212
Total revenues from continuing operations	$534,577	$759,736	$1,047,276	$1,475,131
Operating Income (Loss) From Continuing Operations				
Harsco Metals & Minerals	$(9,238)	$27,053	$13,980	$50,282
Harsco Infrastructure	—	2,288	—	(4,764)
Harsco Industrial	17,429	15,553	34,000	31,162
Harsco Rail	13,526	15,932	19,025	19,110
Corporate (a)	(15,481)	(9,979)	(28,430)	(19,158)
Total operating income from continuing operations	$6,236	$50,847	$38,575	$76,632

(a) For the three months ended June 30, 2014, Corporate includes a $3.4 million loss on disposal of the Harsco Infrastructure Segment and transaction costs and $1.5 million of net periodic pension cost for defined benefit pension plans retained by the Company as part of the Infrastructure Transaction. For the six months ended June 30, 2014, Corporate includes a $5.6 million loss on disposal of the Harsco Infrastructure Segment and transaction costs and $2.9 million of net periodic pension cost for defined benefit pension plans retained by the Company as part of the Infrastructure Transaction.

Reconciliation of Segment Operating Income to Income (Loss) From Continuing Operations Before Income Taxes and Equity Income (Loss)

	Three Months Ended June 30		Six Months Ended June 30	
(In thousands)	2014	2013	2014	2013
Segment operating income	$21,717	$60,826	$67,005	$95,790
General Corporate expense	(15,481)	(9,979)	(28,430)	(19,158)
Operating income from continuing operations	6,236	50,847	38,575	76,632
Interest income	410	830	707	1,236
Interest expense	(11,958)	(12,855)	(23,379)	(24,598)

Change in fair value to unit adjustment liability	(2,473)	—	(5,019)	—
Income (loss) from continuing operations before income taxes and equity income (loss)	$(7,785)	$38,822	$10,884	$53,270

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14. Other Expenses

This Condensed Consolidated Statements of Operations caption includes restructuring program costs, net gains on the disposal of non-core assets, impaired asset write-downs, employee termination benefit costs and costs to exit activities.

	Three Months Ended June 30		Six Months Ended June 30	
(In thousands)	2014	2013	2014	2013
Restructuring programs (see Note 16)	$8,539	$—	$8,539	$—
Net gains	(650)	(877)	(3,008)	(4,569)
Impaired asset write-downs	13,982	—	14,080	689
Other (a)	5,645	4,805	7,249	6,266
Other expenses	$27,516	$3,928	$26,860	$2,386

(a) Other includes employee termination benefit costs and costs to exit activities that are not directly related to the restructuring programs detailed in Note 16, Restructuring Programs.

Impaired asset write-downs are measured as the amount by which the carrying amount of assets exceeds their fair value. Fair value is estimated based upon the expected future realizable cash flows including anticipated selling prices. Non-cash impaired asset write-downs are included in the caption Other, net on the Condensed Consolidated Statements of Cash Flows as adjustments to reconcile Net income (loss) to Net cash provided by operating activities. During the second quarter of 2014, impaired asset write-downs represent non-cash long-lived asset impairment charges to reduce the carrying value of assets at certain sites in the Harsco Metals & Minerals Segment based on the Company's strategic decisions or contract terminations at these sites.

15. Components of Accumulated Other Comprehensive Loss

Accumulated other comprehensive loss is included on the Condensed Consolidated Statements of Stockholders' Equity. The components of Accumulated other comprehensive loss, net of the effect of income taxes, and activity for the six months ended June 30, 2013 and 2014 was as follows:

	Components of Accumulated Other Comprehensive Income (Loss) - Net of Tax				
(In thousands)	Cumulative Foreign Exchange Translation Adjustments	Effective Portion of Derivatives Designated as Hedging Instruments	Cumulative Unrecognized Actuarial Losses on Pension Obligations	Unrealized Loss on Marketable Securities	Total
Balance at December 31, 2012	$62,308	$(8,139)	$ (465,286)	$(51)	$(411,168)
Other comprehensive income (loss) before reclassifications	(46,555) (a)	536 (b)	21,255 (a)	8	(24,756)
Amounts reclassified from accumulated other comprehensive loss	—	—	9,968	—	9,968
Total other comprehensive income (loss)	(46,555)	536	31,223	8	(14,788)
Less: Other comprehensive loss attributable to noncontrolling interests	810	—	—	—	810
	(45,745)	536	31,223	8	(13,978)

Other comprehensive income (loss) attributable to Harsco Corporation					
Balance at June 30, 2013	$16,563	$(7,603)	$ (434,063)	$(43)	$(425,146)

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(In thousands)	Components of Accumulated Other Comprehensive Income (Loss) - Net of Tax				
	Cumulative Foreign Exchange Translation Adjustments	Effective Portion of Derivatives Designated as Hedging Instruments	Cumulative Unrecognized Actuarial Losses on Pension Obligations	Unrealized Loss on Marketable Securities	Total
Balance at December 31, 2013	$6,110	$(7,023)	$ (369,682)	$(20)	$(370,615)
Other comprehensive income (loss) before reclassifications	7,634 (a)	(1,868) (b)	(8,187) (a)	4	(2,417)
Amounts reclassified from accumulated other comprehensive loss	—	1	8,231	—	8,232
Other comprehensive loss from equity method investee	(4,440)	—	632	—	(3,808)
Amounts reclassified from accumulated other comprehensive loss in connection with the Infrastructure Transaction	(1,447)	—	—	—	(1,447)
Total other comprehensive income (loss)	1,747	(1,867)	676	4	560
Less: Other comprehensive (income) loss attributable to noncontrolling interests	425	(11)	—	—	414
Other comprehensive income (loss) attributable to Harsco Corporation	2,172	(1,878)	676	4	974
Balance at June 30, 2014	$8,282	$(8,901)	$ (369,006)	$(16)	$(369,641)

(a) Principally foreign currency fluctuation.
(b) Net change from periodic revaluations.

Amounts reclassified from accumulated other comprehensive loss are as follows:

(In thousands)	Three Months Ended June 30 2014	Six Months Ended June 30 2014	Three Months Ended June 30 2013	Six Months Ended June 30 2013	Affected Caption in the Condensed Consolidated Statements of Operations
Amortization of defined benefit pension items (c):					
Actuarial losses (d)	$2,837	$5,676	$3,154	$6,301	Selling, general and administrative expenses
Actuarial losses (d)	1,584	3,136	2,259	4,525	Cost of services and products sold
Prior-service costs (d)	23	46	66	130	Selling, general and administrative expenses
Prior-service costs (d)	46	91	63	126	Cost of services and products sold
Total before tax	4,490	8,949	5,542	11,082	
Tax benefit	(359)	(718)	(556)	(1,114)	
Total reclassification of defined benefit pension	$4,131	$8,231	$4,986	$9,968	

items, net of tax

Amortization of cash flow hedging instruments (c):					
Foreign currency forward exchange contracts	$—	$2	$(6)	$—	Cost of services and products sold
Tax benefit	—	(1)	—	—	
Total reclassification of cash flow hedging instruments	$—	$1	$(6)	$—	

(c) Amounts in parentheses indicate credits to profit/loss.

(d) These accumulated other comprehensive loss components are included in the computation of net periodic pension costs. See Note 8, Employee Benefit Plans, for additional details.

16. Restructuring Programs

In recent years, the Company has instituted restructuring programs to balance short-term profitability goals with long-term strategies. A primary objective of these programs has been to establish platforms upon which the affected businesses can grow with reduced fixed investment and generate annual operating expense savings. The restructuring programs have been instituted in response to the continuing impact of global financial and economic uncertainty on the Company's end markets. Restructuring costs incurred in these programs were recorded in the Other expenses caption of the Condensed Consolidated Statements of Operations. The timing of associated cash payments is dependent on the type of restructuring cost and can extend over a multi-year period.

Harsco Metals & Minerals Improvement Plan ("Project Orion")

Under Project Orion, the Harsco Metals & Minerals Segment made organizational changes which are expected to improve return on capital and deliver a higher and more consistent level of service to customers by improving several core processes and simplifying the organizational structure. The Company incurred an $8.5 million charge related to Project Orion during the three months ended June 30, 2014. Phase one of Project Orion began in the second quarter of 2014 and will continue through the remainder of 2014. Phase two of Project Orion will begin in late 2014 or early 2015 and will result in an additional charge. The amount of the additional charge cannot be determined at this time.

The restructuring accrual for Project Orion at June 30, 2014 and the activity for the six months then ended were as follows:

(In thousands)	Expense Incurred in 2014	Other Adjustments	Cash Expenditures	Foreign Currency Translation	Remaining Accrual June 30 2014
Harsco Metals & Minerals Segment					
Employee termination benefit costs	$8,539	$1,237	$(1,437)	$2	$8,341
Total	$8,539	$1,237	$(1,437)	$2	$8,341

Prior Restructuring Programs

The remaining accrual for restructuring programs was $2.9 million and $5.1 million at June 30, 2014 and December 31, 2013, respectively. The remaining accrual relates primarily to exit activity costs for lease terminations expected to be paid over the remaining life of the leases.

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ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with the accompanying unaudited condensed consolidated financial statements as well as the audited consolidated financial statements of Harsco Corporation (the "Company"), including the notes thereto, included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2013, which includes additional information about the Company’s critical accounting policies, contractual obligations, practices and the transactions that support the financial results, and provides a more comprehensive summary of the Company’s outlook, trends and strategies for 2014 and beyond.

Certain amounts included in Item 2 of this Quarterly Report on Form 10-Q are rounded in millions and all percentages are calculated based on actual amounts. As a result, minor differences may exist due to rounding.

Forward-Looking Statements

The nature of the Company's business and the many countries in which it operates subject it to changing economic, competitive, regulatory and technological conditions, risks and uncertainties. In accordance with the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995, the Company provides the following cautionary remarks regarding important factors that, among others, could cause future results to differ materially from the results contemplated by forward-looking statements, including the expectations and assumptions expressed or implied herein. Forward-looking statements contained herein could include, among other things, statements about management's confidence in and strategies for performance; expectations for new and existing products, technologies and opportunities; and expectations regarding growth, sales, cash flows, and earnings. Forward-looking statements can be identified by the use of such terms as "may," "could," "expect," "anticipate," "intend," "believe," "likely," "estimate," "plan" or other comparable terms.

Factors that could cause actual results to differ, perhaps materially, from those implied by forward-looking statements include, but are not limited to: (1) changes in the worldwide business environment in which the Company operates, including general economic conditions; (2) changes in currency exchange rates, interest rates, commodity and fuel costs and capital costs; (3) changes in the performance of equity and bond markets that could affect, among other things, the valuation of the assets in the Company's pension plans and the accounting for pension assets, liabilities and expenses; (4) changes in governmental laws and regulations, including environmental, occupational health and safety, tax and import tariff standards; (5) market and competitive changes, including pricing pressures, market demand and acceptance for new products, services and technologies; (6) unforeseen business disruptions in one or more of the many countries in which the Company operates due to political instability, civil disobedience, armed hostilities, public health issues or other calamities; (7) the seasonal nature of the Company's business; (8) the Company's ability to successfully enter into new contracts and complete new acquisitions or strategic ventures in the time-frame contemplated, or at all; (9) the integration of the Company's strategic acquisitions; (10) the amount and timing of repurchases of the Company's common stock, if any; (11) the prolonged recovery in global financial and credit markets and economic conditions generally, which could result in the Company's customers curtailing development projects, construction, production and capital expenditures, which, in turn, could reduce the demand for the Company's products and services and, accordingly, the Company's revenues, margins and profitability; (12) the outcome of any disputes with customers, contractors and subcontractors; (13) the financial condition of the Company's customers, including the ability of customers (especially those that may be highly leveraged and those with inadequate liquidity) to maintain their credit availability; (14) the Company's ability to successfully implement and receive the expected benefits of cost-reduction and restructuring initiatives, including the achievement of expected cost savings in the expected time frame; (15) the ability to successfully implement the Company's strategic initiatives and portfolio optimization and the impact of such initiatives, such as the Harsco Metals & Minerals Segment's Improvement Plan; (16) the ability of the strategic venture between the Company and Clayton, Dubilier & Rice ("CD&R") to effectively integrate the Company's Infrastructure business and the Brand Energy & Infrastructure Services business and realize the synergies contemplated by the transaction; (17) the Company's ability to realize cost savings from the divestiture of the Infrastructure business, as well as the transaction being accretive to earnings and improving operating margins and return on capital; (18) the amount ultimately realized from the Company's exit from the strategic venture between the Company and CD&R and the timing of such exit; (19) risk and uncertainty associated with intangible assets; and

(20) other risk factors listed from time to time in the Company's SEC reports. A further discussion of these, along with other potential risk factors, can be found in Part I, Item 1A, "Risk Factors," of the Company's Annual Report on Form 10-K for the year ended December 31, 2013. The Company cautions that these factors may not be exhaustive and that many of these factors are beyond the Company's ability to control or predict. Accordingly, forward-looking statements should not be relied upon as a prediction of actual results. The Company undertakes no duty to update forward-looking statements except as may be required by law.

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Executive Overview

In November 2013, the Company consummated the previously announced transaction to sell the Company's Harsco Infrastructure Segment into a strategic venture with CD&R as part of a transaction that combines the Harsco Infrastructure Segment with Brand Energy & Infrastructure Services, Inc., which CD&R simultaneously acquired (the "Infrastructure Transaction"). The Company has contributed substantially all of the Company's equity interest in, and the net assets of, the Harsco Infrastructure Segment to the strategic venture in exchange for $300 million, subject to working capital and other adjustments, and an approximate 29% equity interest in the resulting entity (the "Infrastructure strategic venture" or "Brand"). The Company recorded an additional loss on disposal of $3.2 million and $3.9 million during the second quarter and first six months of 2014, respectively. The Company does not anticipate any further adjustments to the loss on disposal of the Harsco Infrastructure Segment.

In May 2014, the Company began executing the first phase of the Harsco Metals & Minerals Segment's Improvement Plan ("Project Orion") after conducting an analysis of the business to identify opportunities to improve its core processes and to simplify its organizational structure. The goals of Project Orion are improving financial returns and providing higher and more consistent levels of value added services to customers by improving the bid and contract management process, improving underperforming contracts, and simplifying operational structures. The Company incurred an $8.5 million charge related to Project Orion during the second quarter of 2014. Through actions initiated through June 30, 2014, the Company anticipates compensation savings of approximately $6 million for the full year December 31, 2014, or approximately $15 million when annualized. Annual recurring benefits under phase one of Project Orion are expected to be approximately $25 million by the end of 2015, which include other operational savings. Please see Note 16, Restructuring Programs, in Part I, Item 1, Financial Statements for additional information.

In connection with Project Orion's focus on underperforming contracts, during the second quarter of 2014, the Company recorded pre-tax charges of $10.9 million primarily for site exit costs and non-cash long-lived asset impairment charges to reduce the carrying value of assets at certain sites to fair value based upon the expected future realizable cash flows, including anticipated selling prices, based on the Company's strategic decisions made during the quarter. The possibility exists that the Company may take similar strategic actions with respect to other underperforming assets at certain sites that may result in additional exit costs and non-cash asset impairment charges.

As the Company has previously disclosed, one of the Company's large steel mill customers in Europe has filed for protection under Italian receivership procedure (the "Marzano Law"). During the fourth quarter of 2013, the Company recorded a bad debt reserve of $2.6 million on receivables with this customer. During the second quarter of 2014, the customer terminated its contract with the Company under provisions of the Marzano Law. As a result, during the second quarter of 2014, the Company recorded an additional bad debt reserve of $3.9 million on the remaining pre-receivership receivables with this customer. The Company also recorded an additional charge of $7.7 million during the second quarter of 2014 primarily for non-cash long-lived asset impairments to reduce the carrying value of assets used at the customer's site to fair value based upon the expected future realizable cash flows, including anticipated selling prices.

Revenues by Segment	Three Months Ended June 30						
(In millions)	2014	2013	Change		%	
Harsco Metals & Minerals	$361.0	$336.1	$24.8		7.4	%
Harsco Infrastructure (a)	—	251.2	(251.2	)	(100.0	)
Harsco Industrial	103.0	93.8	9.2		9.8	
Harsco Rail	70.6	78.6	(8.1	)	(10.3	)
Total revenues	$534.6	$759.7	$(225.2	)	(29.6	)%

Six Months Ended

Revenues by Segment	June 30			
(In millions)	2014	2013	Change	%
Harsco Metals & Minerals	$714.0	$673.5	$40.6	6.0 %
Harsco Infrastructure (a)	—	467.2	(467.2)	(100.0)
Harsco Industrial	205.1	184.2	20.9	11.3
Harsco Rail	128.1	150.2	(22.1)	(14.7)
Total revenues	$1,047.3	$1,475.1	$(427.9)	(29.0)%

(a) In November 2013, the Company consummated the Infrastructure Transaction, and accordingly, there is no revenue for the Harsco Infrastructure Segment for 2014. The results of the Harsco Infrastructure Segment from January 1, 2013 through the date of closing are reported in the Company's results of operations for 2013.

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Revenues by Region (In millions)	Three Months Ended June 30 2014	2013	Change	%
Western Europe	$155.0	$274.6	$(119.6)	(43.6)%
North America	241.1	292.1	(51.0)	(17.5)
Latin America (b)	61.0	81.7	(20.8)	(25.4)
Asia-Pacific	39.3	47.8	(8.5)	(17.8)
Middle East and Africa	19.4	43.3	(23.9)	(55.2)
Eastern Europe	18.8	20.2	(1.4)	(6.8)
Total revenues	$534.6	$759.7	$(225.2)	(29.6)%

Revenues by Region (In millions)	Six Months Ended June 30 2014	2013	Change	%
Western Europe	$314.4	$537.2	$(222.8)	(41.5)%
North America	462.0	561.6	(99.7)	(17.7)
Latin America (b)	123.9	161.4	(37.5)	(23.2)
Asia-Pacific	73.7	91.3	(17.6)	(19.3)
Middle East and Africa	38.4	84.7	(46.3)	(54.7)
Eastern Europe	34.8	38.9	(4.0)	(10.4)
Total revenues	$1,047.3	$1,475.1	$(427.9)	(29.0)%

(b) Includes Mexico.

Revenues for the Company during the second quarter and first six months of 2014 were $534.6 million and $1.0 billion, respectively, compared with $759.7 million and $1.5 billion, respectively, in the second quarter and first six months of 2013. The change is primarily related to the Harsco Infrastructure Segment that was disposed of as part of the Infrastructure Transaction in the fourth quarter of 2013. Foreign currency translation increased revenues by $5.1 million and $1.2 million, respectively, for the second quarter and first six months of 2014 in comparison with the second quarter and first six months of 2013.

Operating Income (Loss) by Segment (c) (In millions)	Three Months Ended June 30 2014	2013	Change	%
Harsco Metals & Minerals	$(9.2)	$27.1	$(36.3)	(134.1)%
Harsco Infrastructure (d)	—	2.3	(2.3)	(100.0)
Harsco Industrial	17.4	15.6	1.9	12.1
Harsco Rail	13.5	15.9	(2.4)	(15.1)
Corporate (e)	(15.5)	(10.0)	(5.5)	(55.1)
Total operating income	$6.2	$50.8	$(44.6)	(87.7)%

Operating Income (Loss) by Segment (c) (In millions)	Six Months Ended June 30 2014	2013	Change	%
Harsco Metals & Minerals	$14.0	$50.3	$(36.3)	(72.2)%
Harsco Infrastructure (d)	—	(4.8)	4.8	100.0
Harsco Industrial	34.0	31.2	2.8	9.1
Harsco Rail	19.0	19.1	(0.1)	(0.4)
Corporate (e)	(28.4)	(19.2)	(9.3)	(48.4)
Total operating income	$38.6	$76.6	$(38.1)	(49.7)%

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Operating Margin by Segment (c)	Three Months Ended June 30 2014	2013	Six Months Ended June 30 2014	2013
Harsco Metals & Minerals	(2.6)%	8.0 %	2.0 %	7.5 %
Harsco Infrastructure (d)	—	0.9	—	(1.0)
Harsco Industrial	16.9	16.6	16.6	16.9
Harsco Rail	19.2	20.3	14.8	12.7
Consolidated operating margin	1.2 %	6.7 %	3.7 %	5.2 %

(c) The Company has reclassified segment operating results for the three and six months ended June 30, 2013 to conform to the revised manner in which the Company now allocates corporate expenses to operating segments as a result of changes in organizational structure resulting from the Infrastructure Transaction, which occurred in the fourth quarter of 2013. The changes do not impact the Company's previously reported consolidated revenues from continuing operations, operating income from continuing operations or income from continuing operations before income taxes and equity loss.
(d) In November 2013, the Company consummated the Infrastructure Transaction, and accordingly, there is no operating income (loss) for the Harsco Infrastructure Segment for 2014. The results of the Harsco Infrastructure Segment from January 1, 2013 through the date of closing are reported in the Company's results of operations for 2013.
(e) For the three and six months ended June 30, 2014, Corporate includes a $3.4 million and $5.6 million loss, respectively, on disposal of the Harsco Infrastructure Segment and transaction costs. Additionally, for the three and six months ended June 30, 2014, Corporate includes net periodic pension cost for defined benefit pension plans retained by the Company as part of the Infrastructure Transaction of $1.5 million and $2.9 million, respectively .

Operating income from continuing operations for the second quarter and the first six months of 2014 was $6.2 million and $38.6 million, respectively, compared with operating income from continuing operations of $50.8 million and $76.6 million, respectively, in the second quarter and first six months of 2013. The change is primarily related to the restructuring charge for Project Orion, the additional bad debt reserve and non-cash long-lived asset impairment charge for the Company's European steel mill customer in receivership, and costs for site exits and non-cash long-lived asset impairment charges for the Harsco Metals & Minerals Segment.

This change in operating income from continuing operations, the non-cash change in fair value to the unit adjustment liability related to the Infrastructure Transaction, and the Company's equity in income (loss) of unconsolidated entities were the primary drivers of the diluted loss per share from continuing operations for the second quarter and first six months of 2014 of $(0.19) and $(0.04), respectively, compared with diluted earnings per share from continuing operations of $0.30 and $0.40, respectively, for the second quarter and first six months of 2013.

The Company continues to have sufficient available liquidity. The Company currently expects operational and business needs to be met by cash from operations supplemented with borrowings from time to time due to historical patterns of seasonal cash flow and for the funding of various projects. See Liquidity and Capital Resources below for further discussion on liquidity, capital resources, and cash flows.

Harsco Metals & Minerals Segment:

Significant Effects on Revenues	Three Months Ended	Six Months Ended
(In millions)	June 30, 2014	June 30, 2014
Revenues — 2013	$336.1	$673.5
Net effects of price/volume changes, primarily attributable to volume changes.	23.4	47.3
Impact of foreign currency translation.	4.6	0.7

Net impact of new contracts and lost contracts (including exited underperforming contracts).	(3.1)	(7.5)
Revenues — 2014	$361.0	$714.0

Factors Positively Affecting Operating Income:

- Increased global steel production in the metals services business. Overall, steel production by customers under services contracts increased 6% in both the second quarter and first six months of 2014 compared with the same periods in 2013.
- Increased nickel prices of 28% and 5% in the second quarter and first six months of 2014, respectively, compared with the same periods in 2013.
- Net impact of new contracts and lost contracts, including exited underperforming contracts.

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Factors Negatively Impacting Operating Income:

- Project Orion restructuring charge of $8.5 million, attributable to severance costs, recorded during the second quarter of 2014.
- Charges of $10.9 million recorded during the second quarter of 2014, primarily attributable to site exit costs and non-cash long-lived asset impairment charges, associated with strategic actions from Project Orion's focus on underperforming contracts.
- Increased bad debt reserve of $3.9 million and a charge of $7.6 million, primarily for non-cash long-lived asset impairment, as a result of contract termination, during the second quarter of 2014 for the Company's large steel mill customer in Europe in receivership.
- Increased bad debt reserve of $3.6 million, net of value added tax, for one of the Company's steel mill customers in Europe as a result of missed progress payments.
- Foreign currency translation in the first six months of 2014 decreased operating income for this Segment by $1.6 million compared with the same period in the prior year. Foreign currency translation did not significantly impact operating income for the second quarter of 2014 compared with the same period in the prior year.

Harsco Industrial Segment:

Significant Effects on Revenues	Three Months Ended	Six Months Ended
(In millions)	June 30, 2014	June 30, 2014
Revenues — 2013	$93.8	$184.2
Effect of Hammco acquisition.	7.2	18.1
Net effects of price/volume changes, primarily attributable to volume changes.	2.4	4.1
Impact of foreign currency translation.	(0.4)	(1.3)
Revenues — 2014	$103.0	$205.1

Factors Positively Affecting Operating Income:

- Incremental effect of the acquisition of Hammco Corporation ("Hammco"), a U.S. manufacturer of high specification air-cooled heat exchangers for the natural gas and petrochemical processing markets, on January 2, 2014.
- Higher gain from sale of assets of $1.4 million in the first six months of 2014 compared with the first six months of 2013.
- Improved demand in North America for industrial boilers and air cooled heat exchangers.

Factors Negatively Impacting Operating Income:

- Decreased demand in Asia-Pacific for air cooled heat exchangers.

Harsco Rail Segment:

Significant Impacts on Revenues	Three Months Ended	Six Months Ended
(In millions)	June 30, 2014	June 30, 2014
Revenues — 2013	$78.6	$150.2
Net impacts of price/volume changes, primarily attributable to volume changes.	(8.9)	(23.9)
Impact of foreign currency translation.	0.9	1.8
Revenues — 2014	$70.6	$128.1

Factors Positively Affecting Operating Income:

- Increased contract services and robust demand for after-market parts.

Factors Negatively Impacting Operating Income:

- Decreased volume from machine sales primarily due to the completion of the large contract with the China Ministry of Railways (the "CRC").

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Outlook, Trends and Strategies

In addition to items noted in the Company's Annual Report on Form 10-K for the year ended December 31, 2013, the following significant items, risks, trends and strategies are expected to affect the Company for the remainder of 2014 and beyond:

- The Company will focus on the goal of providing top quartile returns for its stockholders by balancing its portfolio of businesses, and by executing its strategic and operational strategies with reasonable amounts of financial leverage.
- The Company will continue to build and transform its management team, build and develop strong core capabilities and develop an active and lean corporate center that balances costs with value added services.
- Management will continue to be selective and disciplined in allocating capital by rigorously analyzing projects and utilizing a return based capital allocation process. The Company expects capital expenditures in 2014 to exceed 2013 levels due to a higher level of committed contract renewals in the Harsco Metals & Minerals Segment and targeted investment in the Harsco Industrial Segment.
- The Company expects that the Infrastructure Transaction will provide synergies and growth potential in the Infrastructure strategic venture that create additional value for the Company's equity interest upon exit in the future.
- The Company expects its operational effective income tax rate to approximate 31 percent to 33 percent for the full year 2014.

Harsco Metals & Minerals Segment:

- The Company will focus on improving the Harsco Metals & Minerals Segment's returns through simplifying its business model, executing on operational efficiency opportunities, improving its contract outcomes through better contract portfolio management, and improving the contract mix through addressing underperforming contracts. In line with this focus, in May 2014, the Company began executing the first phase of Project Orion after conducting an analysis of the business to identify opportunities to improve its core processes and to simplify its organizational structure. The first phase of Project Orion will continue through the balance of 2014, with the second phase expected to begin in late 2014 or early 2015.
- The Company will continue its focus on ensuring that forecasted profits for contracts meet certain established requirements and deliver returns above its cost of capital. Project Orion's focus is intended to enable the Company to address underperforming contracts more rapidly with targeted actions to improve the operational efficiencies of the business through central protocols to monitor activities, structures and systems that aid in decision making, and processes designed to identify the best strategic actions available to address underperforming contracts and its overall contract portfolio. In connection with this focus, the possibility exists that the Company may take strategic actions that result in exit costs and non-cash asset impairment charges that may have an adverse effect on the Company's results of operations and liquidity.
- The Company will continue to focus on winning contracts in markets where steel production is increasing and where the customers value the Company's environmental solutions.
- The Company does not expect a material increase in steel production or pricing in 2014.
- During the second quarter of 2014, one of the Company's steel mill customers in Europe missed normal progress payments. The Company has approximately $14 million of receivables, excluding value added tax, with this customer. During the second quarter of 2014, the Company recorded a bad debt reserve of $3.6 million related to this receivable. The Company believes the remaining amounts are collectible; however, if there is an adverse change in the Company's view on collectibility, there could be a charge against income in future periods.
- The Company will monitor certain businesses within the Harsco Metals & Minerals Segment that produce products that are subject to increasing attention from regulatory agencies. The possibility exists that these regulatory agencies may issue new regulations or standards that may have a negative effect on the Company's results.

Harsco Industrial Segment:

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The Company is expecting another year of consistent performance for revenue and operating income in 2014 in the Harsco Industrial Segment, and will continue to focus on product innovation and development to drive strategic growth in its businesses.

- The Company acquired Hammco in January 2014 as part of the Company's focus on growing the Harsco Industrial Segment through disciplined expansion. This acquisition provides the Harsco Industrial Segment with an entry into the process cooler market.

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Harsco Rail Segment:

- Full year performance for this business is unfavorably impacted by the volume comparative of equipment deliveries from its large contract with the CRC, which were mostly completed during the first six months of 2013. Consequently, revenues for this Segment are expected to be modestly lower in 2014 compared with 2013. Notwithstanding the effects of the completion of its contract with the CRC, this Segment anticipates modest organic growth in its after-market parts business and expected deliveries of existing equipment orders with improving operating income and margins.
- The success in China has been leveraged to secure several new orders in other geographies. Recently, the Company secured a second contract award worth over $100 million through 2017 from the SBB, the federal railway system of Switzerland. The award comes as a follow-on option to the Company's previously awarded contract with the SBB worth more than $100 million. The Company's capabilities to compete and deliver on large projects provides increased opportunities to build out its pipeline further, and enables the Company to continue to pursue other large projects.
- The longer-term outlook for this Segment continues to be favorable. The global demand for railway maintenance-of-way equipment, parts and services continues to be strong, giving positive indication of further opportunities.

Infrastructure Strategic Venture:

- The Infrastructure strategic venture creates opportunities for additional value creation from the Company's equity interest in a stronger and larger business with a more diversified portfolio of services and offerings.
- As part of the Infrastructure Transaction, the Company is required to make a quarterly payment to its partner in the Infrastructure strategic venture, either (at the Company's election) (i) in cash, with total payments to equal approximately $22 million per year on a pre-tax basis (approximately $15 million per year after-tax), or (ii) in kind through the transfer of approximately 2.5% of the Company's ownership interest in the Infrastructure strategic venture on an annual basis (the "unit adjustment liability"). The Company's obligation to make such quarterly payments will cease upon the earlier of (i) the Infrastructure strategic venture achieving $487.0 million in last twelve months' earnings before interest, taxes, depreciation and amortization ("EBITDA") for three quarters, which need not be consecutive, or (ii) eight years after the closing of the Infrastructure Transaction. The Company intends to make these quarterly payments in cash and will continue to evaluate the implications of making payments in cash or in kind based upon performance of the Infrastructure strategic venture.
- The Purchase Agreement governing the Infrastructure Transaction provides for closing to be deferred with respect to the transfer of certain of our subsidiaries to Brand. Some of these transfers have not yet occurred. In the case of one such transfer, since the Company has not consummated the transfer of the relevant subsidiary to Brand before August 4, 2014, Brand may elect to unwind the sale of such subsidiary and, if Brand so elects, the Company will be required to reimburse to Brand the portion of the purchase price previously received by the Company for such entity. No such election has been made by Brand at this time, but its right to do so remains. Management does not believe the inability of the Company to satisfy the requirements of the Purchase Agreement with respect to the timing of the transfer of such entity will have a material adverse effect on the Company’s financial condition, results of operations or cash flows.

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Results of Operations

(In millions, except per share amounts)	Three Months Ended June 30 2014	2013	Six Months Ended June 30 2014	2013
Revenues from continuing operations	$534.6	$759.7	$1,047.3	$1,475.1
Cost of services and products sold	417.5	577.2	826.9	1,141.4
Selling, general and administrative expenses	78.0	125.6	144.8	250.3
Research and development expenses	2.0	2.2	4.6	4.4
Loss on disposal of the Harsco Infrastructure Segment and transaction costs	3.4	—	5.6	—
Other expenses	27.5	3.9	26.9	2.4
Operating income from continuing operations	6.2	50.8	38.6	76.6
Interest income	0.4	0.8	0.7	1.2
Interest expense	(12.0)	(12.9)	(23.4)	(24.6)
Change in fair value to the unit adjustment liability	(2.5)	—	(5.0)	—
Income tax expense from continuing operations	(4.3)	(11.5)	(8.8)	(16.5)
Equity in income (loss) of unconsolidated entities, net	(3.0)	0.6	(4.2)	0.6
Income (loss) from continuing operations	(15.1)	27.9	(2.1)	37.4
Diluted earnings (loss) per common share from continuing operations attributable to Harsco Corporation common stockholders	(0.19)	0.30	(0.04)	0.40
Effective income tax rate for continuing operations	(54.7)%	29.6%	80.4%	30.9%

Comparative Analysis of Consolidated Results

Revenues

Revenues for the second quarter of 2014 decreased $225.2 million or 29.6% from the second quarter of 2013. Revenues for the first six months of 2014 decreased $427.9 million or 29.0% from the first six months of 2013. Changes in revenues for the periods presented were attributable to the following significant items:

Change in Revenues — 2014 vs. 2013 (In millions)	Three Months Ended June 30, 2014	Six Months Ended June 30, 2014
Revenue decrease following the Infrastructure Transaction.	$(251.2)	$(467.2)
Net decreased revenues in the Harsco Rail Segment due principally to the completion of the large contract with CRC.	(8.9)	(24.0)
Net increased revenues in the Harsco Metals & Minerals Segment due to price/volume, primarily attributable to volume changes.	20.2	39.9
Net increased revenues in the Harsco Industrial Segment, primarily attributable to the effects of its business acquisition.	9.6	22.2
Impact of foreign currency translation.	5.1	1.2
Total change in revenues — 2014 vs. 2013	$(225.2)	$(427.9)

Cost of Services and Products Sold

Cost of services and products sold for the second quarter of 2014 decreased $159.7 million or 27.7% from the second quarter of 2013. Cost of services and products sold for the first six months of 2014 decreased $314.5 million or 27.6% from the first six months of 2013. Changes in cost of services and products sold for the periods presented were

attributable to the following significant items:

Change in Cost of Services and Products Sold — 2014 vs. 2013	Three Months Ended	Six Months Ended
(In millions)	June 30, 2014	June 30, 2014
Lower costs following the Infrastructure Transaction.	$(182.5)	$(341.3)
Impact of foreign currency translation.	2.9	(0.3)
Increased costs due to changes in revenues (exclusive of the effects of the timing of the Infrastructure Transaction, foreign currency translation, and fluctuations in commodity costs included in selling prices).	15.4	26.9
Other	4.5	0.2
Total change in cost of services and products sold — 2014 vs. 2013	$(159.7)	$(314.5)

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Selling, General and Administrative Expenses
Selling, general and administrative expenses for the second quarter of 2014 decreased $47.7 million or 37.9% from the second quarter of 2013. Selling, general and administrative expenses for the first six months of 2014 decreased $105.6 million or 42.2% from the first six months of 2013. The decrease was primarily related to the lower costs following the Infrastructure Transaction.

Loss on Disposal of Harsco Infrastructure Segment and Transaction Costs
The Company recorded an additional loss of $3.2 million and $3.9 million during the second quarter and first six months of 2014, respectively. The Company does not anticipate any further adjustments to the loss on the disposal of the Harsco Infrastructure Segment. Additionally, the Company incurred $0.2 million and $1.7 million of transaction costs during the second quarter and first six months of 2014, respectively, in conjunction with the Infrastructure Transaction.

Please see Note 3, Acquisitions and Dispositions, in Part I, Item 1, Financial Statements for additional information on the Infrastructure Transaction.

Other Expenses
This Condensed Consolidated Statements of Operations caption includes restructuring program costs, net gains on the disposal of non-core assets, impaired asset write-downs, employee termination benefit costs and costs to exit activities. The most significant changes in Other expenses, during the second quarter and first six months of 2014, relate to restructuring program costs associated with Project Orion and non-cash impaired asset write-downs. Additional information on Other expenses is included in Note 14, Other Expenses, in Part I, Item 1, Financial Statements.

	Three Months Ended June 30		Six Months Ended June 30	
(In thousands)	2014	2013	2014	2013
Restructuring Program costs (see Note 16)	$8,539	$—	$8,539	$—
Net gains	(650)	(877)	(3,008)	(4,569)
Impaired asset write-downs	13,982	—	14,080	689
Other (a)	5,645	4,805	7,249	6,266
Other expenses	$27,516	$3,928	$26,860	$2,386

(a) Other includes employee termination benefit costs and costs to exit activities that are not directly related to the restructuring programs detailed in Note 16, Restructuring Programs, in Part I, Item 1, Financial Statements.

Interest Expense
Interest expense during the second quarter and first six months of 2014 decreased $0.9 million and $1.2 million, respectively, from the second quarter and first six months of 2013. The decrease primarily reflects lower average borrowings offset by higher interest rates on short-term borrowings.

Change in Fair Value to the Unit Adjustment Liability
This caption represents the non-cash fair value adjustment to the Company's unit adjustment liability related to the Infrastructure Transaction.

As part of the Infrastructure Transaction, the Company is required to make a quarterly payment to its partner in the Infrastructure strategic venture. The resulting liability is reflected in the caption, Unit adjustment liability, on the Company's Condensed Consolidated Balance Sheets. The Company will recognize the change in fair value to the unit adjustment liability each period until the Company is no longer required to make these payments or chooses not to make these payments. The change in fair value to the unit adjustment liability is a non-cash expense. For the second quarter and first six months of 2014, the Company recognized expense of $2.5 million and $5.0 million, respectively,

related to the change in fair value to the unit adjustment liability.

The Company's obligation to make such quarterly payments will cease upon the earlier of (i) Brand achieving $487.0 million in last twelve months' EBITDA for three quarters, which need not be consecutive, or (ii) eight years after the closing of the Infrastructure Transaction. In addition, upon the initial public offering of Brand, the Company's quarterly payment obligation will decrease by the portion of CD&R's ownership interest sold or eliminated completely once CD&R's ownership interest in Brand falls below 20%. In the event of a liquidation of Brand, CD&R is entitled to a liquidation preference of approximately $336 million, plus any quarterly payments that had been paid in kind.

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The Company intends to make these quarterly payments in cash and will continue to evaluate the implications of making payments in cash or in kind based upon performance of the Infrastructure strategic venture. In the future, should the Company decide not to make the cash payment, the value of both the equity method investment in Brand and the related unit adjustment liability may be impacted, and the change may be reflected in earnings in that period.

Income Tax Expense

The effective income tax rate related to continuing operations for the three and six months ended June 30, 2014 was (54.7)% and 80.4%, respectively, compared with 29.6% and 30.9% for the three and six months ended June 30, 2013, respectively. The effective income tax rate related to continuing operations and income tax expense from continuing operations changed primarily due to the change in income (loss) from continuing operations and changes in losses generated in certain jurisdictions where no tax benefit can be recognized for both the three and six months ended June 30, 2014 compared with the three and six months ended June 30, 2013. The Company expects its operational effective income tax rate to approximate 31 percent to 33 percent for the full year 2014.

Income (Loss) from Continuing Operations

Loss from continuing operations was $15.1 million in the second quarter of 2014 compared with Income from continuing operations of $27.9 million in the second quarter of 2013. Loss from continuing operations was $2.1 million in the first six months of 2014 compared with the Income from continuing operations of $37.4 million in the first six months of 2013. The change is primarily related to the restructuring charge for Project Orion, the additional bad debt reserve and non-cash long-lived asset impairment charge for the Company's European steel mill customer in receivership, costs for site exits and non-cash long-lived asset impairment charges for the Harsco Metals & Minerals Segment, the non-cash change in fair value to the unit adjustment liability related to the Infrastructure Transaction, and the Company's equity in income (loss) of unconsolidated entities related to the Brand joint venture.

Liquidity and Capital Resources

Overview

The Company continues to have sufficient available liquidity. The Company currently expects operational and business needs to be met with cash from operations supplemented with borrowings from time to time due to historical patterns of seasonal cash flow and for the funding of various projects.

The Company continues to implement and perform capital efficiency initiatives to enhance liquidity. These initiatives have included: focused allocation of capital spending to projects where the highest returns can be achieved while redeploying existing capital investments; optimization of worldwide cash positions; reductions in discretionary spending; and frequent evaluation of customer and business-partner credit risk.

During the first six months of 2014, the Company’s operations provided $74.4 million in operating cash flow, an increase from the $56.4 million provided in the first six months of 2013. In the first six months of 2014, the Company invested $81.6 million in capital expenditures, mostly for the Harsco Metals & Minerals Segment, compared with $120.2 million invested in the first six months of 2013. Additionally, the Company paid $33.1 million in common stock dividends in the first six months of both 2014 and 2013, respectively.

The Company’s net cash borrowings increased by $44.3 million in the first six months of 2014, primarily to fund capital expenditures, principally in the Harsco Metals & Minerals Segment and for the Hammco acquisition.

The Company plans to redeploy discretionary cash for disciplined organic growth and international or market segment diversification; for growth in long-term, higher-return service contracts for the Harsco Metals & Minerals Segment, principally in targeted growth markets or for customer diversification; and for strategic investments or possible acquisitions in the Harsco Rail and Harsco Industrial Segments. The Company also foresees continuing its long and consistent history of paying dividends to stockholders.

The Company continues its focus on improving working capital efficiency. The Company's Continuous Improvement initiatives are being used to further improve effective and efficient use of working capital, particularly in accounts

receivable and inventories.

The Company also generated $6.1 million and $14.9 million in cash from asset sales in the first six months of 2014 and 2013, respectively. Asset sales have been a normal part of the Company's business model, primarily for the Harsco Metals & Minerals Segment.

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Sources and Uses of Cash

The Company’s principal sources of liquidity are cash from operations and borrowings under the Company's credit agreement, augmented by cash proceeds from asset sales. The primary drivers of the Company’s cash flow from operations are the Company’s revenues and income. Cash returns on capital investments made in prior years, for which limited cash is currently required, are a significant source of cash from operations. Depreciation expense related to these investments is a non-cash charge.

Major uses of operating cash flows and borrowed funds include: capital investments, principally in the Harsco Metals & Minerals Segment; payroll costs and related benefits; dividend payments; pension funding payments; inventory purchases for the Harsco Rail and Harsco Industrial Segments; income tax payments; debt principal and interest payments; insurance premiums and payments of self-insured casualty losses; payment of the unit adjustment liability and machinery, equipment, automobile and facility lease payments.

Resources available for cash requirements for operations and growth initiatives

In addition to utilizing cash from operations and cash proceeds from asset sales, the Company has bank credit facilities available throughout the world. Public markets are also accessed through discrete-term note issuance to investors. The Company also utilizes capital leases to finance the acquisition of certain equipment when appropriate which allows the Company to minimize capital expenditures. The Company expects to continue to utilize all these sources to meet future cash requirements for operations and growth initiatives.

The following table illustrates available credit at June 30, 2014:

	June 30, 2014		
(In millions)	Facility Limit	Outstanding Balance	Available Credit
Multi-year revolving credit agreement (a U.S.-based program)	$525.0	$88.5	$436.5

At June 30, 2014 and December 31, 2013, the Company had $88.5 million and $35.0 million, respectively, of borrowings outstanding under its credit agreement. At June 30, 2014 and December 31, 2013, all such balances were classified as long-term borrowings in the Condensed Consolidated Balance Sheets. Classification of such balances is based on the Company's ability and intent to repay such amounts over the subsequent twelve months, as well as the Company's current intent and ability to borrow for a period longer than a year. To the extent the Company expects to repay any amounts within the subsequent twelve months, the amounts are classified as short-term borrowings.

Credit Ratings and Outlook

The following table summarizes the Company’s current debt ratings:

Rating Agency	Long-term Notes	Watch / Outlook
Standard & Poor’s (S&P)	BB+	Negative Outlook
Moody’s	Ba1	Stable Outlook
Fitch	BBB-	Negative Outlook

Any future downgrades to the Company’s credit ratings may increase borrowing costs to the Company, while an improvement in the Company’s credit ratings may decrease such costs. However, any future downgrades in the Company’s credit ratings will not reduce availability under the Company's Credit Agreement.

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Working Capital Position

Changes in the Company's working capital are reflected in the following table:

(Dollars in millions)	June 30 2014	December 31 2013	Increase (Decrease)
Current Assets			
Cash and cash equivalents	$77.5	$93.6	$(16.1)
Trade accounts receivable, net	384.6	353.2	31.5
Other receivables	33.6	46.5	(12.9)
Inventories	176.3	155.7	20.7
Assets held-for-sale	—	114.0	(114.0)
Other current assets	88.6	75.8	12.7
Total current assets	760.6	838.8	(78.2)
Current Liabilities			
Short-term borrowings and current maturities	28.9	27.7	1.2
Accounts payable	191.2	181.4	9.8
Accrued compensation	55.3	53.1	2.2
Income taxes payable	7.9	7.2	0.7
Advances on contracts	66.0	24.1	42.0
Liabilities of assets held-for-sale	—	109.2	(109.2)
Due to unconsolidated affiliate	14.2	25.0	(10.8)
Unit adjustment liability	22.3	22.3	—
Other current liabilities	169.4	156.8	12.6
Total current liabilities	555.2	606.8	(51.6)
Working Capital	$205.4	$232.0	$(26.6)
Current Ratio (a)	1.4	1.4	

(a) Calculated as Total current assets divided by Total current liabilities.

The net $26.6 million decrease in working capital for the first six months of 2014 is due primarily to the following factors:

- Working capital was negatively affected by an increase in Advances on contracts of $42.0 million due to increased customer advances in the Harsco Rail Segment;

- Working capital was negatively affected by a decrease in Other receivables of $12.9 million due to the final working capital settlement related to the Infrastructure Transaction; and

- Working capital was negatively affected by an increase in Other current liabilities of $12.6 million primarily due to the timing of payment of other accruals.

These working capital decreases were partially offset by the following:

- Working capital was positively affected by an increase in Trade accounts receivable, net of $31.5 million due to the timing of invoicing and collections, primarily in the Harsco Metals & Minerals Segment;

- Working capital was positively affected by an increase in Inventories of $20.7 million due primarily to the long lead times associated with orders in the Harsco Rail Segment and the Hammco acquisition in the Harsco Industrial Segment;

- Working capital was positively affected by an increase in Other current assets of $12.7 million due to timing of disbursements related to prepaid expenses; and

The net impact of the settlement of Assets held-for-sale and Liabilities of assets held-for-sale related to the Infrastructure Transaction did not have a significant impact on the Company's working capital at June 30, 2014.

Certainty of Cash Flows

The certainty of the Company's future cash flows is underpinned by the long-term nature of the Company's metals services contracts, the order backlog for the Company's railway track maintenance services and equipment, and overall discretionary cash flows (operating cash flows plus cash from asset sales in excess of the amounts necessary for capital expenditures to maintain current revenue levels) generated by the Company. Historically, the Company has utilized these discretionary cash flows for growth-related capital expenditures, strategic acquisitions, debt repayment and dividend payments.

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The types of products and services that the Company provides are not subject to rapid technological change, which increases the stability of related cash flows. Additionally, the Company believes each business in the balanced portfolio is a leader in the industries and major markets the Company serves. Due to these factors, the Company is confident in the Company's future ability to generate positive cash flows from operations.

Cash Flow Summary

The Company’s cash flows from operating, investing and financing activities, as reflected in the Condensed Consolidated Statements of Cash Flows, are summarized in the following table:

(In millions)	Six Months Ended June 30 2014	2013
Net cash provided (used) by:		
Operating activities	$74.4	$56.4
Investing activities	(98.9)	(107.7)
Financing activities	9.5	49.3
Impact of exchange rate changes on cash	(1.2)	(4.1)
Net change in cash and cash equivalents	$(16.1)	$(6.2)

Cash provided by operating activities — Net cash provided by operating activities in the first six months of 2014 was $74.4 million, an increase of $18.1 million from the first six months of 2013. The increase is primarily attributable to increased customer advances, decreased incentive bonus payments, and timing of accounts receivable collections, partially offset by the net loss in the first half of 2014 compared with net income in the first half of 2013 and the timing of accounts payable disbursements.

Included in the Cash flows from operating activities section of the Condensed Consolidated Statement of Cash Flows is the caption Other, net. For the six months ended June 30, 2014, this caption consisted of principally the impact of non-cash impaired asset write-downs related to the Harsco Metals & Minerals Segment. For the six months ended June 30, 2013, there were no individually significant components of this caption.

Also included in the Cash flows from operating activities section of the Condensed Consolidated Statements of Cash Flows is the caption, Other assets and liabilities. For the six months ended June 30, 2014 and 2013, the decreases in this caption were $29.3 million and $20.0 million, respectively. A summary of the major components of this caption for the periods presented is as follows:

(In millions)	Six Months Ended June 30 2014	2013
Net cash provided (used) by:		
Change in net defined benefit pension liabilities	$(17.8)	$(12.8)
Change in prepaid expenses	(12.9)	(5.4)
Other	1.4	(1.8)
Total	$(29.3)	$(20.0)

Cash used by investing activities — Net cash used in investing activities in the first six months of 2014 was $98.9 million, a decrease of $8.8 million from the first six months of 2013. The net decrease was primarily due to a lower level of capital expenditures, primarily in the Harsco Metals & Minerals Segment and the final working capital adjustment related to the Infrastructure Transaction. Partially offsetting these decreases were the acquisition of Hammco and payment of the unit adjustment liability.

Cash provided by financing activities — Net cash provided by financing activities in the first six months of 2014 was $9.5 million, a decrease of $39.7 million from the first six months of 2013. The change was primarily due to a decrease in year-over-year net cash borrowings.

Debt Covenants

The Company's credit agreement contains covenants that provide for a maximum total consolidated debt to consolidated EBITDA ratio not to exceed 3.5 to 1.0, limit the proportion of subsidiary consolidated indebtedness to a

maximum of 10% of consolidated tangible assets and require a minimum total consolidated EBITDA to consolidated interest charges ratio of 3.0 to 1.0. The Company's 5.75% and 2.70% notes include covenants that require the Company to offer to repurchase the notes at 101% of par in the event of a change of control of the Company or disposition of substantially all of the Company's assets in combination with a downgrade in the Company's credit rating to non-investment grade. At June 30, 2014, the Company was in

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compliance with these covenants as the total consolidated debt to consolidated EBITDA ratio was 2.7 to 1.0, the proportion of subsidiary consolidated indebtedness to consolidated tangible assets was 2.7% and total consolidated EBITDA to consolidated interest charges was 7.2 to 1.0. Based on balances at June 30, 2014, the Company could increase borrowings by $266.2 million and still be in compliance with these debt covenants. Alternatively, keeping all other factors constant, the Company's EBITDA could decrease by $76.0 million and the Company would still be within these debt covenants. The Company expects to continue to be in compliance with these debt covenants for at least the next twelve months.

Cash and Value-Based Management

The Company has various cash management systems throughout the world that centralize cash in various bank accounts where it is economically justifiable and legally permissible to do so. These centralized cash balances are then redeployed to other operations to reduce short-term borrowings and to finance working capital needs or capital expenditures. Due to the transitory nature of cash balances, they are normally invested in bank deposits that can be withdrawn at will or in very liquid short-term bank time deposits and government obligations. The Company's policy is to use the largest banks in the various countries in which the Company operates. The Company monitors the creditworthiness of banks and when appropriate will adjust banking operations to reduce or eliminate exposure to less credit worthy banks. The Company plans to continue the strategy of targeted, prudent investing for strategic purposes for the foreseeable future and to make more efficient use of existing investments.

At June 30, 2014, the Company's consolidated cash and cash equivalents included approximately $74 million held by non-U.S. subsidiaries. At June 30, 2014, less than 10% of the Company's consolidated cash and cash equivalents had regulatory restrictions that would preclude the transfer of funds with and among subsidiaries. The cash and cash equivalents held by non-U.S. subsidiaries also included approximately $25 million held in consolidated strategic ventures. The strategic venture agreements may require strategic venture partner approval to transfer funds with and among subsidiaries. While the Company's remaining non-U.S. cash and cash equivalents can be transferred with and among subsidiaries, the majority of these non-U.S. cash balances will be used to support the ongoing working capital needs and continued growth of the Company's non-U.S. operations.

The Company currently expects to continue paying dividends to stockholders. In July 2014, the Company declared its 258th consecutive quarterly cash dividend, payable in November 2014.

The Company's financial position and debt capacity should enable it to meet current and future requirements. As additional resources are needed, the Company should be able to obtain funds readily and at competitive costs. The Company intends to continue investing in high-return, organic growth projects and prudent, strategic alliances and ventures; and pay cash dividends as a means of enhancing stockholder value.

Recently Adopted and Recently Issued Accounting Standards

Information on recently adopted and recently issued accounting standards is included in Note 2, Recently Adopted and Recently Issued Accounting Standards, in Part I, Item 1, Financial Statements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risks have not changed significantly from those disclosed in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2013.

ITEM 4. CONTROLS AND PROCEDURES

Based on the evaluation required by Securities Exchange Act Rules 13a-15(b) and 15d-15(b), the Company’s management, including the Company's Principal Executive Officer and Principal Financial Officer, conducted an evaluation of the effectiveness of disclosure controls and procedures, as defined in Securities Exchange Act Rules 13a-15(e) and 15d-15(e), at June 30, 2014. Based on that evaluation, the Company's Principal Executive Officer and Principal Financial Officer concluded that the disclosure controls and procedures were effective at June 30, 2014. There have been no changes in internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, internal control over financial reporting during the second quarter of 2014.

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PART II — OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Information on legal proceedings is included in Note 10, Commitments and Contingencies, in Part I, Item 1, Financial Statements.

ITEM 1A. RISK FACTORS

The Company's risk factors as of June 30, 2014 have not changed materially from those described in Part 1, Item 1A, “Risk Factors,” of the Company’s Annual Report on Form 10-K for the year ended December 31, 2013.

ITEM 6. EXHIBITS

See the Exhibit Index following the signature page to this Quarterly Report on Form 10-Q for a list of exhibits filed or furnished with this report, which Exhibit Index is incorporated herein by reference.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

HARSCO CORPORATION
(Registrant)

DATE August 7, 2014	/s/ CHRISTOPHER J. STUMP Christopher J. Stump Corporate Controller (Principal Accounting Officer)

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EXHIBIT INDEX

Exhibit Number	Description
10.1	Specimen Form of Performance Share Units Agreement.
10.2	Specimen Form of Restricted Stock Units Agreement.
10.3	Specimen Form of Stock Appreciation Rights Agreement.
10.4	Notification Letter to F.N. Grasberger dated April 8, 2014.
10.5	Notification Letter to C. Stump dated April 29, 2014.
31	Certification Pursuant to Rule 13a-14(a) or 15d-14(a), as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (Principal Executive Officer and Principal Financial Officer).
32	Certifications Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Principal Executive Officer and Principal Financial Officer).
101	The following financial statements from Harsco Corporation's Quarterly Report on Form 10-Q for the quarter ended June 30, 2014, filed with the Securities and Exchange Commission on August 7, 2014, formatted in XBRL (Extensible Business Reporting Language): (i) the Condensed Consolidated Balance Sheets; (ii) the Condensed Consolidated Statements of Operations; (iii) the Condensed Consolidated Statements of Comprehensive Income (Loss); (iv) the Condensed Consolidated Statements of Cash Flows; (v) the Condensed Consolidated Statements of Equity; and (vi) the Notes to Condensed Consolidated Financial Statements.

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