

LSB INDUSTRIES INC
Form 10-K
March 03, 2011
LSB Industries, Inc.

Form 10-K (12-31-2010)

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2010

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: 1-7677

LSB INDUSTRIES, INC.
(Exact Name of Registrant as Specified in its Charter)

Delaware
(State of Incorporation)

73-1015226
(I.R.S. Employer
Identification No.)

16 South Pennsylvania Avenue
Oklahoma City, Oklahoma
(Address of Principal Executive Offices)

73107
(Zip Code)

Registrant's Telephone Number, Including Area Code: (405) 235-4546

Securities Registered Pursuant to Section 12(b) of the Act:

Name of Each Exchange

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Title of Each Class	On Which Registered
Common Stock, Par Value \$.10	New York Stock Exchange
Preferred Share Purchase Rights	New York Stock Exchange

(Facing Sheet Continued)

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files).

☐ Yes ☐ No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

☐

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

Large accelerated filer ☐ Accelerated filer ☒

Non-accelerated filer ☐ Smaller reporting company ☐

(Do not check if a smaller reporting company)

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Act). ☐ Yes ☒ No

The aggregate market value of the Registrant's voting common equity held by non-affiliates of the Registrant, computed by reference to the price at which the voting common stock was last sold as of June 30, 2010, was approximately \$222 million. As a result, the Registrant is an accelerated filer as of December 31, 2010. For purposes of this computation, shares of the Registrant's common stock beneficially owned by each executive officer and director of the Registrant were deemed to be owned by affiliates of the Registrant as of June 30, 2010. Such determination should not be deemed an admission that such executive officers and directors of our common stock are, in fact, affiliates of the Registrant or affiliates as of the date of this Form 10-K.

As of February 28, 2011, the Registrant had 21,156,897 shares of common stock outstanding (excluding 4,320,462 shares of common stock held as treasury stock).

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PART I

ITEM 1. BUSINESS

General

LSB Industries, Inc. (“LSB” or “Registrant”) was formed in 1968 as an Oklahoma corporation and became a Delaware corporation in 1977. LSB is a diversified holding company involved in manufacturing, marketing and engineering operations through its subsidiaries. LSB and its wholly-owned subsidiaries (the “Company”, “We”, “Us”, or “Our”) own the following core businesses:

- Climate Control Business manufactures and sells a broad range of air conditioning and heating products in the niche markets we serve consisting of geothermal and water source heat pumps, hydronic fan coils, large custom air handlers, modular geothermal chillers and other related products used to control the environment in various structures. Our markets include commercial/institutional and residential new building construction, renovation of existing buildings and replacement of existing systems.
- Chemical Business manufactures and sells nitrogen based chemical products produced from four plants located in Arkansas, Alabama, Oklahoma, and Texas for the industrial, mining and agricultural markets. Our products include high purity and commercial grade anhydrous ammonia, industrial and fertilizer grade ammonium nitrate (“AN”), urea ammonium nitrate (“UAN”), sulfuric acids, nitric acids in various concentrations, nitrogen solutions, diesel exhaust fluid (“DEF”) and various other products. During the fourth quarter of 2010, we began sustained production of anhydrous ammonia at our previously idled chemical plant located in Oklahoma.

We believe our Climate Control Business has developed leadership positions in certain niche markets by offering extensive product lines, customized products and improved technologies. Under this focused strategy, we have developed what we believe to be the most extensive line of geothermal and water source heat pumps and hydronic fan coils in the United States (“U.S.”). Further, we believe that we were a pioneer in the use of geothermal technology in the climate control industry and have used it to create what we believe to be the most energy efficient climate control systems commercially available today. We employ highly flexible production capabilities that allow us to custom design units for new construction as well as the retrofit and replacement markets. This flexibility positions us well for an eventual recovery in commercial/institutional and residential construction markets.

In recent years, we have put heavy emphasis on our geothermal heating, ventilation, and air conditioning (“HVAC”) products, which are considered “green” technology and a form of renewable energy. We believe our geothermal systems are among the most energy efficient systems available in the market for heating and cooling applications in commercial/institutional and single family new construction as well as replacement and renovation markets. In 2010, we captured approximately 38% of the geothermal market, based on Air-Conditioning, Heating and Refrigeration Institute (“AHRI”) reported sales of these products. Although the general construction level has been lower than some previous years in both the commercial/institutional and residential sectors, we have continued to increase our market share of the growing geothermal heating and cooling market.

Our Chemical Business engages in the manufacturing and selling of nitrogen based chemical products from four chemical production facilities located in El Dorado, Arkansas (the “El Dorado Facility”), Cherokee, Alabama (the “Cherokee Facility”), Pryor, Oklahoma (the “Pryor Facility”) and Baytown, Texas (the “Baytown Facility”). Our products include high purity and commercial grade anhydrous ammonia, industrial and fertilizer grade AN, UAN, sulfuric acids, nitric acids in various concentrations, nitrogen solutions, DEF and various other products. Our Chemical Business is a supplier to some of the world’s leading chemical and industrial companies. By focusing on specific geographic areas, we have developed freight and distribution advantages over many of our competitors, and we believe our Chemical Business has established leading regional market positions.

We sell most of our industrial and mining products to customers pursuant to contracts containing minimum volumes or cost plus a profit provision. These contractual sales stabilize the effect of commodity cost changes. Periodically we enter into forward sales commitments for agricultural products but we sell most of our agricultural products at the current spot market price in effect at time of shipment.

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As discussed below under “Chemical Business - Agricultural Products,” the Pryor Facility began limited production in the first quarter of 2010 but did not reach sustained production of anhydrous ammonia until the fourth quarter of 2010. This facility’s production will be predominantly agricultural products. We expect this additional production will alter the ratio of our sales of agricultural products to our sales of industrial acids and mining products in the future.

Certain statements contained in this Part I may be deemed to be forward-looking statements. See "Special Note Regarding Forward-Looking Statements."

Current State of the Economy

Since our two core business segments serve several diverse markets, we consider market fundamentals for each market individually as we evaluate economic conditions.

Climate Control Business - Sales for 2010 were down 6% from 2009 due to a 9% reduction in commercial/institutional product sales partially offset by a 6% increase in residential product sales. The reduction in commercial/institutional sales was due to lower order levels during the latter part of 2009 and first quarter of 2010 as a result of the slowdown in commercial/institutional construction coupled with a lower product order backlog at the beginning of 2010 compared with the beginning of 2009. We have seen an increase in the level of commercial/institutional orders in the last three quarters of 2010 over the order levels in 2009. Sales and order levels of our residential products continue to increase year over year despite the slowdown in new residential construction. Based upon published reports of leading indicators, including the Construction Market Forecasting Service (“CMFS”) published by McGraw-Hill as well as the National Architecture Billings Index (“NABI”) published by American Institute of Architects (“AIA”), the overall commercial/institutional construction sector should increase modestly during 2011, where as CMFS and AIA have projected more aggressive growth in residential construction contract activity during 2011. Another factor that may affect product order rates going forward is the potential for growth in our highly energy-efficient geothermal water-source heat pumps, which could benefit significantly from government stimulus programs, including various tax incentives, although we cannot predict the impact these programs will have on our business.

The Chemical Business - Our Chemical Business’ primary markets are industrial, mining and agricultural. During 2010, approximately 61% of our Chemical Business’ sales were into industrial and mining markets of which approximately 69% of these sales are to customers that have contractual obligations to purchase a minimum quantity or allow us to recover our cost plus a profit, irrespective of the volume of product sold. During 2010, customer demand for our industrial and mining products increased over 2009. We believe that such demand will continue to increase in 2011 as the industrial markets in the United States continue to recover based on the American Chemistry Council’s Chemistry and Economic Report.

The remaining 39% of our Chemical Business’ sales in 2010 were made into the agricultural fertilizer markets to customers that primarily purchase at spot market prices and not pursuant to contractual arrangements. Our agricultural sales volumes and margins depend upon the supply of and the demand for fertilizer, which in turn depends on the market fundamentals for crops including corn, wheat and forage. The current outlook according to most market indicators, including reports in Green Markets, Fertilizer Week and the USDA’s World Agricultural Supply and Regional Estimates, point to positive supply and demand fundamentals for the types of nitrogen fertilizer products we produce and sell. However, it is possible that the fertilizer outlook could change if there are unanticipated changes in commodity prices, acres planted or unfavorable weather conditions. During 2010, the anhydrous ammonia market price increased while natural gas costs generally declined. Our Cherokee and Pryor Facilities produce anhydrous ammonia and UAN from natural gas and have benefited from increased margins. On the other hand, our El Dorado Facility is at a current cost disadvantage for their agricultural grade AN, which is produced from purchased ammonia, compared to their competitors that produce from natural gas.

See further discussion relating to the economy under various risk factors under Item 1A of this Part 1 and “Overview-Economic Conditions” of the Management’s Discussion and Analysis of Financial Condition and Results of Operations (“MD&A”) contained in this report.

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Website Access to Company's Reports

Our internet website address is www.lsb-okc.com. Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to section 13(a) or 15(d) of the Exchange Act are available free of charge through our website within a reasonable amount of time after they are electronically filed with, or furnished to, the Securities and Exchange Commission ("SEC").

Segment Information and Foreign and Domestic Operations and Export Sales

Schedules of the amounts of net sales, gross profit, operating income (loss) and identifiable assets attributable to each of our lines of business and of the amount of our export sales in the aggregate and by major geographic area for each of the last three years appear in Note 21 of the Notes to Consolidated Financial Statements included elsewhere in this report.

Climate Control Business

General

Our Climate Control Business manufactures and sells a broad range of standard and custom designed geothermal and water source heat pumps and hydronic fan coils as well as large custom air handlers and modular chiller systems, including modular geothermal chillers. These products are for use in commercial/institutional and residential HVAC systems. Our products are installed in some of the most recognizable commercial/institutional developments in the United States, including the Prudential Tower, Rockefeller Plaza, Trump Tower, Time Warner Center and many others. In addition, we have a significant presence in the lodging sector with installations in numerous Hyatt, Marriott, Four Seasons, Starwood, Ritz Carlton and Hilton hotels. During 2009 and 2010, our Climate Control Business saw a significant decline in sales associated with the multi-family residential and lodging sectors due to the economic downturn.

The following table summarizes net sales information relating to our products of the Climate Control Business:

	2010	2009	2008
Percentage of net sales of the Climate Control Business:			
Geothermal and water source heat pumps	69%	68%	61%
Hydronic fan coils	15%	17%	27%
Other HVAC products	16%	15%	12%
	100%	100%	100%
Percentage of LSB's consolidated net sales:			
Geothermal and water source heat pumps	28%	34%	25%
Hydronic fan coils	6%	9%	11%
Other HVAC products	7%	7%	5%
	41%	50%	41%

Market Conditions - Climate Control Business

As discussed above, based upon published reports of leading indicators, including CMFS as well as AIA, the overall commercial/institutional construction sector should increase modestly during 2011, where as CMFS and AIA have projected more aggressive growth in residential construction contract activity during 2011.

In addition, we believe that tax credits and incentives, and certain planned direct spending by the federal government contained in the American Reinvestment and Recovery Act of 2009, have and could continue to stimulate sales of our geothermal heat pump products, as well as other “green” products.

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Geothermal and Water Source Heat Pumps

We believe our Climate Control Business is a leading provider of geothermal and water source heat pumps to the commercial/institutional construction and renovation markets in the United States. Water source heat pumps are highly efficient heating and cooling products, which enable individual room climate control through the transfer of heat using a water pipe system connected to a centralized cooling tower or heat injector. Water source heat pumps enjoy a broad range of commercial/institutional applications, particularly in medium to large sized buildings with many small, individually controlled spaces. We believe the market share for commercial/institutional water source heat pumps relative to other types of heating and air-conditioning systems will continue to grow due to the relative efficiency and longevity of such systems, as well as due to the emergence of the replacement market for those systems.

We have also developed the use of geothermal heat pumps in residential and commercial/institutional applications. Geothermal systems, which circulate water or a combination of water and antifreeze through an underground heat exchanger, are among the most energy efficient systems currently available in the market. We believe the energy efficiency, longer life, and relatively short payback periods of geothermal systems, as compared with other systems, as well as tax incentives that are available to homeowners and businesses when installing geothermal systems, will continue to increase demand for our geothermal products. Our products are sold to the commercial/institutional markets, as well as single and multi-family residential new construction, renovation and replacements.

Hydronic Fan Coils

We believe that our Climate Control Business is a leading provider of hydronic fan coils targeting the commercial/institutional markets. Hydronic fan coils use heated or chilled water provided by a centralized chiller or boiler, through a water pipe system, to condition the air and allow individual room control. Hydronic fan coil systems are quieter, have longer lives and lower maintenance costs than other comparable systems used where individual room control is required. Important components of our strategy for competing in the commercial/institutional renovation and replacement markets include the breadth of our product line coupled with customization capability provided by a flexible manufacturing process. Hydronic fan coils enjoy a broad range of commercial/institutional applications, particularly in medium to large sized buildings with many small, individually controlled spaces.

Production, Capital Investments and Backlog - Climate Control Business

We manufacture our products in many sizes and configurations, as required by the purchaser, to fit the space and capacity requirements of hotels, motels, schools, hospitals, apartment buildings, office buildings and other commercial/institutional or residential structures. In addition, most customer product orders are placed well in advance of required delivery dates.

During 2010, we invested approximately \$7.2 million in additional property, plant and equipment ("PP&E") primarily relating to the exercise of an option, pursuant to the terms of the underlying operating lease, to purchase a portion of a production facility. Our investment also included production equipment and other upgrades for additional capacity relating to our Climate Control Business.

As of December 31, 2010, we have committed to spend an additional \$1.8 million primarily for production equipment and facility upgrades. Additional investments will depend upon our long-term outlook for the economic conditions that might affect our markets. These investments have and will continue to increase our capacity to produce and distribute our Climate Control products. See discussions under "Liquidity and Capital Resources-Capital Expenditures" of Item 7 of Part II of this report, including Advanced Manufacturing Energy Credits awarded to two subsidiaries of the Climate Control Business.

As of December 31, 2010 and 2009, the backlog of confirmed customer product orders (purchase orders from customers that have been accepted and received credit approval) for our Climate Control Business was approximately \$47.6 million and \$32.2 million, respectively. The increase in our backlog is primarily the result of increased order levels for our commercial/institutional products, which typically have longer lead times for production scheduling. The backlog of product orders generally does not include amounts relating to shipping and

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handling charges, service orders or service contract orders and exclude contracts related to our engineering and construction business due to the relative size of individual projects and, in some cases, extended timeframe for completion beyond a twelve-month period.

Historically, we have not experienced significant cancellations relating to our backlog of confirmed customer product orders and we expect to ship substantially all of these orders within the next twelve months; however, it is possible that some of our customers could cancel a portion of our backlog or extend the shipment terms.

Distribution - Climate Control Business

Our Climate Control Business sells its products primarily to mechanical contractors, original equipment manufacturers (“OEMs”) and distributors. Our sales to mechanical contractors primarily occur through independent manufacturers' representatives, who also represent complementary product lines not manufactured by us. OEMs generally consist of other air conditioning and heating equipment manufacturers who resell under their own brand name the products purchased from our Climate Control Business in competition with us. The following table summarizes net sales to OEMs relating to our products of the Climate Control Business:

	2010	2009	2008
Net sales to OEMs as a percentage of:			
Net sales of the Climate Control Business	24%	23%	20%
LSB's consolidated net sales	10%	11%	9%

Market - Climate Control Business

Our Climate Control Business market includes commercial/institutional and residential new building construction, renovation of existing buildings and replacement of existing systems.

Raw Materials and Components - Climate Control Business

Numerous domestic and foreign sources exist for the materials and components used by our Climate Control Business, which include compressors, copper, steel, electric motors, aluminum, and valves. Periodically, our Climate Control Business enters into futures contracts for copper. We do not anticipate any difficulties in obtaining necessary materials and components for our Climate Control Business. Although we believe we will be able to pass to our customers the majority of any cost increases in the form of higher prices, the timing of these price increases could lag the increases in the cost of materials and components. While we believe we will have sufficient sources for materials and components, a shortage could impact production of our Climate Control products.

Regulatory Matters - Climate Control Business

The American Reinvestment and Recovery Act of 2009 contains significant incentives for the installation of our geothermal products. Also see discussion concerning Advanced Manufacturing Energy Credits awarded to two subsidiaries under “Liquidity and Capital Resources - Capital Expenditures” of Item 7 of Part II of this report.

Competition - Climate Control Business

Our Climate Control Business competes primarily with several companies, such as Carrier, Trane, Florida Heat Pump, and McQuay, some of whom are also our customers. Some of our competitors serve other markets and have greater financial and other resources than we do. We believe our Climate Control Business manufactures a broader line of geothermal and water source heat pump and fan coil products than any other manufacturer in the United States and

that we are competitive as to price, service, warranty and product performance.

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Continue to Introduce New Products - Climate Control Business

Based on business plans and key objectives submitted by subsidiaries within our Climate Control Business, we expect to continue to launch new products and product upgrades in an effort to maintain and increase our current market position and to establish a presence in new markets served by the Climate Control Business.

Chemical Business

General

Our Chemical Business manufactures products for three principal markets:

- anhydrous ammonia, fertilizer grade AN, UAN, and ammonium nitrate ammonia solution (“ANA”) for agricultural applications,
- high purity and commercial grade anhydrous ammonia, high purity AN, sulfuric acids, concentrated, blended and regular nitric acid, mixed nitrating acids, and DEF for industrial applications, and
 - industrial grade AN and solutions for the mining industry.

The following table summarizes net sales information relating to our products of the Chemical Business:

	2010	2009	2008
Percentage of net sales of the Chemical Business:			
Agricultural products	39%	41%	36%
Industrial acids and other chemical products	36%	37%	38%
Mining products	25%	22%	26%
	100%	100%	100%
Percentage of LSB’s consolidated net sales:			
Agricultural products	22%	20%	20%
Industrial acids and other chemical products	21%	18%	22%
Mining products	15%	11%	15%
	58%	49%	57%

Market Conditions - Chemical Business

We discuss below certain details of our agricultural products, industrial acids and other chemical products, mining products, major customers, raw materials and other sales and industry issues affecting our Chemical Business.

As discussed above and in more detail under “Overview-Economic Conditions” of the MD&A contained in this report, it appears that customer demand for our industrial, mining and agricultural products will be sufficiently strong to allow us to run the four chemical plants at optimal production rates, which is an important operating characteristic in chemical process plants. The industrial and mining customer demand is predominantly driven by contractual arrangements with certain large customers. The fertilizer outlook could be affected by significant changes in commodity prices, acres planted or weather conditions.

Agricultural Products

Our Chemical Business produces agricultural grade AN at the El Dorado Facility, anhydrous ammonia and UAN at the Pryor Facility, and anhydrous ammonia, UAN, and ANA at the Cherokee Facility; all of which are nitrogen based fertilizers. Farmers and ranchers decide which type of nitrogen-based fertilizer to apply based on the crop planted, soil

and weather conditions, regional farming practices and relative nitrogen fertilizer prices. Our agricultural markets include a high concentration of pastureland and row crops, which favor our products. We sell these agricultural products to farmers, ranchers, fertilizer dealers and distributors primarily in the ranch land and grain production markets in the United States. We develop our market position in these areas by emphasizing high quality products, customer service and technical advice. During the past few years, we have been successful in expanding outside our traditional markets by barging to distributors on the Tennessee and Ohio rivers, and by rail

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into certain Western States. The El Dorado Facility produces a high performance AN fertilizer that, because of its uniform size, is easier to apply than many competing nitrogen-based fertilizer products.

Our subsidiary, El Dorado Chemical Company (“EDC”) establishes long-term relationships with end-users through its network of wholesale and retail distribution centers and our subsidiary, Cherokee Nitrogen Company (“CNC”) sells directly to agricultural customers. Our subsidiary, Pryor Chemical Company (“PCC”), which owns the Pryor Facility, is primarily selling anhydrous ammonia for the agricultural market and is also a party to an UAN purchase and sale agreement (the “UAN Agreement”) with Koch Nitrogen Company (“Koch”) under which Koch agrees to purchase and distribute substantially all of the UAN at market prices produced at the Pryor Facility. The term of the UAN Agreement is through June 2014, but may be terminated earlier by either party pursuant to the terms of the agreement.

The Pryor Facility began limited production of anhydrous ammonia and UAN in the first quarter of 2010. The Pryor Facility did not reach sustained production of anhydrous ammonia until the fourth quarter of 2010. Throughout November and December, market demand for ammonia was strong and most ammonia produced at the Pryor Facility was sold, rather than converted to UAN. During November and December 2010, the Pryor Facility produced a total of approximately 33,000 tons of anhydrous ammonia. Approximately 4,700 tons of the ammonia were converted into 11,500 tons of UAN and most of the balance was sold as ammonia. We expect to begin to convert more anhydrous ammonia to UAN, which will be sold to Koch as discussed above. Currently, the products sold from the Pryor Facility are predominantly agricultural fertilizer.

Industrial Acids and Other Chemical Products

Our Chemical Business manufactures and sells industrial acids and other chemical products primarily to the polyurethane, paper, fibers, fuel additives, emission control, and electronics industries. We are a major supplier of concentrated nitric acid and mixed nitrating acids, specialty products used in the manufacture of fibers, gaskets, fuel additives, ordnance, and other chemical products. In addition, at the El Dorado Facility, we produce and sell blended and regular nitric acid and we are a niche market supplier of sulfuric acid, primarily to the region’s key paper and related chemical manufacturers. At the Cherokee Facility, we are also a niche market supplier of industrial and high purity ammonia for many specialty applications, including the reduction of air emissions from power plants. As discussed below under “Introduction of New Product” of this Item 1, in January 2010, the Cherokee Facility began producing and selling DEF. In addition, the Pryor Facility is a supplier of anhydrous ammonia to industrial markets for use in a number of industrial manufacturing applications.

We believe the Baytown Facility is one of the largest nitric acid manufacturing units in the United States, with demonstrated capacity exceeding 1,350 short tons per day. The majority of the Baytown Facility’s production is sold to Bayer pursuant to a long-term contract (the “Bayer Agreement”) that provides for a pass-through of certain costs, including the anhydrous ammonia costs, plus a profit. The initial term of the Bayer Agreement is through June 2014, with certain renewal options.

We compete based upon service, price, location of production and distribution sites, product quality and performance. We also believe we are one of the largest domestic merchant marketers of concentrated and blended nitric acids and provide inventory management as part of the value-added services offered to certain customers.

Mining Products

Our Chemical Business manufactures industrial grade AN at the El Dorado Facility and 83% AN solution at the Cherokee Facility for the mining industry. Effective January 1, 2010, EDC is a party to a long-term cost-plus supply agreement (the “Orica Agreement”). Under the Orica Agreement, EDC supplies Orica International Pte Ltd. with a significant volume of industrial grade AN per year for a term through December 2014. The Orica Agreement replaced

EDC's previous agreement to supply industrial grade AN to Orica USA, Inc.

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Major Customers - Chemical Business

The following summarizes net sales to our major customers relating to our products of the Chemical Business:

	2010	2009	2008
Net sales to Orica as a percentage of:			
Net sales of the Chemical Business	18%	14%	19%
LSB's consolidated net sales	11%	7%	11%
Net sales to Bayer as a percentage of:			
Net sales of the Chemical Business	13%	14%	19%
LSB's consolidated net sales	8%	7%	11%

Raw Materials - Chemical Business

The products our Chemical Business manufactures are primarily derived from the following raw material feedstocks: anhydrous ammonia, natural gas and sulfur. These raw material feedstocks are commodities, subject to price fluctuations.

The El Dorado Facility purchases approximately 200,000 tons of anhydrous ammonia and 55,000 tons of sulfur annually and produces and sells approximately 470,000 tons of nitrogen-based products and approximately 165,000 tons of sulfuric acid per year. Although anhydrous ammonia is produced from natural gas, the price does not necessarily follow the spot price of natural gas in the U.S. because anhydrous ammonia is an internationally traded commodity and the relative price is set in the world market while natural gas is primarily a nationally traded commodity. The ammonia supply to the El Dorado Facility is transported from the Gulf of Mexico by pipeline. Under an agreement with its principal supplier of anhydrous ammonia, EDC purchases a majority of its anhydrous ammonia requirements for its El Dorado Facility through December 2012 from this supplier. Periodically, we will enter into futures/forward contracts to economically hedge the cost of certain of the anhydrous ammonia requirements. We believe that we can obtain anhydrous ammonia from other sources in the event of an interruption of service under the above-referenced contract. Prices for anhydrous ammonia during 2010 ranged from \$300 to \$470 per metric ton. During 2010, the average prices for sulfur ranged from \$90 to \$160 per long ton.

The Cherokee Facility normally consumes 5 to 6 million MMBtu's of natural gas to produce and sell approximately 300,000 to 370,000 tons of nitrogen-based products per year. Natural gas is a primary raw material for producing anhydrous ammonia and UAN. The Cherokee Facility's natural gas feedstock requirements are generally purchased at spot market price. Periodically, we will enter into futures/forward contracts to economically hedge the cost of certain of the natural gas requirements. In 2010, daily spot prices per MMBtu, excluding transportation, ranged from \$3.11 to \$7.37. Periodically, the Cherokee Facility purchases anhydrous ammonia to supplement its annual production capacity of approximately 175,000 tons. Anhydrous ammonia can be delivered to Cherokee Facility by truck, rail or barge.

The Baytown Facility typically consumes more than 100,000 tons of purchased anhydrous ammonia per year; however, the majority of the Baytown Facility's production is sold to Bayer pursuant to the Bayer Agreement that provides for a pass-through of certain costs, including the anhydrous ammonia costs, plus a profit.

At the Pryor Facility, natural gas is a primary raw material for producing anhydrous ammonia and UAN. The Pryor Facility's natural gas feedstock requirements are generally purchased at spot market price. Periodically, we will enter into futures/forward contracts to economically hedge the cost of certain of the natural gas requirements. We plan to produce and sell approximately 325,000 tons of UAN annually. In addition to the UAN production, we believe we have excess ammonia capacity which, if achievable, would allow us to sell up to 90,000 tons of ammonia annually. At

these rates, the Pryor Facility would consume approximately 6.9 million MMBtu's of natural gas annually.

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Spot anhydrous ammonia, natural gas and sulfur costs have fluctuated dramatically in recent years. The following table shows, for the periods indicated, the high and low published prices for:

- ammonia based upon the low Tampa metric price per ton as published by Fertecon and FMB Ammonia reports,
- natural gas based upon the daily spot price at the Tennessee 500 pipeline pricing point, and
- sulfur based upon the average quarterly Tampa price per long ton as published in Green Markets.

	Ammonia Price Per Metric Ton		Natural Gas Prices Per MMBtu				Sulfur Price Per Long Ton
	High	Low	High	Low	High	Low	
2010	\$470	\$300	\$ 7.37	\$3.11	\$160	\$ 90	
2009	\$355	\$125	\$ 6.08	\$1.87	\$ 30	minimal	
2008	\$931	\$125	\$13.16	\$5.36	\$617	\$150	

As of February 28, 2011, the published price, as described above, for ammonia was \$515 per metric ton and natural gas was \$3.75 per MMBtu. The price per long ton for sulfur was \$185 per long ton.

Sales Strategy - Chemical Business

Our Chemical Business has pursued a strategy of developing customers that purchase substantial quantities of products pursuant to sales agreements and/or pricing arrangements that provide for the pass through of raw material costs in order to minimize the impact of the uncertainty of the sales prices of our products in relation to the cost of raw materials (anhydrous ammonia, natural gas and sulfur). These pricing arrangements help mitigate the volatility risk inherent in the raw material feedstocks. For 2010, approximately 61% of the Chemical Business' sales were into industrial and mining markets of which approximately 69% of these sales were made pursuant to these types of arrangements. The remaining 39% of our 2010 sales were into agricultural markets primarily at the price in effect at time of shipment. We enter into futures/forward contracts to economically hedge the cost of natural gas and anhydrous ammonia for the purpose of securing the profit margin on a certain portion of our sales commitments with firm sales prices in our Chemical Business. During 2011, we expect that the agricultural sales as a percent of total sales will increase significantly as a result of the planned annual production of 325,000 ton of UAN at the Pryor Facility.

The sales prices of our agricultural products have only a moderate correlation to the anhydrous ammonia and natural gas feedstock costs and reflect market conditions for like and competing nitrogen sources. This can compromise our ability to recover our full cost to produce the product in this market. Additionally, the lack of sufficient non-seasonal sales volume to operate our manufacturing facilities at optimum levels can preclude the Chemical Business from reaching full performance potential. Our primary efforts to improve the results of our Chemical Business include maximizing the production at our chemical facilities and emphasizing our marketing efforts to customers that will accept the volatility risk inherent with natural gas and anhydrous ammonia, while maintaining a strong presence in the agricultural sector.

Introduction of New Product - Chemical Business

As part of the Clean Air Act, the United States Environmental Protection Agency ("EPA") enacted emissions standards, which became effective in 2010, that require the further reduction of nitrogen oxide emissions from diesel engines, starting with heavy-duty vehicles. CNC has developed DEF under the trade name, EarthPure DEFTM, specifically for this application. CNC began production of DEF in January 2010. The production of DEF is currently relatively small as the market is in the early stage of development. We expect this market to grow as the domestic heavy-duty truck fleet is replaced in future years.

Seasonality - Chemical Business

We believe that the only significant seasonal products that we market are fertilizer and related chemical products sold by our Chemical Business to the agricultural industry. The selling seasons for those products are primarily during the spring and fall planting seasons, which typically extend from March through June and from September through November in the geographical markets in which the majority of our agricultural products are distributed. As

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a result, our Chemical Business typically increases its inventory of AN and UAN prior to the beginning of each planting season. In addition, the amount and timing of sales to the agricultural markets depend upon weather conditions and other circumstances beyond our control.

Regulatory Matters - Chemical Business

Our Chemical Business is subject to extensive federal, state and local environmental laws, rules and regulations as discussed under "Environmental Matters" of this Item 1 and various risk factors under Item 1A.

Competition - Chemical Business

Our Chemical Business competes with several chemical companies in our markets, such as Agrium, CF Industries, Dyno Nobel, Koch, Potash Corporation of Saskatchewan, and Yara International, many of whom have greater financial and other resources than we do. We believe that competition within the markets served by our Chemical Business is primarily based upon service, price, location of production and distribution sites, and product quality and performance.

In addition, see discussion concerning potential increase of imported fertilizer grade AN and UAN under Item 1A of this Part 1.

Employees

As of December 31, 2010, we employed 1,780 persons. As of that date, our Climate Control Business employed 1,233 persons, none of whom were represented by a union, and our Chemical Business employed 480 persons, with 148 represented by unions under agreements that expire in July through November of 2013.

Environmental Matters

Our operations are subject to numerous environmental laws ("Environmental Laws") and to other federal, state and local laws regarding health and safety matters ("Health Laws"). In particular, the manufacture and distribution of chemical products are activities which entail environmental risks and impose obligations under the Environmental Laws and the Health Laws, many of which provide for certain performance obligations, substantial fines and criminal sanctions for violations. There can be no assurance that we will not incur material costs or liabilities in complying with such laws or in paying fines or penalties for violation of such laws. The Environmental Laws and Health Laws and enforcement policies thereunder relating to our Chemical Business have in the past resulted, and could in the future result, in compliance expenses, cleanup costs, penalties or other liabilities relating to the handling, manufacture, use, emission, discharge or disposal of effluents at or from our facilities or the use or disposal of certain of its chemical products. Historically, significant expenditures have been incurred by subsidiaries within our Chemical Business in order to comply with the Environmental Laws and Health Laws and are reasonably expected to be incurred in the future.

We are obligated to monitor certain discharge water outlets at our Chemical Business facilities should we discontinue the operations of a facility. We also have certain facilities in our Chemical Business that contain asbestos insulation around certain piping and heated surfaces, which we plan to maintain or replace, as needed, with non-asbestos insulation through our standard repair and maintenance activities to prevent deterioration.

1. Discharge Water Matters

The El Dorado Facility owned by EDC generates process wastewater, which includes cooling tower and boiler blowdowns, contact storm water and miscellaneous spills and leaks from process equipment. The process water

discharge, storm-water runoff and miscellaneous spills and leaks are governed by a state National Pollutant Discharge Elimination System (“NPDES”) discharge water permit issued by the Arkansas Department of Environmental Quality (“ADEQ”), which permit is generally required to be renewed every five years. The El Dorado Facility is currently operating under a NPDES discharge water permit (“2004 NPDES permit”), which became effective in 2004. In November 2010, a preliminary draft of a discharge water permit renewal, which contains more restrictive ammonia limits, was issued by the ADEQ for EDC’s review. EDC submitted comments to

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the ADEQ on the draft permit in December 2010. The preliminary draft is subject to approval by the EPA of the rule change.

The El Dorado Facility has generally demonstrated its ability to comply with applicable ammonia and nitrate permit limits, and believes that if it is required to meet the more restrictive dissolved minerals permit levels, it should be able to do so. However, as part of our long-term compliance plan, EDC is pursuing a rulemaking and permit modification with the ADEQ. The ADEQ approved a rule change, subject to certification by the Arkansas Secretary of State and approval by the EPA. The ADEQ incorporated the revised dissolved minerals limits in the preliminary draft permit received in November 2010.

During January 2010, EDC received an Administrative Order from the EPA noting certain violations of the 2004 NPDES permit and requesting EDC to demonstrate compliance with the permit or provide a plan and schedule for returning to compliance. EDC has provided the EPA a response which states that the El Dorado Facility is now in compliance with the permit, that the El Dorado Facility expects to maintain compliance and that a majority of the alleged violations were resolved through a consent administrative order with the ADEQ. During the meeting with the EPA prior to the issuance of the Administrative Order, the EPA advised EDC that its primary objective was to bring the El Dorado Facility into compliance with the 2004 NPDES permit requirements, but reserved the right to assess penalties for past and continuing violations of the permit. As a result, it is unknown whether the EPA might elect to pursue civil penalties against EDC. Therefore, no liability has been established at December 31, 2010 as a result of the Administrative Order.

In conjunction with our long-term compliance plan, the city of El Dorado, Arkansas received approval to construct a pipeline for disposal of wastewater generated by the city and by certain companies in the El Dorado area. The companies intending to use the pipeline will contribute to the cost of construction and operation of the pipeline. Although EDC believes it can comply with the more restrictive permit limits, EDC intends to participate in the construction of the pipeline that will be owned by the city in order to ensure that EDC will be able to comply with future permit limits. EDC anticipates its cost in connection with the construction of the pipeline for EDC's right to use the pipeline to dispose of its wastewater will be approximately \$4.0 million. The city plans to complete the construction of the pipeline in 2013.

In addition, the El Dorado Facility is currently operating under a consent administrative order ("2006 CAO") that recognizes the presence of nitrate contamination in the shallow groundwater. The 2006 CAO requires EDC to continue semi-annual groundwater monitoring, to continue operation of a groundwater recovery system and to submit a human health and ecological risk assessment to the ADEQ relating to the El Dorado Facility. The final remedy for shallow groundwater contamination, should any remediation be required, will be selected pursuant to a new consent administrative order and based upon the risk assessment. The cost of any additional remediation that may be required will be determined based on the results of the investigation and risk assessment, which costs (or range of costs) cannot currently be reasonably estimated. Therefore, no liability has been established at December 31, 2010, in connection with this matter.

2. Air Matters

The EPA has sent information requests to most, if not all, of the nitric acid plants in the United States, including to us relating to our El Dorado and Cherokee Facilities and the Baytown Facility. The EPA is requesting information under Section 114 of the Clean Air Act as to construction and modification activities at each of these facilities over a period of years to enable the EPA to determine whether these facilities are in compliance with certain provisions of the Clean Air Act. In connection with a review by our Chemical Business of these facilities in obtaining information for the EPA pursuant to the EPA's request, our Chemical Business management believes, subject to further review, investigation and discussion with the EPA, that certain facilities within our Chemical Business may be required to

make certain capital improvements to certain emission equipment in order to comply with the requirements of the Clean Air Act. If changes to the production equipment at these facilities are required in order to bring this equipment into compliance with the Clean Air Act, the type of emission control equipment that might be imposed is unknown and, as a result, the amount of capital expenditures necessary in order to bring the equipment into compliance is unknown at this time but could be substantial.

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Further, if it is determined that the equipment at any of our chemical facilities have not met the requirements of the Clean Air Act, our Chemical Business could be subject to penalties in an amount not to exceed \$27,500 per day as to each facility not in compliance and be required to retrofit each facility with the “best available control technology.” We are currently unable to determine the amount (or range of amounts) of any penalties that may be assessed by the EPA. Therefore no liability has been established at December 31, 2010, in connection with this matter.

3. Other Environmental Matters

In December 2002, two subsidiaries within our Chemical Business, sold substantially all of their operating assets relating to a Kansas chemical facility (“Hallowell Facility”) but retained ownership of the real property. At December 31, 2002, even though we continued to own the real property, we did not assess our continuing involvement with our former Hallowell Facility to be significant and therefore accounted for the sale as discontinued operations. In connection with this sale, our subsidiary leased the real property to the buyer under a triple net long-term lease agreement. However, our subsidiary retained the obligation to be responsible for, and perform the activities under, a previously executed consent order to investigate the surface and subsurface contamination at the real property and a corrective action strategy based on the investigation. In addition, certain of our subsidiaries agreed to indemnify the buyer of such assets for these environmental matters. The successor (“Chevron”) of a prior owner of the Hallowell Facility has agreed in writing, within certain limitations, to pay and has been paying one-half of the costs of the interim measures relating to this matter as approved by the Kansas Department of Environmental Quality, subject to reallocation.

Our subsidiary and Chevron are pursuing a course with the state of Kansas of long-term surface and groundwater monitoring to track the natural decline in contamination. Currently, our subsidiary and Chevron are in the process of performing additional surface and groundwater testing. We have accrued for our allocable portion of costs for the additional testing, monitoring and risk assessments that could be reasonably estimated. The ultimate required remediation, if any, is unknown.

In addition, the Kansas Department of Health and Environment (“KDHE”) notified our subsidiary and Chevron that this site has been referred to the KDHE’s Natural Resources Trustee, who is to consider and recommend restoration, replacement and/or whether to seek compensation. KDHE will consider the recommendations in their evaluation. Currently, it is unknown what damages, if any, the KDHE will claim. The nature and extent of a portion of the requirements are not currently defined and the associated costs (or range of costs) are not reasonably estimable.

At December 31, 2010, our estimated allocable portion of the total estimated liability (which is included in current accrued and other liabilities) related to the Hallowell Facility is \$178,000. The estimated amount is not discounted to its present value. It is reasonably possible that a change in the estimate of our liability could occur in the near term.

During 2010, EDC became aware that certain personnel at its Whitewright, Texas agricultural distribution site, which personnel had been previously terminated by EDC, disposed of chemicals and debris at the site without authorization. Upon learning of these acts by the former employees, EDC contracted with an environmental company to analyze the areas of such disposal and dispose of any chemicals and contaminated soils. Upon completion of testing, it was determined that the area contained contaminants above state action levels. As a result, EDC notified the appropriate authorities in the state of Texas of the contamination. EDC has installed numerous monitoring wells in coordination with the state. We have incurred costs totaling \$208,000 associated with this project, which includes an estimated \$50,000 in current accrued and other liabilities at December 31, 2010. The estimated amount is not discounted to its present value. It is reasonably possible that a change in the estimate of our liability could occur in the near term.

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ITEM 1A. RISK FACTORS

Risks Related to Us and Our Business

Our Climate Control and Chemical Businesses and their customers are sensitive to adverse economic cycles.

Our Climate Control Business can be affected by cyclical factors, such as interest rates, inflation and economic downturns. Our Climate Control Business depends on sales to customers in the construction and renovation industries, which are particularly sensitive to these factors. Due to the recession, we have experienced and could continue to experience a decline in both commercial/institutional and residential construction and, therefore, demand for our Climate Control Business products. A decline in the economic activity in the United States has in the past, and could in the future, have a material adverse effect on us and our customers in the construction and renovation industries in which our Climate Control Business sells a substantial amount of its products. Such a decline could result in a decrease in revenues and profits, and an increase in bad debts, in our Climate Control Business and could have a material adverse effect on our operating results, financial condition and liquidity.

Our Chemical Business also can be affected by cyclical factors such as inflation, global energy policy and costs, global market conditions and economic downturns in specific industries. Certain sales of our Chemical Business are sensitive to the level of activity in the agricultural, mining, automotive and housing industries. A substantial decline in the activity of our Chemical Business has in the past, and could in the future, have a material adverse effect on the results of our Chemical Business and on our liquidity and capital resources.

Weather conditions adversely affect our Chemical Business.

The agricultural products produced and sold by our Chemical Business have in the past, and could in the future, be materially affected by adverse weather conditions (such as excessive rains or drought) in the primary markets for our fertilizer and related agricultural products. If any of these unusual weather events occur during the primary seasons for sales of our agricultural products (March-June and September-November), this could have a material adverse effect on the agricultural sales of our Chemical Business and our financial condition and results of operations.

Terrorist attacks and other acts of violence or war, and natural disasters (such as hurricanes, pandemic health crisis, etc.), have and could negatively impact U.S. and foreign companies, the financial markets, the industries where we operate, our operations and profitability.

Terrorist attacks and natural disasters (such as hurricanes) have in the past, and can in the future, negatively affect our operations. We cannot predict further terrorist attacks and natural disasters in the U.S. and elsewhere. These attacks or natural disasters have contributed to economic instability in the U.S. and elsewhere, and further acts of terrorism, violence, war or natural disasters could further affect the industries where we operate, our ability to purchase raw materials, our business, results of operations and financial condition. In addition, terrorist attacks and natural disasters may directly impact our physical facilities, especially our chemical facilities, or those of our suppliers or customers and could impact our sales, our production capability and our ability to deliver products to our customers. In the past, hurricanes affecting the Gulf Coast of the U.S. have negatively impacted our operations and those of our customers. The consequences of any terrorist attacks or hostilities or natural disasters are unpredictable, and we may not be able to foresee events that could have an adverse effect on our operations.

Environmental and regulatory matters entail significant risk for us.

Our businesses are subject to numerous environmental laws and regulations, primarily relating to our Chemical Business. The manufacture and distribution of chemical products are activities, which entail environmental risks and

impose obligations under environmental laws and regulations, many of which provide for substantial fines and potential criminal sanctions for violations. Although we have established processes to monitor, review and manage our businesses to comply with the numerous environmental laws and regulations, our Chemical Business has in the past, and may in the future, be subject to fines, penalties and sanctions for violations and substantial expenditures for cleanup costs and other liabilities relating to the handling, manufacture, use, emission, discharge or disposal of effluents at or from the Chemical Business' facilities. Further, a number of our Chemical Business' facilities are dependent on environmental permits to operate, the loss or modification of which could have a material adverse effect on their operations and our financial condition.

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If changes to the production equipment at our chemical facilities are required in order to comply with environmental regulations, the amount of capital expenditures necessary to bring the equipment into compliance is unknown at this time and could be substantial.

We may be required to expand our security procedures and install additional security equipment for our Chemical Business in order to comply with current and possible future government regulations, including the Homeland Security Act of 2002.

The chemical industry in general, and producers and distributors of anhydrous ammonia and AN specifically, are scrutinized by the government, industry and public on security issues. Under current and proposed regulations, including the Homeland Security Act of 2002, we may be required to incur substantial additional costs relating to security at our chemical facilities and distribution centers, as well as in the transportation of our products. These costs could have a material impact on our financial condition, results of operations, and liquidity. The cost of such regulatory changes, if significant enough, could lead some of our customers to choose alternate products to anhydrous ammonia and AN, which would have a significant impact on our Chemical Business.

Proposed governmental laws and regulations relating to greenhouse gas emissions may subject certain of our Chemical Business' facilities to significant new costs and restrictions on their operations.

The manufacturing facilities within our Chemical Business use significant amounts of electricity, natural gas and other raw materials necessary for the production of their chemical products that result, or could result, in certain greenhouse gas emissions into the environment. Federal and state courts and administrative agencies, including the EPA, are considering the scope and scale of greenhouse gas emission regulation. There are bills pending or that have been proposed in Congress that would regulate greenhouse gas emissions through a cap-and-trade system under which emitters would be required to either install abatement systems where feasible or buy allowances for offsets of emissions of greenhouse gas. The EPA has instituted a mandatory greenhouse gas reporting requirement that began in 2010, which impacts all of our chemical manufacturing sites. Greenhouse gas regulation could increase the price of the electricity and other energy sources purchased by our chemical facilities; increase costs for natural gas and other raw materials (such as anhydrous ammonia); potentially restrict access to or the use of certain raw materials necessary to produce our chemical products; and require us to incur substantial expenditures to retrofit our chemical facilities to comply with the proposed new laws and regulations regulating greenhouse gas emissions, if adopted. Federal, state and local governments may also pass laws mandating the use of alternative energy sources, such as wind power and solar energy, which may increase the cost of energy use in certain of our chemical and other manufacturing operations. While future emission regulations or new laws appear possible, it is too early to predict how these regulations, if and when adopted, will affect our businesses, operations, liquidity or financial results.

There is intense competition in the Climate Control and Chemical industries.

Substantially all of the markets in which we participate are highly competitive with respect to product quality, price, design innovations, distribution, service, warranties, reliability and efficiency. We compete with a number of companies that have greater financial, marketing and other resources. Competitive factors could require us to reduce prices or increase spending on product development, marketing and sales that would have a material adverse effect on our business, results of operation and financial condition.

A substantial portion of our sales is dependent upon a limited number of customers.

For 2010, five customers of our Chemical Business accounted for approximately 45% of its net sales and 26% of our consolidated sales, and our Climate Control Business had three customers (including affiliates and their distributors) that accounted for approximately 24% of its net sales and 10% of our consolidated sales. The loss of, or a material

reduction in purchase levels by, one or more of these customers could have a material adverse effect on our business and our results of operations, financial condition and liquidity if we are unable to replace a customer on substantially similar terms.

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Cost and the lack of availability of raw materials could materially affect our profitability and liquidity.

Our sales and profits are heavily affected by the costs and availability of primary raw materials. These primary raw materials, which are purchased from unrelated third parties, are subject to considerable price volatility. Historically, when there have been rapid increases in the cost of these primary raw materials, we have sometimes been unable to timely increase our sales prices to cover all of the higher costs incurred. While we periodically enter into futures/forward contracts to economically hedge against price increases in certain of these raw materials, there can be no assurance that we will effectively manage against price fluctuations in those raw materials.

Anhydrous ammonia, natural gas and sulfur represent the primary raw material feedstocks in the production of most of the products of the Chemical Business. Although our Chemical Business has a program to enter into contracts with certain customers that provide for the pass-through of raw material costs, we have a substantial amount of sales that do not provide for the pass-through of raw material costs. In addition, the Climate Control Business depends on raw materials such as copper and steel, which have shown considerable price volatility. As a result, in the future, we may not be able to pass along to all of our customers the full amount of any increases in raw material costs. There can be no assurance that future price fluctuations in our raw materials will not have an adverse effect on our financial condition, liquidity and results of operations.

Since we source certain of our raw materials and components on a global basis, we may experience long lead times in procuring those raw materials and components purchased overseas, as well as being subject to tariff controls and other international trade barriers, which may increase the uncertainty of raw material and component availability and pricing volatility.

Additionally, we depend on certain vendors to deliver the primary raw materials and other key components that are required in the production of our products. Any disruption in the supply of the primary raw materials and other key components could result in lost production or delayed shipments. We have suspended in the past, and could suspend in the future, production at our chemical facilities due to, among other things, the high cost or lack of availability of such primary raw materials, which could adversely impact our competitiveness in the markets we serve. Accordingly, our financial condition, liquidity and results of operations could be materially affected in the future by the lack of availability of primary raw materials and other key components.

Potential increase of imported ammonium nitrate from Russia.

In 2000, the U.S. and Russia entered into a suspension agreement limiting the quantity of, and setting the minimum prices for, fertilizer grade AN sold from Russia into the U.S.

The Russians have requested that the suspension agreement be changed to only require that the prices of its imported AN reflect the Russian producers full production costs, plus profit. The Russian producers of AN could benefit from state set prices of natural gas, the principal raw material for AN, which could be less than what U.S. producers are required to pay for their natural gas. Other factors, however, such as transportation costs may partially offset natural gas and production cost advantages. This change, if accepted by the U.S., could result in a substantial increase in the amount of AN imported into the U.S. from Russia at prices that could be less than the cost to produce AN by U.S. producers plus a profit. Russia is the world's largest producer of fertilizer grade AN, and we are led to believe that it has substantial excess AN production capacity.

For 2010, net sales of fertilizer grade AN accounted for 16% and 9% of our Chemical Business net sales and consolidated net sales, respectively. If the suspension agreement is changed, as discussed above, this change could result in Russia substantially increasing the amount of AN sold in the U.S. at prices less than the U.S. producers are required to charge in order to cover their cost plus a profit, and could have an adverse effect on our revenues and

operating results.

Potential increase of imported urea ammonium nitrate (UAN).

A large percentage of the domestic UAN market is supplied by imports. Significant additional UAN production began in the Caribbean during 2010, and we believe that some of this additional UAN production could be marketed in the U.S. Generally, foreign production of UAN is produced at a lower cost than UAN produced in the U.S., and

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could have an adverse impact on the domestic UAN market, and the domestic fertilizer market in general, including the UAN and fertilizer markets of our Chemical Business, by foreign producers increasing supply and possibly reducing prices.

For 2010, net sales of UAN accounted for 11% and 6% of our Chemical Business net sales and consolidated net sales, respectively. Additionally, UAN is the primary product to be produced and sold by the Pryor Facility. This potential additional import of UAN could have an adverse impact on our revenues and operating results.

Our previously idled Pryor Facility has a limited operating history.

The Pryor Facility reached sustained production of anhydrous ammonia in the fourth quarter of 2010. The nitric acid, neutralizer, and urea plants at the Pryor Facility were reactivated to produce UAN. However, our ability to operate the Pryor Facility for extended periods is unknown due to our limited operating history at this facility.

Our previously utilized net operating loss carryforwards are subject to certain limitations and examination.

We had generated significant net operating loss (“NOL”) carryforwards from certain historical losses. During recent years, we have utilized all of the remaining federal NOL carryforwards and a portion of our state NOL carryforwards. The utilization of these NOL carryforwards has reduced our income tax liabilities. The federal tax returns for 1999 through 2006 remain subject to examination for the purpose of determining the amount of remaining tax NOL and other carryforwards. With few exceptions, the 2007-2009 years remain open for all purposes of examination by the U.S. Internal Revenue Service (“IRS”) and other major tax jurisdictions. During 2011, we were notified that we will be under examination by the IRS and certain state tax authorities for the tax years 2007-2009.

We may have inadequate insurance.

While we maintain liability insurance, including certain coverage for environmental contamination, it is subject to coverage limits and policies may exclude coverage for some types of damages (which may include warranty and product liability claims). Although there may currently be sources from which such coverage may be obtained, it may not continue to be available to us on commercially reasonable terms or the possible types of liabilities that may be incurred by us may not be covered by our insurance. In addition, our insurance carriers may not be able to meet their obligations under the policies or the dollar amount of the liabilities may exceed our policy limits. Even a partially uninsured claim, if successful and of significant magnitude, could have a material adverse effect on our business, results of operations, financial condition and liquidity.

LSB is a holding company and depends, in large part, on receiving funds from its subsidiaries to fund our indebtedness.

Because LSB is a holding company and operations are conducted through its subsidiaries, including ThermaClime, LLC (“ThermaClime”) and its subsidiaries, LSB’s ability to make scheduled payments of principal and interest on its indebtedness depends, in large part, on the operating performance and cash flows of its subsidiaries and the ability of its subsidiaries to make distributions and pay dividends to LSB. Under its loan agreements, ThermaClime and its subsidiaries may only make distributions and pay dividends to LSB under limited circumstances and in limited amounts.

Loss of key personnel could negatively affect our business.

We believe that our performance has been and will continue to be dependent upon the efforts of our principal executive officers. We cannot promise that our principal executive officers will continue to be available. Jack E.

Golsen has an employment agreement with us. No other principal executive has an employment agreement with us. The loss of some of our principal executive officers could have a material adverse effect on us. We believe that our future success will depend in large part on our continued ability to attract and retain highly skilled and qualified personnel.

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We are effectively controlled by the Golsen Group.

Jack E. Golsen, our Chairman of the Board and Chief Executive Officer (“CEO”), members of his immediate family (spouse and children), including Barry H. Golsen, our Vice Chairman and President, entities owned by them and trusts for which they possess voting or dispositive power as trustee (collectively, the “Golsen Group”) owned as of February 28, 2011, an aggregate of 3,506,093 shares of our common stock and 1,020,000 shares of our voting preferred stock (1,000,000 of which shares have .875 votes per share, or 875,000 votes), which together votes as a class and represents approximately 20% of the voting power of our issued and outstanding voting securities as of that date. In addition, the Golsen Group also beneficially owned options and other convertible securities that allowed its members to acquire an additional 197,250 shares of our common stock within 60 days of February 28, 2011. Thus, the Golsen Group may be considered to effectively control us. As a result, the ability of other stockholders to influence our management and policies could be limited.

We have not paid dividends on our outstanding common stock in many years.

Although we have paid dividends on our outstanding series of preferred stock (two of the three outstanding series of preferred stock are owned by the Golsen Group), we have not paid cash dividends on our outstanding common stock in many years, and we do not currently anticipate paying cash dividends on our outstanding common stock in the near future. However, our board of directors has not made a decision whether or not to pay such dividends on our common stock in 2011. In addition, there are certain limitations contained in our loan agreements, which limit our subsidiaries from up streaming funds to LSB that may limit our ability to pay dividends on our outstanding common stock.

Future issuance or potential issuance of our common stock could adversely affect the price of our common stock, our ability to raise funds in new stock offerings and could dilute the percentage ownership of our common stockholders.

Future sales of substantial amounts of our common stock or equity-related securities in the public market, or the perception that such sales could occur, could adversely affect prevailing trading prices of our common stock and could impair our ability to raise capital through future offerings of equity or equity-related securities. No prediction can be made as to the effect, if any, that future sales of shares of common stock or the availability of shares of common stock for future sale will have on the trading price of our common stock. Such future sales could also significantly reduce the percentage ownership of our common stockholders.

We are subject to a variety of factors that could discourage other parties from attempting to acquire us.

Our certificate of incorporation provides for a staggered board of directors and, except in limited circumstances, a two-thirds vote of outstanding voting shares to approve a merger, consolidation or sale of all, or substantially all, of our assets. In addition, we have entered into severance agreements with our executive officers and some of the executive officers of certain subsidiaries that provide, among other things, that if, within a specified period of time after the occurrence of a change in control of LSB, these officers are terminated, other than for cause, or the officer terminates his employment for good reason, we must pay such officer an amount equal to 2.9 times the officer’s average annual gross salary for the last five years preceding the change in control.

We have authorized and unissued (including shares held in treasury) 53,843,928 shares of common stock and 4,229,526 shares of preferred stock as of December 31, 2010. These unissued shares could be used by our management to make it more difficult, and thereby discourage an attempt to acquire control of us.

We have adopted a preferred share purchase plan, which is designed to protect us against certain creeping acquisitions, open market purchases and certain mergers and other combinations with acquiring companies.

The foregoing provisions and agreements are designed to discourage a third party tender offer, proxy contest, or other attempts to acquire control of us and could have the effect of making it more difficult to remove incumbent management.

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Delaware has adopted an anti-takeover law which, among other things, will delay for three years business combinations with acquirers of 15% or more of the outstanding voting stock of publicly-held companies (such as us), unless;

- prior to such time the board of directors of the corporation approved the business combination that results in the stockholder becoming an invested stockholder;
- the acquirer owned at least 85% of the outstanding voting stock of such company prior to commencement of the transaction;
- two-thirds of the stockholders, other than the acquirer, vote to approve the business combination after approval thereof by the board of directors; or
- the stockholders of the corporation amends its articles of incorporation or by-laws electing not to be governed by this provision.

ITEM 1B. UNRESOLVED STAFF COMMENTS

Not applicable.

ITEM 2. PROPERTIES

Climate Control Business

Our Climate Control Business manufactures most of its geothermal and water source heat pump products in a 340,000 square foot facility in Oklahoma City, Oklahoma. During 2010, we exercised an option, pursuant to the terms of the underlying operating lease, to purchase a portion of this facility. As a result, we own this facility, subject to a mortgage. For 2010, we utilized approximately 60% of the productive capacity of this manufacturing facility, based primarily on two ten-hour shifts per day and a four-day workweek. In addition, we own a 46,000 square foot building, subject to a mortgage, which is adjacent to this manufacturing facility, primarily used for storage of raw material and component inventory. We also utilize approximately 110,000 square feet of an existing facility for a distribution center, which facility we own, subject to a mortgage.

Our Climate Control Business conducts its fan coil manufacturing operation in a facility located in Oklahoma City, Oklahoma, consisting of approximately 265,000 square feet. We own this facility, subject to a mortgage. For 2010, our fan coil manufacturing operation utilized approximately 44% of the productive capacity, based primarily on one ten-hour shift per day and a four-day workweek.

Our Climate Control Business conducts its large air handler manufacturing operation in a facility located in Oklahoma City, Oklahoma, consisting of approximately 110,000 square feet. We own this facility subject to a mortgage. For 2010, we utilized approximately 84% of the productive capacity of this manufacturing facility, based primarily on a one eight-hour shift on a five-day workweek and a partial second shift in selected areas.

The modular chiller manufacturing operation of the Climate Control Business is in the process of establishing separate production facilities within Oklahoma City in order to increase production capacity and accommodate potential sales volume increases expected due to new products currently under development. Currently, modular chillers are being produced in our geothermal and water source heat pump manufacturing facility. The new production facility will occupy approximately 70,000 square feet in an existing facility owned by us, subject to a mortgage. The expected date for completing this transition is during the second quarter of 2011.

All of the properties utilized by our Climate Control Business are suitable to meet the current needs of that business.

Chemical Business

Our Chemical Business primarily conducts manufacturing operations in facilities located:

- on 150 acres of a 1,400 acre tract of land in El Dorado, Arkansas,
- on 160 acres of a 1,300 acre tract of land in Cherokee, Alabama,
- on property within Bayer's complex in the Baytown, Texas, and
 - on 58 acres in an industrial park in Pryor, Oklahoma.

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We own all of these manufacturing facilities except the Baytown Facility. Except for certain assets that are owned by El Dorado Nitric Company and its subsidiaries (“EDN”) for use in the production process within the Baytown Facility, the Baytown Facility is owned by Bayer. EDN operates and maintains the Baytown Facility pursuant to the Bayer Agreement. Certain real property and equipment located at the El Dorado and Cherokee Facilities are being used to secure a \$50 million term loan. For 2010, the following facilities were utilized based on continuous operation, which is adjusted for downtime for planned major maintenance activities (“Turnarounds”).

	Percentage of Capacity
El Dorado Facility (1)	81 %
Cherokee Facility (2)	99 %
Baytown Facility	88 %
Pryor Facility (3)	n/a

(1) The percentage of capacity for the El Dorado Facility relates to its nitric acid capacity. The El Dorado Facility has capacity to produce other nitrogen products in excess of its nitric acid capacity.

(2) The percentage of capacity for the Cherokee Facility relates to its ammonia production capacity. The Cherokee Facility is able to purchase anhydrous ammonia by truck, rail or barge to supplement its ammonia production capacity. The Cherokee Facility has additional capacity for nitric acid, AN and UAN in excess of its ammonia capacity.

(3) As discussed, our previously idled Pryor Facility did not reach sustained production until the fourth quarter of 2010. As a result, the capacity utilized was minimal. We expect to be able to report the percentage of capacity in 2011.

In addition to the El Dorado and Cherokee Facilities, our Chemical Business distributes its agricultural products through 15 wholesale and retail distribution centers, with 13 of the centers located in Texas (10 of which we own and 3 of which we lease); 1 center located in Tennessee (owned); and 1 center located in Missouri (owned).

All of the properties utilized by our Chemical Business are suitable and adequate to meet the current needs of that business.

ITEM 3. LEGAL PROCEEDINGS

1. Environmental See “Business-Environmental Matters” for a discussion as to:

- certain environmental matters relating to water and air issues at our El Dorado Facility;
- certain environmental remediation matters at our former Hallowell Facility; and
- certain environmental matters at one of our agricultural distribution centers.

2. Other

The Jayhawk Group

In November 2006, we entered into an agreement with Jayhawk Capital Management, LLC, Jayhawk Investments, L.P., Jayhawk Institutional Partners, L.P. and Kent McCarthy, the manager and sole member of Jayhawk Capital, (collectively, the “Jayhawk Group”), in which the Jayhawk Group agreed, among other things, that if we undertook, in our sole discretion, within one year from the date of agreement a tender offer for our Series 2 \$3.25 convertible exchangeable Class C preferred stock (“Series 2 Preferred”) or to issue our common stock for a portion of our Series 2 Preferred pursuant to a private exchange, that they would tender or exchange an aggregate of no more than 180,450 shares of the 340,900 shares of the Series 2 Preferred beneficially owned by the Jayhawk Group, subject to, among

other things, the entities owned and controlled by Jack E. Golsen, our Chairman and Chief Executive Officer (“Golsen”), and his immediate family, that beneficially own Series 2 Preferred only being able to exchange or tender approximately the same percentage of shares of Series 2 Preferred beneficially owned by them as the Jayhawk Group was able to tender or exchange under the terms of the agreement.

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During 2007, we made a tender offer for our outstanding Series 2 Preferred at the rate of 7.4 shares of our common stock for each share of Series 2 Preferred so tendered. In July 2007, we redeemed the balance of our outstanding shares of Series 2 Preferred. Pursuant to its terms, the Series 2 Preferred was convertible into 4.329 shares of our common stock for each share of Series 2 Preferred. As a result of the redemption, the Jayhawk Group converted the balance of its Series 2 Preferred pursuant to the terms of the Series 2 Preferred in lieu of having its shares redeemed.

The Jayhawk Group has filed suit against us and Golsen alleging that the Jayhawk Group should have been able to tender all of its Series 2 Preferred pursuant to the tender offer, notwithstanding the above-described agreement, based on the following claims against us and Golsen:

- fraudulent inducement and fraud,
- violation of 10(b) of the Exchange Act and Rule 10b-5,
- violation of 17-12A501 of the Kansas Uniform Securities Act, and
- breach of contract.

The Jayhawk Group seeks damages up to \$12 million based on the additional number of common shares it allegedly would have received on conversion of all of its Series 2 Preferred through the February 2007 tender offer, plus punitive damages. In May 2008, the General Counsel for the Jayhawk Group offered to settle its claims against us and Golsen in return for a payment of \$100,000, representing the approximate legal fees it had incurred investigating the claims at that time. Through counsel, we verbally agreed to the settlement offer and confirmed the agreement by e-mail. Afterward, the Jayhawk Group's General Counsel purported to withdraw the settlement offer, and asserted that Jayhawk is not bound by any settlement agreement. We contend that the settlement agreement is binding on the Jayhawk Group. We intend to contest the lawsuit vigorously, and have asserted that Jayhawk is bound by an agreement to settle the claims for \$100,000. Our insurer, Chartis, a subsidiary of AIG, has agreed to defend this lawsuit on our behalf and on behalf of Golsen and to indemnify under a reservation of rights to deny liability under certain conditions. We have incurred expenses associated with this matter up to our insurance deductible of \$250,000, and our insurer is paying defense cost in excess of our deductible in this matter. Although our insurer is defending this matter under a reservation of rights, we are not currently aware of any material issue in this case that would result in our insurer denying coverage. Therefore, no liability has been established at December 31, 2010 as a result of this matter.

Other Claims and Legal Actions

We are also involved in various other claims and legal actions including product liability claims for damages related to our Climate Control products. Most of the product liability claims are covered by our general liability insurance, which generally includes a deductible of \$250,000 per claim. For any claims or legal actions that we have assessed the likelihood of our liability as probable, we have recognized our estimated liability up to the applicable deductible. At December 31, 2010, our accrued general liability insurance claims were \$1,230,000 and are included in accrued and other liabilities. It is reasonably possible that the actual development of claims could exceed our estimates but, after consultation with legal counsel, if those general liability insurance claims for which we have not recognized a liability were determined adversely to us, it would not have a material effect on our business, financial condition or results of operations.

ITEM 4. [Reserved]

EXECUTIVE OFFICERS OF THE REGISTRANT

Our officers serve one-year terms, renewable on an annual basis by the board of directors. Information regarding LSB's executive officers is as follows:

Jack E. Golsen (1) - Chairman of the Board and Chief Executive Officer. Mr. Golsen, age 82 first became a director in 1969. His term will expire in 2013. Mr. Golsen, founder of LSB, is our Chairman of the Board of Directors and Chief Executive Officer and has served in those capacities since our inception in 1969. Mr. Golsen served as our President from 1969 until 2004. During 1996, he was inducted into the Oklahoma Commerce and Industry Hall of Honor as one of Oklahoma's leading industrialists. Mr. Golsen has a Bachelor of Science degree

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from the University of New Mexico. Mr. Golsen is a Trustee of Oklahoma City University and has served on its Finance Committee for many years. During his career, he acquired or started the companies which formed the Company. He has served on the boards of insurance companies, several banks and was Board Chairman of Equity Bank for Savings N.A. which was formerly owned by the Company. In 1972, he was recognized nationally as the person who prevented a widespread collapse of the Wall Street investment banking industry. Refer to “The Second Crash” by Charles Ellis, and six additional books about the Wall Street crisis.

Barry H. Golsen, J.D. (1) - Vice Chairman of the Board, President, and President of the Climate Control Business. Mr. Golsen, age 60, first became a director in 1981. His term will expire in 2012. Mr. Golsen was elected President of LSB in 2004. Mr. Golsen has served as our Vice Chairman of the Board of Directors since August 1994. Mr. Golsen has served in several capacities with various LSB subsidiary companies and has been the President of our Climate Control Business for more than ten years. Mr. Golsen served as a director of the Oklahoma branch of the Federal Reserve Bank. Mr. Golsen has both his undergraduate and law degrees from the University of Oklahoma.

David R. Goss - Executive Vice President of Operations and Director. Mr. Goss, age 70, first became a director in 1971. His term will expire in 2012. Mr. Goss, a certified public accountant, is our Executive Vice President of Operations and has served in substantially the same capacity for more than ten years. Mr. Goss is a graduate of Rutgers University.

Tony M. Shelby - Executive Vice President of Finance and Director. Mr. Shelby, age 69, first became a director in 1971. His term will expire in 2011. Mr. Shelby, a certified public accountant, is our Executive Vice President of Finance and Chief Financial Officer, a position he has held for more than ten years. Prior to becoming our Executive Vice President of Finance and Chief Financial Officer, he served as Chief Financial Officer of a subsidiary of LSB and was with the accounting firm of Arthur Young & Co., a predecessor to Ernst & Young LLP. Mr. Shelby is a graduate of Oklahoma City University.

Steven J. Golsen (1) - Chief Operating Officer of the Climate Control Business. Mr. Golsen, age 58, has been nominated to stand for election as a director at our 2011 Annual Meeting of Stockholders. If elected, his term will expire in 2014. Mr. Golsen attended the University of New Mexico and University of Oklahoma. Mr. Golsen has been employed by the Company since 1976. Mr. Golsen has served as Chief Operating Officer of our Machine Tool and Specialized Engineering Business and Climate Control Business for more than ten years.

Jim D. Jones (2) - Senior Vice President and Treasurer. Mr. Jones, age 68, has been Senior Vice President and Treasurer since July 2003, and has served as an officer of LSB since April 1977. Mr. Jones is a certified public accountant and was with the accounting firm of Arthur Young & Co., a predecessor to Ernst & Young LLP. Mr. Jones is a graduate of the University of Central Oklahoma.

David M. Shear (1) - Senior Vice President and General Counsel. Mr. Shear, age 51, has been Senior Vice President and General Counsel since July 2004 and General Counsel and Secretary since 1990. Mr. Shear attended Brandeis University, graduating cum laude in 1981. At Brandeis University, Mr. Shear was the founding Editor-In-Chief of Chronos, the first journal of undergraduate scholarly articles. Mr. Shear attended the Boston University School of Law, where he was a contributing Editor of the Annual Review of Banking Law. Mr. Shear acted as a staff attorney at the Bureau of Competition with the Federal Trade Commission from 1985 to 1986. From 1986 through 1989, Mr. Shear was an associate in the Boston law firm of Weiss, Angoff, Coltin, Koski and Wolf.

Michael D. Tepper – Senior Vice President of International Operations. Mr. Tepper, age 72, has served in substantially the same capacity for more than ten years. Mr. Tepper is a graduate of the Wharton School of the University of Pennsylvania.

Michael G. Adams - Vice President and Corporate Controller. Mr. Adams, age 61, has been Vice President and Corporate Controller since 2008 and has served as an officer of LSB since March 1990. Mr. Adams is a certified public accountant and was with the accounting firm of Arthur Young & Co., a predecessor to Ernst & Young LLP. Mr. Adams is a graduate of the University of Oklahoma.

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Harold L. Rieker Jr. - Vice President and Principal Accounting Officer. Mr. Rieker, age 50, has been Vice President and Principal Accounting Officer since 2008 and has served as an officer of LSB since March 2006. Mr. Rieker is a certified public accountant and was with the accounting firm of Grant Thornton LLP. Mr. Rieker is a graduate of the University of Central Oklahoma.

(1) Barry H. Golsen and Steven J. Golsen are the sons of Jack E. Golsen and David M. Shear is married to the niece of Jack E. Golsen.

(2) The Company and Mr. Jones entered into a settlement order with the SEC, which resulted in Mr. Jones entering into an agreement with the Oklahoma Accounting Board placing him on probation through July 2011. Under the order with the SEC, the Company and Mr. Jones agreed, without admitting or denying any wrongdoing, not to commit violations of certain provisions of the Securities Exchange Act of 1934, as amended. Mr. Jones also consented not to appear before the SEC as an accountant, but can apply for reinstatement at any time after July 2011.

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PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Market Information

Our common stock is trading on the New York Stock Exchange under the symbol "LXU". The following table shows, for the periods indicated, the high and low sales prices.

Quarter	Year Ended December 31,			
	2010		2009	
	High	Low	High	Low
First	\$15.99	\$12.61	\$10.87	\$6.62
Second	\$19.96	\$13.23	\$18.16	\$9.67
Third	\$18.99	\$12.71	\$18.31	\$14.85
Fourth	\$24.58	\$18.60	\$15.70	\$10.62

Stockholders

As of February 28, 2011, we had 612 record holders of our common stock. This number does not include investors whose ownership is recorded in the name of their brokerage company.

Dividends

See discussion concerning dividends below under "Liquidity and Capital Resources - Dividends" of Item 7 contained in this report.

Equity Compensation Plans

See discussions relating to our equity compensation plans under Item 12 of Part III contained in this report.

Sale of Unregistered Securities

During the three months ended December 31, 2010, we issued the following unregistered equity securities:

In December 2010, we issued 900 shares of common stock upon the holder's conversion of 22.5 shares of our noncumulative redeemable preferred stock ("Noncumulative Preferred"). Pursuant to the terms of the Noncumulative Preferred, the conversion rate was 40 shares of common stock for each share of Noncumulative Preferred. The common stock was issued pursuant to the exemption from the registration of securities afforded by Section 3(a)(9) of the Securities Act. No commissions or other remuneration was paid for this issuance. We did not receive any proceeds upon the conversion of the Noncumulative Preferred.

Purchases of Equity Securities by the Issuer and Affiliated Purchasers

During the three months ended December 2010, there were no purchases of equity securities by the Company and affiliated purchasers.

Preferred Share Rights Plan

We have adopted a preferred share rights plan, which is designed to protect us against certain creeping acquisitions, open market purchases and certain mergers and other combinations with acquiring companies. See Note 16 of the Notes to Consolidated Financial Statements included in this report as to discussion relating to the terms of the preferred share rights plan.

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ITEM 6. SELECTED FINANCIAL DATA (1)

	Year ended December 31,				
	2010	2009	2008	2007	2006
(Dollars In Thousands, Except Per Share Data)					
Selected Statement of Income Data:					
Net sales	\$ 609,905	\$ 531,838	\$ 748,967	\$ 586,407	\$ 491,952
Interest expense	\$ 7,427	\$ 6,746	\$ 11,381	\$ 12,078	\$ 11,915
Provisions for income taxes (2)	\$ 19,787	\$ 15,024	\$ 18,776	\$ 2,540	\$ 901
Income from continuing operations	\$ 29,715	\$ 21,849	\$ 36,560	\$ 46,534	\$ 15,768
Net income	\$ 29,574	\$ 21,584	\$ 36,547	\$ 46,882	\$ 15,515
Net income applicable to common stock	\$ 29,269	\$ 21,278	\$ 36,241	\$ 41,274	\$ 12,885
Income (loss) per common share applicable to common stock:					
Basic:					
Income from continuing operations	\$ 1.39	\$ 1.01	\$ 1.71	\$ 2.09	\$.92
Net income (loss) from discontinued operations	\$ (.01)	\$ (.01)	\$ -	\$.02	\$ (.02)
Net income	\$ 1.38	\$ 1.00	\$ 1.71	\$ 2.11	\$.90
Diluted:					
Income from continuing operations	\$ 1.33	\$.97	\$ 1.58	\$ 1.82	\$.77
Net income (loss) from discontinued operations	\$ (.01)	\$ (.01)	\$ -	\$.02	\$ (.01)
Net income	\$ 1.32	\$.96	\$ 1.58	\$ 1.84	\$.76
Selected Balance Sheet Data:					
Total assets	\$ 387,981	\$ 338,633	\$ 335,767	\$ 307,554	\$ 219,927
Redeemable preferred stock	\$ 45	\$ 48	\$ 52	\$ 56	\$ 65
Long-term debt, including current portion	\$ 95,392	\$ 101,801	\$ 105,160	\$ 122,107	\$ 97,692
Stockholders' equity	\$ 179,370	\$ 150,607	\$ 130,044	\$ 94,283	\$ 43,634
Selected other data:					
Cash dividends declared per common share	\$ -	\$ -	\$ -	\$ -	\$ -

(1) See discussions included in Item 7 of Part II of this report.

(2) Beginning in the fourth quarter of 2007, we began recognizing a provision for regular federal income taxes as the result of reversing the valuation allowance on federal NOL carryforwards and other timing differences and the associated utilization of the federal NOL carryforwards.

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ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") should be read in conjunction with a review of the other Items included in this Form 10-K and our December 31, 2010 Consolidated Financial Statements included elsewhere in this report. Certain statements contained in this MD&A may be deemed to be forward-looking statements. See "Special Note Regarding Forward-Looking Statements."

Overview

General

LSB is a manufacturing, marketing and engineering company operating through our subsidiaries. LSB and its wholly-owned subsidiaries own the following core businesses:

- Climate Control Business manufactures and sells a broad range of air conditioning and heating products in the niche markets we serve consisting of geothermal and water source heat pumps, hydronic fan coils, large custom air handlers, modular geothermal chillers and other related products used to control the environment in commercial/institutional and residential new building construction, renovation of existing buildings and replacement of existing systems. For 2010, approximately 41% of our consolidated net sales relates to the Climate Control Business.
- Chemical Business manufactures and sells nitrogen based chemical products produced from four plants located in Arkansas, Alabama, Oklahoma, and Texas for the industrial, mining and agricultural markets. Our products include high purity and commercial grade anhydrous ammonia, industrial and fertilizer grade AN, UAN, sulfuric acids, nitric acids in various concentrations, nitrogen solutions, DEF and various other products. For 2010, approximately 58% of our consolidated net sales relates to the Chemical Business.

As discussed below under "Chemical Business", the Pryor Facility began limited production of anhydrous ammonia and UAN in the first quarter of 2010. The Pryor Facility did not reach sustained production of anhydrous ammonia until the fourth quarter of 2010. Throughout November and December, market demand for ammonia was strong and most ammonia produced at the Pryor Facility was sold, rather than converted to UAN. During November and December 2010, the Pryor Facility produced a total of approximately 33,000 tons of anhydrous ammonia. Approximately 4,700 tons of the ammonia were converted into 11,500 tons of UAN and most of the balance was sold as ammonia.

Economic Conditions

Since our two core business segments serve several diverse markets, we consider market fundamentals for each market individually as we evaluate economic conditions.

Climate Control Business - Sales for 2010 were down 6% from 2009 including an 18% decline in hydronic fan coil sales and a 5% decline in geothermal and water source heat pump sales. From a construction sector perspective, the net decrease is due to a 9% reduction in commercial/institutional product sales partially offset by a 6% increase in residential product sales. The reduction in commercial/institutional sales was due to lower order levels during the latter part of 2009 and first quarter of 2010 as a result of the slowdown in commercial/institutional construction coupled with a lower product order backlog at the beginning of 2010 compared with the beginning of 2009. We have seen an increase in the level of commercial/institutional orders in the last three quarters of 2010 over the order levels in 2009. Sales and order levels of our residential products continue to increase year over year despite the slowdown in new residential construction. Based upon published reports of leading indicators, including the CMFS published by McGraw-Hill as well as the NABI published by AIA, the overall commercial/institutional construction sector should

increase modestly during 2011, where as CMFS and AIA have projected more aggressive growth in residential construction contract activity during 2011. Another factor that may affect product order rates going forward is the potential for growth in our highly energy-efficient geothermal water-source heat pumps, which could benefit significantly from government stimulus programs, including various tax incentives, although we cannot predict the impact these programs will have on our business.

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The Chemical Business - Our Chemical Business' primary markets are industrial, mining and agricultural. During 2010, approximately 61% of our Chemical Business' sales were into industrial and mining markets of which approximately 69% of these sales are to customers that have contractual obligations to purchase a minimum quantity or allow us to recover our cost plus a profit, irrespective of the volume of product sold. During 2010, customer demand for our industrial and mining products increased over 2009. We believe that such demand will continue to increase in 2011 as the industrial markets in the United States continue to recover based on the American Chemistry Council's Chemistry and Economic Report.

The remaining 39% of our Chemical Business' sales in 2010 were made into the agricultural fertilizer markets to customers that primarily purchase at spot market prices and not pursuant to contractual arrangements. Our agricultural sales volumes and margins depend upon the supply of and the demand for fertilizer, which in turn depends on the market fundamentals for crops including corn, wheat and forage. The current outlook according to most market indicators, including reports in Green Markets, Fertilizer Week and the USDA's World Agricultural Supply and Regional Estimates, point to positive supply and demand fundamentals for the types of nitrogen fertilizer products we produce and sell. However, it is possible that the fertilizer outlook could change if there are unanticipated changes in commodity prices, acres planted or unfavorable weather conditions. During 2010, the anhydrous ammonia market price increased while natural gas costs generally declined. Our Cherokee and Pryor Facilities produce anhydrous ammonia and UAN from natural gas and have benefited from increased margins. On the other hand, our El Dorado Facility is at a current cost disadvantage for their agricultural grade AN, which is produced from purchased ammonia, compared to their competitors that produce from natural gas.

2010 Results

Our consolidated net sales for 2010 were \$609.9 million compared to \$531.8 million for 2009. The sales increase of approximately \$78.1 million includes an increase of \$93.3 million in our Chemical Business partially offset by a decrease of \$15.6 million in our Climate Control Business. Although our Climate Control Business' sales were lower for 2010, our annual order levels and year-end backlog increased over 2009.

Our consolidated operating income was \$55.9 million for 2010 compared to \$40.7 million for 2009. The increase in operating income of \$15.2 million included an increase of \$16.8 million in our Chemical Business partially offset by a decrease of \$2.4 million in our Climate Control Business. In addition, our general corporate expense and other business operations net expenses decreased \$0.8 million.

Our resulting effective income tax rate for 2010 was approximately 40% compared to 41% for 2009. As previously reported, during 2010, we determined that certain nondeductible expenses had not been properly identified relating to the 2007-2009 provisions for income taxes. As a result, we recorded an additional income tax provision of approximately \$800,000 for 2010. For 2010, the effect of this adjustment decreased basic and diluted net income per share by \$.04 and \$.03, respectively.

Climate Control Business

Our Climate Control sales for 2010 were \$250.5 million, or \$15.6 million below 2009, comprised of an approximately \$8.4 million decline in hydronic fan coil sales and a \$8.3 million decrease in geothermal and water source heat pump sales partially offset by an increase of \$1.1 million in other HVAC sales. From a commercial/institutional market sector perspective, the net decrease includes a \$19.2 million decline in commercial/institutional product sales offset by an approximately \$3.6 million increase in residential product sales. The decline in the commercial/institutional sector of our business is attributable to the general economic conditions in the industries and markets we serve.

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We continue to closely follow economic indicators and have attempted to assess the impact on the commercial/institutional and residential construction sectors that we serve, including, but not limited to, new construction and/or renovation of facilities in the following sectors:

- Single-Family Residential
 - Education
 - Healthcare
 - Offices
- Multi-Family Residential
 - Lodging
 - Manufacturing
 - Pharmaceutical

During 2010, approximately 75% of our Climate Control Business' sales were to the commercial/institutional and multi-family construction markets, and the remaining 25% were sales of geothermal heat pumps ("GHPs") to the single-family residential market.

For 2010, the product order intake level was \$254.7 million as compared to \$207.2 million for 2009. For the fourth quarter of 2010, the product order intake was \$61.3 million and sales were \$72.5 million compared to \$48.5 million and \$59.7 million, respectively, for the same period of 2009. For 2010, product orders for commercial/institutional and residential products increased 23.5% and 21.3%, respectively, as compared to 2009. Our product order level consists of confirmed purchase orders from customers that have been accepted and received credit approval.

Our order backlog was \$47.6 million at December 31, 2010 as compared to \$54.8 million at September 30, 2010, \$48.2 million at June 30, 2010, \$36.0 million at March 31, 2010, and \$32.2 million at December 31, 2009. The backlog consists of confirmed customer orders for product to be shipped at a future date. Historically, we have not experienced significant cancellations relating to our backlog of confirmed customer product orders, and we expect to ship substantially all of these orders within the next twelve months; however, it is possible that some of our customers could cancel a portion of our backlog or extend the shipment terms. For the first two months of 2011, our new orders received were approximately \$43 million and our backlog was approximately \$52 million at February 28, 2011.

Product orders and backlog, as reported, generally do not include amounts relating to shipping and handling charges, service orders or service contract orders. In addition, product orders and backlog, as reported, exclude contracts related to our engineering and construction business due to the relative size of individual projects and, in some cases, extended timeframe for completion beyond a twelve-month period.

Our GHPs use a form of renewable energy and, under certain conditions, can reduce energy costs up to 80% compared to conventional HVAC systems. Tax legislation continues to provide incentives for customers purchasing products using forms of renewable energy. Homeowners who install GHP's are eligible for a 30% tax credit. Businesses that install GHP's are eligible for a 10% tax credit and five year accelerated depreciation on the balance of the system cost. During 2011, businesses also have the option of electing 100% bonus depreciation on qualifying equipment, such as GHP's, that are placed in service during the year.

Although our Climate Control Business has shown steady improvement in new order levels during the last three quarters of 2010 over the comparable quarters of 2009, we expect to see a continuing slow recovery in the short-term as compared to pre-recession levels. We have significantly increased our sales and marketing efforts for all of our Climate Control products, primarily to expand the market for our products, including GHPs. We believe that the recently enacted federal tax credits for GHPs have had a positive impact on sales of those highly energy efficient and green products.

Chemical Business

Our Chemical Business operates the El Dorado Facility, the Cherokee Facility, the Baytown Facility and the Pryor Facility. The El Dorado and Baytown Facilities produce nitrogen products from anhydrous ammonia delivered by

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pipeline. The El Dorado Facility also produces sulfuric acid from recovered elemental sulfur delivered by truck and rail. The Cherokee and Pryor Facilities produce anhydrous ammonia and nitrogen products from natural gas delivered by pipeline but can also receive supplemental anhydrous ammonia by truck, rail or barge.

Our Chemical Business sales for 2010 were \$351.1 million, an increase of \$93.3 million. The sales increase was a result of increased volumes of mining and industrial acid products. Agricultural sales also increased primarily due to sales from our Pryor Facility of \$25.0 million, which facility did not recognize sales in 2009. In addition, increases in raw material costs resulted in higher selling prices to customers that have contractual obligations allowing us to recover our costs.

The percentage change in sales (volume and dollars) for 2010 compared to 2009 is as follows:

	Percentage Change of Tons Dollars Increase	
Chemical products:		
Agricultural	10%	30%
Industrial acids and other	27%	32%
Mining	31%	54%
Total weighted-average change	24%	36%

The disproportionate change in agricultural tons sold versus sales dollars is primarily due to lower agricultural grade AN demand due to dry, hot weather conditions in certain of our primary markets, partially offset by increased selling prices. UAN sales volumes were also lower and were impacted primarily by lower inventory on hand at the beginning of the 2010 third quarter and an extended Turnaround at our Cherokee Facility.

The increase in industrial acids and mining sales both in tons and dollars is partially due to improved economic conditions resulting in increased customer demand, as well as higher ammonia feedstock cost in 2010 that was passed through in the selling price pursuant to pricing arrangements with certain customers.

Since the Pryor Facility did not reach sustained production until the fourth quarter of 2010, most of its operating expenses for 2010 and 2009 were not attributable to the production of product and were therefore expensed as incurred rather than charged to inventory. Approximately \$13.3 million and \$16.0 million of Pryor Facility operating expenses were classified as selling, general and administrative expense ("SG&A") in 2010 and 2009, respectively.

During the fourth quarter of 2010, the Pryor Facility reached sustained production and produced 41,000 tons of anhydrous ammonia, most of which was sold. For the fourth quarter of 2010, Pryor Facility reported unrelated party sales of \$17.2 million and operating income of \$11.4 million, which includes other income of \$3.0 million relating to property insurance recoveries.

As discussed below under "Liquidity and Capital Resources-Recognition of Insurance Recoveries", we received payments totaling \$6.5 million in 2010 associated with the Pryor Facility's property insurance claim, of which \$5.7 million is included in other income. Also, our Chemical Business recognized \$1.6 million of other income associated with other property insurance recoveries.

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Our primary raw material feedstocks (anhydrous ammonia, natural gas and sulfur) are commodities subject to significant price fluctuations, which we generally purchase at prices in effect at the time of delivery. During 2010, the average prices for those commodities compared to 2009 were as follows:

	2010	2009
Natural gas average price per MMBtu based upon Tennessee 500 pipeline pricing point	\$4.74	\$ 4.31
Ammonia average price based upon low Tampa price per metric ton	\$ 405	\$ 272
Sulfur price based upon Tampa average quarterly price per long ton	\$ 123	\$ 11

Most of our Chemical Business sales in the industrial and mining markets were pursuant to sales contracts and/or pricing arrangements on terms that include the cost of raw material feedstock as a pass through component in the sales price. Our Chemical Business sales in the agricultural markets primarily were at the market price in effect at the time of sale or at a negotiated future price.

Liquidity and Capital Resources

The following is our cash and cash equivalents, short-term investments, total interest bearing debt and stockholders' equity:

	December 31, 2010	December 31, 2009
	(Dollars In Millions)	
Cash and cash equivalents	\$ 66.9	\$ 61.7
Short-term investments (1)	10.0	10.1
	\$ 76.9	\$ 71.8
Long-term debt:		
2007 Debentures due 2012	\$ 26.9	\$ 29.4
Secured Term Loan due 2012	48.8	50.0
Other	19.7	22.4
Total long-term debt, including current portion	\$ 95.4	\$ 101.8
Total stockholders' equity	\$ 179.4	\$ 150.6
Long-term debt to stockholders' equity ratio (2)	0.5	0.7

(1) These investments consist of certificates of deposit with an original maturity of 13 weeks. All of these investments were held by financial institutions within the United States and none of these investments were in excess of the federally insured limits.

(2) This ratio is based on total long-term debt divided by total stockholders' equity and excludes the use of cash on hand and short-term investments to pay down debt.

At December 31, 2010, our cash, cash equivalents and short-term investments totaled \$76.9 million and our \$50 million revolving credit facility (the "Working Capital Revolver Loan") was undrawn and available to fund operations, if needed, subject to the amount of our eligible collateral and outstanding letters of credit.

For 2011, we expect our primary cash needs will be for working capital and capital expenditures. We plan to rely upon internally generated cash flows, cash on hand, proposed new financing, and the borrowing availability under the

Working Capital Revolver Loan to fund operations and pay obligations. See discussion below concerning our proposed new financing and our universal shelf registration statement. Our internally generated cash flows and liquidity could be affected by possible declines in sales volumes resulting from the uncertainty relative to the current economic conditions.

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Our convertible senior subordinated notes due July 2012 (the “2007 Debentures”) bear interest at the annual rate of 5.5%. Interest is payable in arrears on January 1 and July 1 of each year.

The secured term loan due November 2012 (the “Secured Term Loan”) accrues interest at a defined LIBOR rate plus 3%, which LIBOR rate is adjusted on a quarterly basis. The interest rate at December 31, 2010 was approximately 3.29%. The Secured Term Loan requires only quarterly interest payments with the final payment of interest and principal at maturity. However, we agreed to apply certain insurance proceeds to reduce the outstanding principal as the proceeds are received, of which we used approximately \$1.2 million to pay down the Secured Term Loan. The Secured Term Loan is secured by the real property and equipment located at the El Dorado and Cherokee Facilities.

Since the 2007 Debentures and the Secured Term Loan both mature in 2012, and considering the uncertainty that exists in current and anticipated near-term credit availability, we reviewed various alternatives for the early retirement of these obligations. Based on this review, ThermaClima engaged the Secured Term Loan lender on an exclusive basis through March 31, 2011 to use its best efforts to syndicate a new term loan of \$75 million (“Loan”). If the Loan is completed based on currently proposed terms, the Loan would be for a term of five years, collateralized with certain assets within our Chemical Business that are currently collateral for ThermaClima’s Secured Term Loan. The proposed financial covenants of the Loan are substantially identical to the financial covenants of the Secured Term Loan. We plan to use the proceeds of the Loan to prepay ThermaClima’s Secured Term Loan and the balance for working capital. ThermaClima would also be allowed under the Loan to transfer/distribute up to \$27 million to LSB to purchase or retire or repay, in a manner to be determined, the outstanding 2007 Debentures. The closing of the Loan is subject to numerous conditions, including the syndication of the Loan and completion of definitive loan agreements. We believe we will be successful in obtaining financing, which will allow us to restructure the maturing debt on terms favorable to us.

Certain subsidiaries are subject to numerous covenants under the Secured Term Loan including, but not limited to, limitation on the incurrence of certain additional indebtedness and liens, limitations on mergers, acquisitions, dissolution and sale of assets, and limitations on declaration of dividends and distributions to us, all with certain exceptions.

The Working Capital Revolver Loan, which certain subsidiaries (the “Borrowers”) are parties to, is available to fund these subsidiaries working capital requirements, if necessary, through April 13, 2012. Under the Working Capital Revolver Loan, the Borrowers may borrow on a revolving basis up to \$50.0 million based on specific percentages of eligible accounts receivable and inventories. At December 31, 2010, we had approximately \$48.9 million of borrowing availability under the Working Capital Revolver Loan based on eligible collateral and outstanding letters of credit.

The financial covenants of the Working Capital Revolver Loan and the Secured Term Loan are discussed below under “Subordinated Debentures and Loan Agreements - Terms and Conditions”. The Borrowers’ ability to maintain borrowing availability under the Working Capital Revolver Loan depends on their ability to comply with the terms and conditions of the loan agreements and their ability to generate cash flow from operations. The Borrowers are restricted under their credit agreements as to the funds they may transfer to LSB and its subsidiaries that are not parties to the loan agreement. This limitation does not prohibit payment to LSB of amounts due under a Services Agreement, Management Agreement and a Tax Sharing Agreement with ThermaClima. Based upon our current projections, we believe that cash and borrowing availability under our Working Capital Revolver Loan is adequate to fund operations during 2011.

In 2009, we filed a universal shelf registration statement on Form S-3, with the SEC. The shelf registration statement provides that we could offer and sell up to \$200 million of our securities consisting of equity (common and preferred), debt (senior and subordinated), warrants and units, or a combination thereof. This disclosure shall not constitute an

offer to sell or the solicitation of an offer to buy, nor shall there be any sale of these securities in any state in which such offer, solicitation or sale would be unlawful prior to registration or qualification under the securities laws of any such state.

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Income Taxes

We recognize and pay federal income taxes at regular corporate tax rates. The federal tax returns for 1999 through 2006 remain subject to examination for the purpose of determining the amount of tax NOL and other carryforwards. With few exceptions, the 2007-2009 years remain open for all purposes of examination by the IRS and other major tax jurisdictions. During 2011, we were notified that we will be under examination by the IRS and certain state tax authorities for the tax years 2007-2009.

We believe that we do not have any material uncertain tax positions other than the failure to file original or amended state income tax returns in some jurisdictions where LSB or some of its subsidiaries may have a filing responsibility. We had approximately \$700,000 and \$608,000 accrued for uncertain tax liabilities at December 31, 2010 and 2009, respectively.

Capital Expenditures

Capital Expenditures-2010

Cash used for capital expenditures during 2010 was \$34.5 million, including \$2.3 million primarily for production equipment and other upgrades for additional capacity in our Climate Control Business and \$31.7 million for our Chemical Business, primarily for process and reliability improvements of our operating facilities. The Chemical Business capital expenditures include \$15.6 million associated with the Pryor Facility, of which approximately \$8.0 million replaced PP&E damaged by a fire. The Chemical Business capital expenditures also include approximately \$0.5 million associated with maintaining compliance with environmental laws, regulations and guidelines. The capital expenditures were primarily funded from working capital and a portion of the payments received associated with our property insurance claims. In addition to capital expenditures purchased with cash, one of our Climate Control Business subsidiaries exercised its option, pursuant to the terms of the underlying operating lease, to purchase a portion of its production facility for approximately \$4.9 million, which purchase was financed by a third party lender.

Committed and Planned Capital Expenditures-2011

At December 31, 2010, we had committed capital expenditures of approximately \$3.5 million for 2011. The committed expenditures included \$1.6 million primarily for process and reliability improvements in our Chemical Business and approximately \$0.1 million to maintain compliance with environmental laws, regulations and guidelines. In addition, our commitments included \$1.8 million primarily for production equipment and facility upgrades in our Climate Control Business. We plan to fund these expenditures from working capital.

In addition to committed capital expenditures at December 31, 2010, we had additional planned capital expenditures for 2011 in our Chemical Business of approximately \$24.3 million and in our Climate Control Business of approximately \$18.4 million.

The planned capital expenditures are subject to economic conditions and approval by senior management. If these capital expenditures are approved, most of these expenditures will likely be funded from working capital and internal cash flows. In addition, see discussion below under “Wastewater Pipeline” relating to expenditures associated with the participation of the construction of a wastewater pipeline. Also see discussion below under “Information Request from EPA” that may require additional capital improvement to certain emission equipment not currently included in our committed or planned capital expenditures for 2011.

Wastewater Pipeline

The El Dorado Facility generates process wastewater, which is subject to a wastewater discharge permit issued by the ADEQ, which permit is generally renewed every five years. In conjunction with our long-term compliance plan, EDC intends to participate in a wastewater pipeline project for disposal of wastewater that the city of El Dorado, Arkansas will construct and own. The ability for the El Dorado Facility to use the wastewater pipeline will ensure EDC's ability to comply with future permit limits. In order to participate and to use the pipeline, EDC would be required to pay a portion of the construction cost of the pipeline and a portion of future operating costs. EDC

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anticipates that its share of the cost to construct the pipeline will be approximately \$4.0 million and its share of future operating costs will not be significant. The city plans to complete the construction in 2013.

Advanced Manufacturing Energy Credits

On January 8, 2010, two subsidiaries within the Climate Control Business were awarded Internal Revenue Code § 48C tax credits (also referred to as “Advanced Manufacturing Energy Credits”) of approximately \$9.6 million. The award is based on anticipated capital expenditures made from February 2009 through February 2013 for machinery that will be used to produce geothermal heat pumps and green modular chillers. As these subsidiaries invest in the qualifying machinery, we will be entitled to an income tax credit equal to 30% of the machinery cost, up to the total credit amount awarded. For 2009, we utilized \$266,000 of § 48C tax credits and we anticipate utilizing \$85,000 of these tax credits to partially offset our federal income tax liability for 2010.

Information Request from EPA

The EPA has sent information requests to most, if not all, of the nitric acid plants in the United States, including to us relating to our El Dorado, Cherokee and Baytown Facilities. The EPA is requesting information under Section 114 of the Clean Air Act as to construction and modification activities at each of these facilities over a period of years to enable the EPA to determine whether these facilities are in compliance with certain provisions of the Clean Air Act. In connection with a review by our Chemical Business of these facilities in obtaining information for the EPA pursuant to the EPA’s request, our Chemical Business management believes, subject to further review, investigation and discussion with the EPA, that certain facilities within our Chemical Business may be required to make certain capital improvements to certain emission equipment in order to comply with the requirements of the Clean Air Act. If changes to the production equipment at these facilities are required in order to bring this equipment into compliance with the Clean Air Act, the type of emission control equipment that might be imposed is unknown and, as a result, the amount of capital expenditures necessary in order to bring the equipment into compliance is unknown at this time but could be substantial.

Further, if it is determined that the equipment at any of our chemical facilities have not met the requirements of the Clean Air Act, our Chemical Business could be subject to penalties in an amount not to exceed \$27,500 per day as to each facility not in compliance and be required to retrofit each facility with the “best available control technology.” We believe this technology is already employed at the Baytown Facility. We are currently unable to determine the amount (or range of amounts) of any penalties that may be assessed by the EPA. Therefore no liability has been established at December 31, 2010, in connection with this matter.

Collective Bargaining Agreements

In July 2010, EDC entered into a new three-year collective bargaining agreement with the United Steel Workers of America at the El Dorado Facility, which commenced on August 1, 2010 and expires on July 31, 2013.

In October 2010, EDC entered into a new three-year labor contract with the International Association of Machinists and Aerospace Workers AFL-CIO on behalf of Local No. 224, which commenced on October 17, 2010 and expires on October 16, 2013.

In November 2010, CNC entered into a new three-year collective bargaining agreement with the United Steel, Paper and Forestry, Rubber, Manufacturing, Energy, Allied Industrial and Service Workers International Union, AFL-CIO, CLC, on behalf of Local Union No. 00417, which commenced on November 12, 2010 and expires on November 11, 2013.

Recognition of Insurance Recoveries

Cherokee Facility – As previously reported, in February 2009, a small nitric acid plant located at the Cherokee Facility suffered damage due to a fire. Our property insurance policy provided for replacement cost coverage relating to property damage with a \$1,000,000 property loss deductible. Because our replacement cost claim for property damages exceeded our property loss deductible and the net book value of the damaged property, we did not recognize a loss relating to property damage at the time of the fire but we recorded a property insurance claim

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receivable relating to this event. See table below summarizing the activity associated with the property insurance claim during 2010. We used approximately \$1,227,000 of the insurance proceeds to pay down the Secured Term Loan and the remaining proceeds were primarily used to pay interest expense incurred on the loan. As of December 31, 2010, we do not have any remaining insurance claims associated with our property damage coverage or any insurance claims associated with our business interruption coverage relating to this event.

Bryan Distribution Center – As previously reported, in July 2009, one of our fifteen agricultural distribution centers operated by our Chemical Business was destroyed by fire, resulting in the cessation of operations at this center, which is located in Bryan, Texas (the “Bryan Center”). Our general liability insurance policy provided for coverage against third party damages with a \$250,000 loss deductible. Our property insurance policy provided for replacement cost coverage relating to property damage and for business interruption coverage for certain lost profits and extra expense with a total \$100,000 loss deductible for both coverages. As of December 31, 2010, the third party general liability claims have exceeded our \$250,000 deductible. We have recognized the \$250,000 general liability deductible and the insurance company has been managing, processing and paying directly the third party general liability claims associated with this event. Because our replacement cost claim for property damages exceeded our property loss deductible and the net book value of the damaged property, we did not recognize a loss relating to property damage from this fire but rather we recorded an insurance claim receivable relating to this event. During the fourth quarter of 2009, we received \$545,000 from our insurance carrier as a partial payment on our insurance claim, which amount was applied against our insurance claim receivable. See the table below summarizing the activity associated with the insurance claim during 2010. We used the insurance proceeds primarily to recover the working capital utilized to rebuild the distribution center. As of December 31, 2010, we do not have any remaining insurance claims associated with our property damage coverage or any insurance claims associated with our business interruption coverage relating to this event.

Pryor Facility – As previously reported, in June 2010, a pipe failure in the primary reformer of the ammonia plant at the Pryor Facility resulted in a fire that damaged the ammonia plant. The costs associated with the rebuild of the ammonia reformer were approximately \$8 million, which work was completed by the end of September 2010. Our property insurance policy provides for replacement cost coverage relating to property damage with a \$1,000,000 loss deductible and for business interruption coverage for certain lost profits and extra expense with a 30-day waiting period plus a \$250,000 deductible. Because our replacement cost claim for property damages exceeded our property loss deductible and the net book value of the damaged property, we did not recognize a loss relating to property damage from this fire but rather we recorded an insurance claim receivable relating to this event. See table below summarizing the activity associated with the insurance claim during 2010. We used the insurance proceeds primarily to partially recover the working capital utilized to rebuild the ammonia reformer. As of December 31, 2010, we do not have any remaining insurance claims associated with our property damage coverage. A notice of an insurance claim for business interruption has been filed but the amount has not been determined. Based on our initial analysis, we believe the business interruption insurance claim will substantially exceed our deductible discussed above. A recovery, if any, from our business interruption coverage has not been recognized since it is considered a gain contingency, which will be recognized if, and when, realized or realizable and earned.

	Cherokee Facility	2010 Bryan Center (In Thousands)	Pryor Facility
Beginning insurance claim receivable balance	\$ 1,175	\$ 35	\$ -
Additions to insurance claims (1)	172	409	740
Portions of insurance recoveries applied against claims receivable	(1,347)	(444)	(740)
Ending insurance claim receivable balance	\$ -	\$ -	\$ -

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Total insurance recoveries (2)	\$	2,032	\$	1,315	\$	6,464
Insurance recoveries in excess of losses incurred (3)	\$	685	\$	871	\$	5,724

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- (1) Amounts relate to payables (approved by our insurance carriers) to unrelated third parties, payable to our insurance carrier associated with the general liability deductible, and the disposal of the net book value of the damaged property.
- (2) Approximately \$1,858,000 \$564,000 and \$6,113,000 relates to PP&E associated with the Cherokee Facility, Bryan Center and Pryor Facility, respectively.
- (3) All of these amounts are included in other income and relate to PP&E except for \$18,000 associated with Bryan Center.

Estimated Plant Turnaround Costs - 2011

Our Chemical Business expenses the costs of Turnarounds as they are incurred. Based on our current plan for Turnarounds during 2011, we currently estimate that we will incur approximately \$7.0 million to \$8.0 million of Turnaround costs, which we plan to fund from our available working capital. However, it is possible that the actual costs could be significantly different from our estimates.

Expenses Associated with Environmental Regulatory Compliance

Our Chemical Business is subject to specific federal and state environmental compliance laws, regulations and guidelines. As a result, our Chemical Business incurred expenses of \$3.1 million in 2010 in connection with environmental regulatory issues. For 2011, we expect to incur expenses ranging from \$3.0 million to \$4.0 million in connection with environmental regulatory issues. However, it is possible that the actual costs could be significantly different than our estimates.

Proposed Legislation and Regulations Concerning Greenhouse Gas Emissions

The manufacturing facilities within our Chemical Business use significant amounts of electricity, natural gas and other raw materials necessary for the production of their chemical products that result, or could result, in certain greenhouse gas emissions into the environment. Federal and state courts and administrative agencies, including the EPA, are considering the scope and scale of greenhouse gas emission regulation. There are bills pending or that have been proposed in Congress that would regulate greenhouse gas emissions through a cap-and-trade system under which emitters would be required to either install abatement systems where feasible or buy allowances for offsets of emissions of greenhouse gas. The EPA has instituted a mandatory greenhouse gas reporting requirement that began in 2010, which impacts all of our chemical manufacturing sites. Greenhouse gas regulation could increase the price of the electricity and other energy sources purchased by our chemical facilities; increase costs for natural gas and other raw materials (such as anhydrous ammonia); potentially restrict access to or the use of natural gas and other raw materials necessary to produce our chemical products; and require us to incur substantial expenditures to retrofit our chemical facilities to comply with the proposed new laws and regulations regulating greenhouse gas emissions, if adopted. Federal, state and local governments may also pass laws mandating the use of alternative energy sources, such as wind power and solar energy, which may increase the cost of energy use in certain of our chemical and other manufacturing operations. While future emission regulations or new laws appear possible, it is too early to predict how these regulations, if and when adopted, will affect our businesses, operations, liquidity or financial results.

Authorization to Repurchase 2007 Debentures and Stock

Our board of directors has granted management the authority to repurchase our 2007 Debentures on terms that management deems favorable to us if an opportunity is presented. Under this authority, we acquired in unsolicited transactions \$2,500,000 aggregate principal face during 2010, using \$2,494,000 of our working capital to purchase this portion of the 2007 Debentures. As a result, \$26,900,000 remains outstanding at December 31, 2010.

In addition, our board of directors enacted a stock repurchase authorization for an unstipulated number of shares for an indefinite period. The stock repurchase authorization will remain in effect until such time as our board of directors decides to end it. During 2010, we repurchased 177,100 shares of our common stock at a weighted-average price of \$13.67 per share using funds from our working capital.

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If we should repurchase an additional portion of our 2007 Debentures or stock, we currently intend to fund any repurchases from our available working capital or the proposed financing discussed above; however, our plan could change in the near term.

Dividends

LSB is a holding company and, accordingly, its ability to pay cash dividends on its preferred stock and common stock depends in large part on its ability to obtain funds from its subsidiaries. The ability of ThermaClima (which owns a substantial portion of the companies comprising the Climate Control Business and Chemical Business) and its wholly-owned subsidiaries to pay dividends and to make distributions to LSB is restricted by certain covenants contained in the Working Capital Revolver Loan and the Secured Term Loan agreements. Under the terms of these agreements, so long as no default or event of default has occurred, is continuing or would result therefrom, ThermaClima cannot transfer funds to LSB in the form of cash dividends or other distributions or advances, except for the following, under the terms of the loans:

- outstanding loans entered into subsequent to November 2, 2007 in excess of \$2.0 million at any time;
- amounts under a certain management agreement between LSB and ThermaClima, provided certain conditions are met;
- the repayment of costs and expenses incurred by LSB that are directly allocable to ThermaClima or its subsidiaries for LSB's provision of services under certain services agreement;
- the amount of income taxes that ThermaClima would be required to pay if they were not consolidated with LSB, and
- an amount not to exceed fifty percent (50%) of ThermaClima's consolidated net income during each fiscal year determined in accordance with generally accepted accounting principles plus income taxes paid to LSB within the previous bullet above, provided that certain other conditions are met.

Holders of our common stock are entitled to receive dividends only when and if declared by our board of directors. We have not paid cash dividends on our outstanding common stock in many years, and we do not currently anticipate paying cash dividends on our outstanding common stock in the near future. However, our board of directors has not made a decision whether or not to pay such dividends on our common stock in 2011.

During 2010, dividends totaling \$305,000 were declared and paid on our outstanding preferred stock using funds from our working capital. Each share of preferred stock is entitled to receive an annual dividend, only when declared by our board of directors, payable as follows:

- Series D 6% cumulative, convertible Class C preferred stock ("Series D Preferred") at the rate of \$.06 a share, which dividend is cumulative;
- Series B 12% cumulative, convertible preferred stock ("Series B Preferred") at the rate of \$12.00 a share, which dividend is cumulative; and
 - Noncumulative Preferred at the rate of \$10.00 a share, which is noncumulative.

On January 27, 2011, our board of directors declared the following dividends:

- \$.06 per share on our outstanding Series D Preferred for an aggregate dividend of \$60,000, payable on March 31, 2011;
- \$12.00 per share on our outstanding Series B Preferred for an aggregate dividend of \$240,000, payable on March 31, 2011; and
- \$10.00 per share on our outstanding Noncumulative Preferred for an aggregate dividend of approximately \$4,700, payable on April 1, 2011.

All shares of the Series D Preferred and Series B Preferred are owned by the Golsen Group. See “Related Party Transactions” of this MD&A for a discussion as to the amount of dividends paid to the Golsen Group during 2010. There are no optional or mandatory redemption rights with respect to the Series B Preferred or Series D Preferred.

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Compliance with Long - Term Debt Covenants

As discussed below under “Subordinated Debentures and Loan Agreements - Terms and Conditions”, the Secured Term Loan and Working Capital Revolver Loan, as amended, of ThermaClime and its subsidiaries require, among other things, that ThermaClime meet certain financial covenants. Currently, ThermaClime's forecast is that ThermaClime will be able to meet all financial covenant requirements for 2011.

Subordinated Debentures and Loan Agreements - Terms and Conditions

5.5% Convertible Senior Subordinated Debentures - In June 2007, we completed a private placement to twenty-two qualified institutional buyers, pursuant to which we sold \$60.0 million aggregate principal amount of the 2007 Debentures. Only \$26.9 million remains outstanding at December 31, 2010, including \$5.0 million owned by the Golsen Group.

The 2007 Debentures bear interest at the rate of 5.5% per year and mature on July 1, 2012. Interest is payable in arrears on January 1 and July 1 of each year. The 2007 Debentures are unsecured obligations and are subordinated in right of payment to all of our existing and future senior indebtedness, including indebtedness under our revolving debt facilities. The 2007 Debentures are effectively subordinated to all of our present and future liabilities, including trade payables.

The 2007 Debentures are convertible by the holders in whole or in part into shares of our common stock prior to their maturity. The conversion rate of the 2007 Debentures for the holders electing to convert all or any portion of a debenture is 36.4 shares of our common stock per \$1,000 principal amount of debentures (representing a conversion price of \$27.47 per share of common stock), subject to adjustment under certain conditions as set forth in the Indenture.

The 2007 Debentures may be redeemed at our option, in whole or in part, upon notice at a redemption price, payable at our option in cash or, subject to certain conditions, in shares of our common stock, equal to 100% of the principal amount of the debentures to be redeemed plus accrued and unpaid interest. We may redeem only if the closing sale price of our common stock has exceeded 115% of the conversion price, or \$31.59, for at least 20 trading days in the 30 consecutive trading day period ending immediately prior to the redemption date.

Working Capital Revolver Loan - ThermaClime's Working Capital Revolver Loan is available to fund its working capital requirements, if necessary, through April 13, 2012. Under the Working Capital Revolver Loan, ThermaClime and its subsidiaries may borrow on a revolving basis up to \$50.0 million based on specific percentages of eligible accounts receivable and inventories. At December 31, 2010, there were no outstanding borrowings. In addition, the net credit available for borrowings under our Working Capital Revolver Loan was approximately \$48.9 million at December 31, 2010, based on our eligible collateral and outstanding letters of credit as of that date. The Working Capital Revolver Loan requires that ThermaClime meet certain financial covenants, including an EBITDA requirement of greater than \$25 million; a minimum fixed charge coverage ratio of not less than 1.10 to 1; and a maximum senior leverage coverage ratio of not greater than 4.50 to 1. These requirements are measured quarterly on a trailing twelve-month basis and as defined in the agreement. As of December 31, 2010 and as defined in the agreement, ThermaClime's EBITDA was approximately \$68 million; the fixed charge coverage ratio was 10.39 to 1; and the senior leverage coverage ratio was 0.74 to 1.

Secured Term Loan - In November 2007, ThermaClime and certain of its subsidiaries entered into the \$50 million Secured Term Loan with a certain lender. Proceeds from the Secured Term Loan were used to repay the previous senior secured loan. The Secured Term Loan matures on November 2, 2012. The Secured Term Loan accrues interest at a defined LIBOR rate plus 3%, which LIBOR rate is adjusted on a quarterly basis. The interest rate at December 31,

2010 was approximately 3.29%. The Secured Term Loan requires only quarterly interest payments with the final payment of interest and principal at maturity. During 2010, we received proceeds from our insurance carrier as a partial payment on an insurance claim, of which we used approximately \$1.2 million to pay down the Secured Term Loan. As a result, approximately \$48.8 million remain outstanding at December 31, 2010. The Secured Term Loan is secured by the real property and equipment located at the El Dorado and Cherokee Facilities. The carrying value of the pledged assets is approximately \$64 million at December 31, 2010.

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The Secured Term Loan borrowers are subject to numerous covenants under the agreement including, but not limited to, limitation on the incurrence of certain additional indebtedness and liens; limitations on mergers, acquisitions, dissolution and sale of assets; and limitations on declaration of dividends and distributions to us, all with certain exceptions. At December 31, 2010, the carrying value of the restricted net assets of ThermaClima and its subsidiaries was approximately \$78 million. As defined in the agreement, the Secured Term Loan borrowers are also subject to a minimum fixed charge coverage ratio of not less than 1.10 to 1 and a maximum leverage ratio of not greater than 4.50 to 1. Both of these requirements are measured quarterly on a trailing twelve-month basis. As of December 31, 2010 and as defined in the agreement, Secured Term Loan borrowers' fixed charge coverage ratio was 5.21 to 1 and the leverage coverage ratio was 0.85 to 1. The maturity date of the Secured Term Loan can be accelerated by the lender upon the occurrence of a continuing event of default, as defined.

Cross-Default Provisions - The Working Capital Revolver Loan agreement and the Secured Term Loan contain cross-default provisions. If ThermaClima fails to meet the financial covenants of either of these agreements, the lenders may declare an event of default.

Seasonality

We believe that our only significant seasonal products are fertilizer and related chemical products sold by our Chemical Business to the agricultural industry. The selling seasons for those products are primarily during the spring and fall planting seasons, which typically extend from March through June and from September through November in the geographical markets in which the majority of our agricultural products are distributed. As a result, our Chemical Business increases its inventory of agricultural products prior to the beginning of each planting season. In addition, the amount and timing of sales to the agricultural markets depend upon weather conditions and other circumstances beyond our control.

Related Party Transactions

Golsen Group

The Golsen Group holds \$5,000,000 of the 2007 Debentures. As a result in January 2010, we paid interest of \$137,500 relating to the debentures held by the Golsen Group that was accrued at December 31, 2009. During 2010, we incurred interest expense of \$275,000 relating to the debentures held by the Golsen Group, of which \$137,500 was accrued at December 31, 2010 and subsequently paid in January 2011. In March 2010, we paid dividends totaling \$300,000 on our Series B Preferred and our Series D Preferred, all of the outstanding shares of which are owned by the Golsen Group.

Results of Operations

The following Results of Operations should be read in conjunction with our consolidated financial statements for the years ended December 31, 2010, 2009, and 2008 and accompanying notes and the discussions above under "Overview" and "Liquidity and Capital Resources."

We present the following information about our results of operations for our two core business segments, Climate Control Business and Chemical Business. Gross profit by business segment represents net sales less cost of sales. In addition, our chief operating decision makers use operating income by business segment for purposes of making decisions that include resource allocations and performance evaluations. Operating income by business segment represents gross profit by business segment less selling, SG&A incurred by each business segment plus other income and other expense earned/incurred by each business segment before general corporate expenses and other business operations, net. The business operation classified as "Other" primarily sells industrial machinery and related components

to machine tool dealers and end users. General corporate expenses and other business operations, net consist of unallocated portions of gross profit, SG&A, other income and other expense.

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The following table contains certain information about our continuing operations in different business segments for each of the three years ended December 31:

	2010	2009	2008
	(In Thousands)		
Net sales:			
Climate Control	\$ 250,521	\$ 266,169	\$ 311,380
Chemical	351,086	257,832	424,117
Other	8,298	7,837	13,470
	\$ 609,905	\$ 531,838	\$ 748,967
Gross profit:			
Climate Control	\$ 86,364	\$ 92,409	\$ 96,633
Chemical	49,295	42,422	37,991
Other	2,966	2,583	4,256
	\$ 138,625	\$ 137,414	\$ 138,880
Operating income (loss):			
Climate Control	\$ 35,338	\$ 37,706	\$ 38,944
Chemical	31,948	15,122	31,340
General corporate expense and other business operations, net	(11,361)	(12,118)	(11,129)
	55,925	40,710	59,155
Interest expense	(7,427)	(6,746)	(11,381)
Gains (loss) on extinguishment of debt	(52)	1,783	5,529
Non-operating income, net:			
Climate Control	3	8	1
Chemical	7	31	27
Corporate and other business operations	43	91	1,068
Provisions for income taxes	(19,787)	(15,024)	(18,776)
Equity in earnings of affiliate - Climate Control	1,003	996	937
Income from continuing operations	\$ 29,715	\$ 21,849	\$ 36,560

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Year Ended December 31, 2010 Compared to Year Ended December 31, 2009

Climate Control Business

The following table contains certain information about our net sales, gross profit and operating income in our Climate Control segment for 2010 and 2009:

	2010	2009	Change	Percentage Change
	(Dollars In Thousands)			
Net sales:				
Geothermal and water source heat pumps	\$ 171,561	\$ 179,865	\$ (8,304)	(4.6) %
Hydronic fan coils	37,923	46,381	(8,458)	(18.2) %
Other HVAC products	41,037	39,923	1,114	2.8 %
Total Climate Control	\$ 250,521	\$ 266,169	\$ (15,648)	(5.9) %
Gross profit – Climate Control	\$ 86,364	\$ 92,409	\$ (6,045)	(6.5) %
Gross profit percentage – Climate Control (1)	34.5 %	34.7 %	(0.2) %	
Operating income – Climate Control	\$ 35,338	\$ 37,706	\$ (2,368)	(6.3) %

(1) As a percentage of net sales

Net Sales – Climate Control

- Net sales of our geothermal and water source heat pump products decreased primarily as a result of a 9.3% decline in sales of our commercial/institutional products due to the slowdown in the construction and renovation activities in the markets we serve partially offset by a 5.9% increase in sales of our residential products, principally during the second half of 2010. During 2010, we continued to maintain a market share leadership position of approximately 38%, based on market data supplied by the AHRI;
- Net sales of our hydronic fan coils decreased primarily due to a 7.4% decline in the number of units sold due to the slowdown in the construction and renovation activities in the markets we serve and a 13.3% decrease in the average unit sales price due to a change in product mix. During 2010, we continue to have a market share leadership position of approximately 29% based on market data supplied by the AHRI;
- Net sales of our other HVAC products increased as the result of higher sales of custom air handlers and modular chillers partially offset by lower sales in our engineering and construction services.

Gross Profit – Climate Control

The decline in gross profit in our Climate Control Business was the result of lower sales volume as discussed above and to a lesser extent higher raw material costs offset by an improvement in product mix, primarily the increase in residential product sales. The gross profit as a percentage of sales was approximately the same for both periods.

Operating Income – Climate Control

Operating income decreased primarily as a result of the decrease in gross profit as discussed above partially offset by a decrease in operating expenses. Significant changes in operating expenses include a decrease in commission expenses of \$1.0 million due primarily to lower sales volume, a net decrease in warranty expenses of \$0.8 million

primarily as a result of lower sales volume partially offset by the impact of increasing our warranty coverage period for certain products, and decreases in expenses relating to employee health insurance costs primarily due to a reduction in actual spending and product liability costs due primarily to a decline in the value of claims (\$1.0 million and \$0.8 million, respectively).

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Chemical Business

The following table contains certain information about our net sales, gross profit and operating income in our Chemical segment for 2010 and 2009:

	2010	2009	Change	Percentage Change
	(Dollars In Thousands)			
Net sales:				
Agricultural products	\$ 135,598	\$ 104,300	\$ 31,298	30.0 %
Industrial acids and other chemical products	126,846	95,997	30,849	32.1 %
Mining products	88,642	57,535	31,107	54.1 %
Total Chemical	\$ 351,086	\$ 257,832	\$ 93,254	36.2 %
Gross profit - Chemical	\$ 49,295	\$ 42,422	\$ 6,873	16.2 %
Gross profit percentage – Chemical (1)	14.0 %	16.5 %	(2.5) %	
Operating income - Chemical	\$ 31,948	\$ 15,122	\$ 16,826	111.3 %

(1) As a percentage of net sales

Net Sales - Chemical

The El Dorado and Cherokee Facilities produce all the chemical products described in the table above and the Baytown Facility produces only industrial acids products. The Pryor Facility produces agricultural and industrial chemical products as discussed above under “Overview-General”. For 2010, overall sales prices for the Chemical Business increased 13% and the volume of tons sold increased 24%, compared with 2009, generally as a result of the following:

- Agricultural products sales-Agricultural products sales increase of \$31.3 million, or 30%, was primarily a result of price increases driven by a general increase in market demand reflecting an improving economy and the impact of higher raw material costs. In addition, tons of agricultural products sold increased 10% including an increase of 19,000 tons of UAN and 49,000 tons of ammonia sold into agricultural markets from the Pryor Facility partially offset by 25,000 fewer tons of fertilizer grade AN due to unfavorable weather conditions in the first quarter 2010.
- Industrial acids and other chemical products sales-Industrial acids and other products sales increase of \$30.8 million, or 32%, primarily related to a 27% increase in tons sold including an increase of 134,000 tons, 18,000 tons and 11,000 tons from the Baytown, El Dorado and Cherokee Facilities, respectively. The increase in volume is primarily due to improved economic conditions, spot sales opportunities and new customers.
- Mining products sales-Mining products sales increase of \$31.1 million, or 54%, includes an increase of tons sold of 31%, including volume increases of 66,000 tons of industrial grade AN and 13,000 tons of ammonia nitrate solutions. In addition, sales prices were higher driven by a general increase in raw material and other costs, which we are able to pass through to certain customers pursuant to the terms of supply agreements. Our industrial grade AN is primarily sold to one customer pursuant to a multi-year take or pay supply contract in which the customer agreed to purchase, and our El Dorado Facility agreed to reserve certain minimum volumes of industrial grade AN during 2010. The cost-plus supply contract, effective January 1, 2010, increased the annual minimum volume from 210,000 tons to 240,000 tons. Pursuant to the terms of the contract, the customer has been invoiced for the fixed costs and profit associated with the reserved capacity despite not taking the minimum volume requirement.

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Gross Profit - Chemical

Gross profit increased \$6.9 million on an increase in sales of \$93.3 million. The increase was due, in part, to reduced costs per ton as the result of improved production efficiencies and higher volumes. Gross profit for agricultural products was \$6.4 million higher, which included \$7.4 million from agricultural ammonia sales at the recently started Pryor Facility, an increase of \$6.9 million from UAN and other agricultural products sales primarily due to rising prices, partially offset by a decrease of \$7.9 million from fertilizer grade AN sales. As noted above under “Overview – Chemical Business”, the average price of one of our primary raw material feedstocks (anhydrous ammonia) increased in 2010, which contributed to the lower gross profit on fertilizer grade AN sales. In addition, gross profit on industrial and mining products was \$6.8 million higher. Also impacting gross profit were:

- \$5.8 million reduction in gross profit from firm sales commitments made in prior periods,
 - \$1.2 million reduction in gains from precious metals recoveries,
 - \$1.3 million reduction in gross profit due to other plant variances, and
- \$2.0 million reduction in losses on natural gas and ammonia hedging contracts.

Primarily as a result of these items and due to increased volumes to customers with contractual arrangements allowing us to recover our raw material costs, our overall gross profit as a percentage of sales decreased 2.5%.

Operating Income - Chemical

In addition to the increase in gross profit of \$6.9 million discussed above, our Chemical Business’ operating income includes operating and other expenses associated with the Pryor Facility of approximately \$13.6 million for 2010 compared to \$16.0 million for 2009. We also recorded a gain of \$5.7 million from insurance recoveries at our Pryor Facility, and other insurance gains of \$1.6 million as discussed above under “Liquidity and Capital Resources - Recognition of Insurance Recoveries”.

Other

The business operation classified as “Other” primarily sells industrial machinery and related components to machine tool dealers and end users. General corporate expenses and other business operations, net consist of unallocated portions of gross profit, SG&A, other income and other expense. The following table contains certain information about our net sales and gross profit classified as “Other” and general corporate expenses and other business operations, net, for 2010 and 2009:

	2010	2009	Change	Percentage Change
	(Dollars In Thousands)			
Net sales - Other	\$ 8,298	\$ 7,837	\$ 461	5.9 %
Gross profit - Other	\$ 2,966	\$ 2,583	\$ 383	14.8 %
Gross profit percentage – Other (1)	35.7 %	33.0 %	2.7 %	
General corporate expense and other business operations, net	\$ (11,361)	\$ (12,118)	\$ 757	(6.2) %

(1) As a percentage of net sales

Net Sales - Other

The increase in net sales classified as “Other” relates primarily to the improvement in demand for industrial machinery.

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Gross Profit - Other

The increase in gross profit classified as “Other” is due primarily to the increase in sales as discussed above.

General Corporate Expense and Other Business Operations, Net

Our general corporate expense and other business operations, net, decreased by \$0.8 million primarily as the result of the increase in gross profit classified as “Other” as discussed above.

Interest Expense

Interest expense was \$7.4 million for 2010 compared to \$6.7 million for 2009, an increase of approximately \$0.7 million. This increase primarily relates to losses (realized and unrealized) of \$1.5 million recognized in 2010 associated with our interest rate contracts compared to \$0.7 million in 2009.

Loss and Gain on Extinguishment of Debt

During 2010, we acquired \$2,500,000 aggregate principal amount of the 2007 Debentures for \$2,494,000 and recognized a loss on extinguishment of debt of \$52,000, after writing off the unamortized debt issuance costs associated with the 2007 Debentures acquired. During 2009, we acquired \$11,100,000 aggregate principal amount of the 2007 Debentures for approximately \$8,938,000 and recognized a gain on extinguishment of debt of \$1,783,000, after writing off the unamortized debt issuance costs associated with the 2007 Debentures acquired.

Provision For Income Taxes

The provision for income taxes for 2010 was \$19.8 million compared to \$15.0 million for 2009. The resulting effective tax rate for 2010 was 40% compared to 41% for 2009. As previously reported and discussed above under “Overview – 2010 Results”, during 2010, we determined that certain nondeductible expenses had not been properly identified relating to the 2007-2009 provisions for income taxes. As a result, we recorded an additional income tax provision of approximately \$800,000 for 2010.

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Year Ended December 31, 2009 Compared to Year Ended December 31, 2008

Climate Control Business

The following table contains certain information about our net sales, gross profit and operating income in our Climate Control segment for 2009 and 2008:

	2009	2008	Change	Percentage Change
	(Dollars In Thousands)			
Net sales:				
Geothermal and water source heat pumps	\$ 179,865	\$ 190,960	\$ (11,095)	(5.8) %
Hydronic fan coils	46,381	83,472	(37,091)	(44.4) %
Other HVAC products	39,923	36,948	2,975	8.1 %
Total Climate Control	\$ 266,169	\$ 311,380	\$ (45,211)	(14.5) %
Gross profit – Climate Control	\$ 92,409	\$ 96,633	\$ (4,224)	(4.4) %
Gross profit percentage – Climate Control (1)	34.7 %	31.0 %	3.7 %	
Operating income – Climate Control	\$ 37,706	\$ 38,944	\$ (1,238)	(3.2) %

(1) As a percentage of net sales

Net Sales – Climate Control

- Net sales of our geothermal and water source heat pump products decreased primarily as a result of a 9.8% decrease in sales of our commercial/institutional products due to the slowdown in the construction and renovation activities in the markets we serve partially offset by a 4.0% increase in sales of our residential products. During 2009, we continued to maintain a market share leadership position of approximately 40%, based on market data supplied by the AHRI;
- Net sales of our hydronic fan coils decreased primarily due to a 43.7% decrease in the number of units sold due to the slowdown in the construction and renovation activities in the markets we serve and a decline in the average unit sales price due to change in product mix. During 2009, we continue to have a market share leadership position of approximately 30% based on market data supplied by the AHRI;
- Net sales of our other HVAC products increased primarily as the result of an increase in engineering and construction services completed on construction contracts entered into during 2008 as well as an increase in sales of our modular chillers partially offset by a decline in sales of our large custom air handlers.

Gross Profit – Climate Control

The decrease in gross profit was primarily the result of lower sales volume in our hydronic fan coil and geothermal and water source heat pump products partially offset by a change in product mix, primarily a higher content of geothermal and water source heat pump products that have a higher gross profit percentage, and a decrease in the cost of our raw materials. In addition, our engineering and construction business increased its contribution to gross profit on completed projects and customer change orders. As a result, our gross profit percentage improved 3.7% compared to 2008. Competitive pressures on product pricing and recent increases in market prices of raw materials, especially steel, copper and aluminum, could impact gross margins negatively going forward, if we are unable to pass these cost increases to our customers in the form of higher sales prices.

Operating Income – Climate Control

Operating income decreased slightly primarily as a result of the decrease in gross profit as discussed above partially offset by lower operating expenses. Significant changes in operating expenses include lower freight and commission expenses due primarily to reduced sales volume (\$3.1 million and \$2.3 million, respectively) and lower legal and

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other professional fees (\$0.7 million) due primarily to a patent infringement defense in 2008 and other miscellaneous items (\$0.5 million) partially offset by an increase in advertising expenses (\$3.6 million) as a result of a marketing program launched by one of our subsidiaries.

Chemical Business

The following table contains certain information about our net sales, gross profit and operating income in our Chemical segment for 2009 and 2008:

	2009	2008	Change	Percentage Change
		(Dollars In Thousands)		
Net sales:				
Agricultural products	\$ 104,300	\$ 152,802	\$ (48,502)	(31.7) %
Industrial acids and other chemical products	95,997	162,941	(66,944)	(41.1) %
Mining products	57,535	108,374	(50,839)	(46.9) %
Total Chemical	\$ 257,832	\$ 424,117	\$ (166,285)	(39.2) %
Gross profit - Chemical	\$ 42,422	\$ 37,991	\$ 4,431	11.7 %
Gross profit percentage – Chemical (1)	16.5 %	9.0 %	7.5 %	
Operating income - Chemical	\$ 15,122	\$ 31,340	\$ (16,218)	(51.7) %

(1) As a percentage of net sales

Net Sales - Chemical

The El Dorado and Cherokee Facilities produce all the chemical products described in the table above and the Baytown Facility produces only industrial acids products. For 2009, overall sales prices for the Chemical Business decreased 35% and the volume of tons sold decreased 7%, compared with 2008, generally as a result of the following:

- Sales prices for products produced at the El Dorado Facility decreased 33% related, in part, to the lower cost of raw material, anhydrous ammonia, part of which is passed through to our customers pursuant to contracts and/or pricing arrangements that include raw material feedstock as a pass-through component in the sales price. Our industrial grade AN is sold to one customer pursuant to a multi-year take or pay supply contract in which the customer has agreed to purchase from our El Dorado Facility a certain minimum volume of industrial grade AN during the year. This customer ordered less than the contractual minimum quantity of industrial grade AN product that it was required to purchase during 2009 contributing to the decline in sales. Pursuant to the terms of the contract, the customer was invoiced and paid for certain unrecovered fixed costs and profit on the minimum volume not taken in 2009. Pricing for agricultural grade AN was lower in 2009 due primarily to falling commodity prices beginning in the later half of 2008. However, fertilizer grade AN volume of tons shipped at the El Dorado Facility increased 36% compared to 2008 as the result of more favorable market conditions. Overall volume of all products sold from the El Dorado Facility increased slightly compared to 2008.
- Sales prices and volumes for products produced at the Cherokee Facility decreased 41% and 3%, respectively, primarily related to the lower market-driven demand for UAN in 2009. This situation was compounded by unfavorable weather conditions in Cherokee's primary market resulting in lower fertilizer application. Sales prices also decreased with the pass through of our lower natural gas costs in 2009 compared to 2008, under pricing arrangements with certain of our industrial customers.

- Sales prices decreased approximately 35% for products produced at the Baytown Facility due to lower ammonia cost, which is a pass-through component to Bayer. Overall volumes decreased 24% as the result of a decline in customer demand primarily due to the economic downturn. Sales are also lower due to the elimination of a pass-through cost component for lease expense pursuant to the terms of the Bayer Agreement. The lower sales prices and lower volumes had only a minimum impact to gross profit and operating income due to certain provisions of the Bayer Agreement.

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Gross Profit - Chemical

The increase in gross profit of our Chemical Business includes \$6.6 million in higher margins on our chemical products sold in excess of then current market prices due to firm sales commitments made in 2008 when market prices were higher, and \$6.4 million reduction of losses (both realized and unrealized) on natural gas and ammonia hedging contracts in 2009 compared to 2008. Also contributing to the increase in gross profit was improved production efficiencies of \$3.9 million due, in part, to unplanned downtime incurred at the Cherokee Facility in 2008, a reduction in our turnaround costs due to the timing of certain turnarounds, and an increase in recoveries of precious metals. This increase in gross profit was partially offset by lower agricultural product margins of \$10.8 million due primarily to lower margins on UAN fertilizer. Our UAN margins were lower due to market conditions, including poor weather conditions, a reluctance of distributors to build inventory, and possibly lower levels of nitrogen fertilizer applied to crops. In addition, the Pryor Facility incurred a \$1.2 million loss on firm sales commitments entered into during 2009, of which \$0.4 million relates to outstanding firm sales commitments at December 31, 2009. Primarily as a result of these items, our overall gross profit as a percentage of sales improved for 2009 compared to 2008.

Operating Income - Chemical

The decrease of our Chemical Business' operating income includes start up expenses associated with the Pryor Facility of approximately \$16.0 million (which does not include the \$1.2 million loss on the Pryor Facility's sales commitments discussed above) compared to \$2.4 million for 2008. In addition, we recognized other operating income of \$7.6 million from a litigation judgment during 2008. This decrease was partially offset by the increase in gross profit of \$4.4 million as discussed above.

Other

The business operation classified as "Other" primarily sells industrial machinery and related components to machine tool dealers and end users. General corporate expenses and other business operations, net consist of unallocated portions of gross profit, SG&A, other income and other expense. The following table contains certain information about our net sales and gross profit classified as "Other" and general corporate expenses and other business operations, net, for 2009 and 2008:

	2009	2008	Change	Percentage Change
		(Dollars In Thousands)		
Net sales - Other	\$ 7,837	\$ 13,470	\$ (5,633)	(41.8)%
Gross profit - Other	\$ 2,583	\$ 4,256	\$ (1,673)	(39.3)%
Gross profit percentage – Other (1)	33.0 %	31.6 %	1.4 %	
General corporate expense and other business operations, net	\$ (12,118)	\$ (11,129)	\$ (989)	8.9 %

(1) As a percentage of net sales

Net Sales - Other

The decrease in net sales classified as "Other" relates primarily to lower demand for new industrial machinery as a result of the present global economic conditions and downturn in capital equipment spending.

Gross Profit - Other

The decrease in gross profit classified as “Other” is due primarily to the decrease in sales as discussed above.

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General Corporate Expense and Other Business Operations, Net

Our general corporate expense and other business operations, net increased by approximately \$1.0 million primarily as the result of the decrease in gross profit classified as “Other” as discussed above partially offset by a decrease of \$1.1 million of professional fees primarily relating to a reduction in fees associated with the assistance in our evaluation of internal controls and procedures and related documentation for Sarbanes-Oxley requirements and to legal fees on various legal matters.

Interest Expense

Interest expense was \$6.7 million for 2009 compared to \$11.4 million for 2008, a decrease of approximately \$4.7 million. This decrease primarily relates to a decrease in losses of \$2.1 million associated with our interest rate contracts, a decrease of \$1.6 million as the result of the acquisitions of the 2007 Debentures and a decrease of \$1.1 million due to the decline in the LIBOR rate associated with the Secured Term Loan.

Gain on Extinguishment of Debt

During 2009 and 2008, we acquired \$11.1 million and \$19.5 million, respectively, aggregate principal amount of the 2007 Debentures for approximately \$8.9 million and \$13.2 million, respectively, and recognized a gain on extinguishment of debt of \$1.8 million and \$5.5 million, respectively, after expensing the unamortized debt issuance costs associated with the 2007 Debentures acquired.

Non-Operating Other Income, Net

Our non-operating other income, net was \$0.1 million for 2009 compared to \$1.1 million for 2008. The decrease of \$1.0 million relates primarily to higher returns received in 2008 from highly liquid investments.

Provision For Income Taxes

The provision for income taxes for 2009 was \$15.0 million compared to \$18.8 million for 2008. The resulting effective tax rate for 2009 was 40.7% compared to 33.9% for 2008. During 2009, we incurred an additional provision relating to adjustments reconciling the 2008 federal and state income tax returns to the 2008 estimated tax provision. Additionally, the impact of lower taxable income which limited the amount of the manufacturing deduction that can be utilized also increased our provision for income taxes. During 2008, we incurred current and deferred federal and state income taxes due, in part, to increased taxable income and higher effective tax rates partially offset by a net deferred income tax benefit of \$1.6 million as the result of a detailed analysis performed on all our deferred tax assets and liabilities and the realizability of those deferred tax assets.

Cash Flow From Continuing Operating Activities

Historically, our primary cash needs have been for operating expenses, working capital and capital expenditures. We have financed our cash requirements primarily through internally generated cash flow, borrowings under our revolving credit facilities, secured asset financing and the sale of assets. See additional discussions concerning cash flow relating to our Climate Control and Chemical Businesses under “Overview” and “Liquidity and Capital Resources” of this MD&A.

For 2010, net cash provided by continuing operating activities was \$44.2 million, including net income plus depreciation and amortization, deferred income taxes, gain on property insurance recoveries associated with PP&E, and other adjustments and net cash provided by the following significant changes in assets and liabilities.

Accounts receivable increased \$17.3 million including:

- an increase of \$11.0 million relating to the Chemical Business as the result of increased sales of our mining products, increased sales at our Baytown Facility and sales from our Pryor Facility and
- an increase of \$6.7 million relating to the Climate Control Business due primarily to higher sales during the latter portion of the fourth quarter of 2010 compared to the same period of 2009.

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Inventories increased \$9.3 million primarily in the Chemical Business as the result of increased raw material costs and the start of production at our Pryor Facility.

The change in prepaid and accrued income taxes of \$5.9 million primarily relates to the recognition of higher income taxes for 2010 on improved operating results (including \$0.8 million as discussed above under “Results of Operations” relating to 2010) partially offset by payments made to the taxing authorities.

Other supplies and prepaid items increased \$1.6 million including:

- an increase of \$1.9 million of supplies relating to the Chemical Business due primarily to a planned increase in the volume on hand at our facilities partially offset by
 - a decrease of \$1.0 million of precious metals primarily as the result of lower costs and volume on hand.

Accounts payable increased \$15.6 million including:

- an increase of \$14.7 million in the Chemical Business primarily as the result of increased raw material costs and repairs incurred during the fourth quarter of 2010 at the El Dorado Facility and
- an increase of \$1.2 million in the Climate Control Business due primarily to increased costs and purchases of raw materials.

Customer deposits increased \$2.0 million in the Chemical Business due primarily to cash received from customers associated with customer product orders.

Cash Flow from Continuing Investing Activities

Net cash used by continuing investing activities for 2010 was \$26.0 million that consisted primarily of \$34.5 million for capital expenditures of which \$2.3 million and \$31.7 million are for the benefit of our Climate Control and Chemical Businesses, respectively. The cash used for capital expenditures by our Chemical Business includes \$15.6 million relating to the Pryor Facility. This use of cash was partially offset by \$8.8 million of proceeds from property insurances recoveries associated with PP&E.

Cash Flow from Continuing Financing Activities

Net cash used by continuing financing activities was \$12.6 million that primarily consisted of payments on long-term debt and loans totaling \$9.3 million, the acquisition of a portion of the 2007 Debentures for \$2.5 million and purchases of treasury stock of \$2.4 million.

Critical Accounting Policies and Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amount of assets, liabilities, revenues and expenses, and disclosures of contingencies. For each of the last three years ended December 31, 2010, 2009, and 2008, we did not experience a material change in accounting estimates. However, it is reasonably possible that the estimates and assumptions utilized as of December 31, 2010 could change in the near term. In addition, the more critical areas of financial reporting impacted by management's judgment, estimates and assumptions include the following:

Accounts Receivable and Credit Risk – Our accounts receivable are stated at net realizable value. This value includes an appropriate allowance for estimated uncollectible accounts to reflect any loss anticipated on accounts receivable balances. Our estimate is based on historical experience and periodic assessment of outstanding accounts receivable,

particularly those accounts which are past due (based upon the terms of the sale). Our periodic assessment of our accounts receivable is based on our best estimate of amounts that are not recoverable. In addition, our sales to contractors and independent sales representatives are generally subject to a mechanic's lien in the Climate Control Business. Our other sales are generally unsecured. Credit is extended to customers based on an evaluation of the customer's financial condition and other factors. Concentrations of credit risk with respect to trade receivables (primarily relating to the Climate Control Business) are limited due to the large number of customers

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comprising our customer bases and their dispersion across many different industries and geographic areas, however, ten customers (including their affiliates) account for approximately 30% of our total net receivables at December 31, 2010. We do not believe this concentration in these ten customers represents a significant credit risk due to the financial stability of these customers. At December 31, 2010 and 2009, our allowance for doubtful accounts of \$636,000 and \$676,000, respectively, were netted against our accounts receivable. For 2010, 2009, and 2008, our provision for losses on accounts receivable was \$145,000, \$90,000, and \$371,000, respectively.

Inventories - Inventories are stated at the lower of cost (determined using the first-in, first-out ("FIFO") basis) or market (net realizable value). Finished goods and work-in-process inventories include material, labor, and manufacturing overhead costs. Additionally, we review inventories and record inventory reserves for slow-moving inventory items. At December 31, 2010 and 2009, the carrying value of certain nitrogen-based inventories produced by our Chemical Business was reduced to market because cost exceeded the net realizable value by \$0.2 million and \$0.5 million, respectively. In addition, the carrying value of certain slow-moving inventory items (Climate Control products) was reduced to market because cost exceeded the net realizable value by \$1.6 million and \$1.2 million at December 31, 2010 and 2009, respectively. For 2010, 2009, and 2008, our provision for (realization of) losses on inventory was \$0.2 million, \$(2.4 million), and \$3.8 million, respectively.

Precious Metals - Precious metals are used as a catalyst in the Chemical Business manufacturing process. Precious metals are carried at cost, with cost being determined using the FIFO basis. As of December 31, 2010 and 2009, precious metals were \$12.0 million and \$13.1 million, respectively, and are included in supplies, prepaid items and other in the consolidated balance sheets. Because some of the catalyst consumed in the production process cannot be readily recovered and the amount and timing of recoveries are not predictable, we follow the practice of expensing precious metals as they are consumed. For 2010, 2009, and 2008, the amounts expensed for precious metals were approximately \$6.6 million, \$5.9 million and \$7.8 million, respectively. These precious metals expenses are included in cost of sales. Occasionally, during major maintenance or capital projects, we may be able to perform procedures to recover precious metals (previously expensed) which have accumulated over time within the manufacturing equipment. For 2010, 2009, and 2008, we recognized recoveries of precious metals at historical FIFO costs of approximately \$1.3 million, \$2.6 million and \$1.5 million, respectively. When we accumulate precious metals in excess of our production requirements, we may sell a portion of the excess metals. We recognized gains of \$0.1 million for 2010 (none in 2009 or 2008) from the sale of excess precious metals. These recoveries and gains are reductions to cost of sales.

Impairment of Long-Lived Assets and Goodwill - Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of our asset (asset group) may not be recoverable and goodwill is reviewed for impairment at least annually. For long-lived assets, an impairment loss would be recognized when the carrying amount of an asset (asset group) exceeds the estimated undiscounted future cash flows expected to result from the use of the asset (asset group) and its eventual disposition. For goodwill, an impairment loss generally would be recognized when the carrying amount of the reporting unit's net assets exceeds the estimated fair value of the reporting unit. Reporting units are one level below the business segment level. If assets to be held and used are considered to be impaired, the impairment to be recognized is the amount by which the carrying amounts of the assets exceed the fair values of the assets as measured by the present value of future net cash flows expected to be generated by the assets or their appraised value. In general, assets held for sale are reported at the lower of the carrying amounts of the assets or fair values less costs to sell. At December 31, 2010, we had no long-lived assets classified as assets held for sale. We have considered impairment of our long-lived assets and goodwill. The timing of impairments cannot be predicted with reasonable certainty and are primarily dependent on market conditions outside our control. Should sales prices permanently decline dramatically without a similar decline in the raw material costs or should other matters, including the environmental requirements and/or operating requirements set by Federal and State agencies change substantially from our current expectations, a provision for impairment may be required based upon such event or events. See Item 1 "Business-Environmental Matters." Based on estimates obtained from external

sources and internal estimates based on inquiry and other techniques, we recognized an impairment relating to certain non-core equipment of \$0.2 million relating to Corporate assets during 2008 (none in 2010 and 2009). This impairment is included in other expense.

Accrued Insurance Liabilities - We are self-insured up to certain limits for group health, workers' compensation and general liability claims. Above these limits, we have commercial stop-loss insurance coverage for our contractual exposure on group health claims and statutory limits under workers' compensation obligations. We

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also carry umbrella insurance of \$75 million for most general liability and auto liability risks. We have a separate \$30 million insurance policy covering pollution liability at our Chemical Business facilities. Additional pollution liability coverage for our other facilities is provided in our general liability and umbrella policies. Our accrued insurance liabilities are based on estimates of claims, which include the reported incurred claims amounts plus the reserves established by our insurance adjustors and/or estimates provided by attorneys handling the claims, if any. In addition, our accrued insurance liabilities include estimates of incurred, but not reported, claims based on historical claims experience. The determination of such claims and the appropriateness of the related liability is periodically reviewed and revised, if needed. Changes in these estimated liabilities are charged to operations. Potential legal fees and other directly related costs associated with insurance claims are not accrued but rather are expensed as incurred. At December 31, 2010 and 2009, our accrued group health and workers' compensation insurance claims were \$2.5 million and \$2.3 million, respectively, and our accrued general liability insurance claims were \$1.2 million and \$1.4 million respectively. These accrued insurance claims are included in accrued and other liabilities. It is reasonably possible that the actual development of claims could be different than our estimates.

Accrued Warranty Costs – Our Climate Control Business sells equipment that has an expected life, under normal circumstances and use, which extends over several years. As such, we provide warranties after equipment shipment/start up covering defects in materials and workmanship.

Our accounting policy and methodology for warranty arrangements is to measure and recognize the expense and liability for such warranty obligations at the time of sale using a percentage of sales and cost per unit of equipment, based upon our historical and estimated future warranty costs. We also recognize the additional warranty expense and liability to cover atypical costs associated with a specific product, or component thereof, or project installation, when such costs are probable and reasonably estimable. It is reasonably possible that our estimated accrued warranty costs could change in the near term.

Generally for commercial/institutional products, the base warranty coverage for most of the manufactured equipment in the Climate Control Business is limited to eighteen months from the date of shipment or twelve months from the date of start up, whichever is shorter, and to ninety days for spare parts. For residential products, the base warranty coverage for manufactured equipment in the Climate Control Business is limited to ten years from the date of shipment for material and to five years from the date of shipment for labor associated with the repair. The warranty provides that most equipment is required to be returned to the factory or an authorized representative and the warranty is limited to the repair and replacement of the defective product, with a maximum warranty of the refund of the purchase price. Furthermore, companies within the Climate Control Business generally disclaim and exclude warranties related to merchantability or fitness for any particular purpose and disclaim and exclude any liability for consequential or incidental damages. In some cases, the customer may purchase or a specific product may be sold with an extended warranty. The above discussion is generally applicable to such extended warranties, but variations do occur depending upon specific contractual obligations, certain system components, and local laws.

At December 31, 2010 and 2009, our accrued product warranty obligations were \$4.0 million and \$3.1 million, respectively and are included in current and noncurrent accrued and other liabilities in the consolidated balance sheets. For 2010, 2009, and 2008, our warranty expense was \$4.5 million, \$5.3 million, and \$5.5 million, respectively.

Executive Benefit Agreements - We have entered into benefit agreements with certain key executives. Costs associated with these individual benefit agreements are accrued based on the estimated remaining service period when such benefits become probable they will be paid. Total costs accrued equal the present value of specified payments to be made after benefits become payable. In 1992, we entered into individual benefit agreements with certain key executives ("1992 Agreements") that provide for annual benefit payments for life (in addition to salary). The liability for these benefits under the 1992 Agreements is \$1.2 million and \$1.1 million as of December 31, 2010 and 2009, respectively, and is included in current and noncurrent accrued and other liabilities in the consolidated balance sheets.

In 1981, we entered into individual death benefit agreements with certain key executives. In addition, as part of the 1992 Agreements, should the executive die prior to attaining the age of 65, we will pay the beneficiary named in the agreement in 120 equal monthly installments aggregating to an amount specified in the agreement. In 2005, we entered into a death benefit agreement with our CEO. As of December 31, 2010 and 2009, the liability for death

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benefits is \$4.1 million and \$3.4 million, respectively, which is included in current and noncurrent accrued and noncurrent liabilities in the consolidated balance sheets.

Income Taxes - We recognize deferred tax assets and liabilities for the expected future tax consequences attributable to NOL carryforwards, tax credit carryforwards, and differences between the financial statement carrying amounts and the tax basis of our assets and liabilities. We establish valuation allowances if we believe it is more-likely-than-not that some or all of deferred tax assets will not be realized. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

In addition, we do not recognize a tax benefit unless we conclude that it is more-likely-than-not that the benefit will be sustained on audit by the taxing authority based solely on the technical merits of the associated tax position. If the recognition threshold is met, we recognize a tax benefit measured at the largest amount of the tax benefit that, in our judgment, is greater than 50% likely to be realized. We record interest related to unrecognized tax positions in interest expense and penalties in operating other expense.

We reduce income tax expense for investment tax credits in the year the credit arises and is earned.

Contingencies – Certain conditions may exist which may result in a loss, but which will only be resolved when future events occur. We and our legal counsel assess such contingent liabilities, and such assessment inherently involves an exercise of judgment. If the assessment of a contingency indicates that it is probable that a loss has been incurred, we would accrue for such contingent losses when such losses can be reasonably estimated. If the assessment indicates that a potentially material loss contingency is not probable but reasonably possible, or is probable but cannot be estimated, the nature of the contingent liability, together with an estimate of the range of possible loss if determinable and material, would be disclosed. Estimates of potential legal fees and other directly related costs associated with contingencies are not accrued but rather are expensed as incurred. Loss contingency liabilities are included in current and noncurrent accrued and other liabilities and are based on current estimates that may be revised in the near term. In addition, we recognize contingent gains when such gains are realized or realizable and earned. We are a party to various litigation and other contingencies, the ultimate outcome of which is not presently known. Should the ultimate outcome of these contingencies be adverse, such outcome could create an event of default under ThermaClime's Working Capital Revolver Loan and the Secured Term Loan and could adversely impact our liquidity and capital resources.

Regulatory Compliance - Our Chemical Business is subject to specific federal and state regulatory compliance laws and guidelines. We have developed policies and procedures related to regulatory compliance. We must continually monitor whether we have maintained compliance with such laws and regulations and the operating implications, if any, and amount of penalties, fines and assessments that may result from noncompliance. At December 31, 2010, liabilities totaling \$0.2 million have been accrued relating to remediation and surface and groundwater monitoring costs associated with our former Kansas facility and remediation and monitoring costs associated with one of our agricultural distribution centers. These liabilities are included in current accrued and other liabilities and are based on current estimates that may be revised in the near term.

Asset Retirement Obligations - We are obligated to monitor certain discharge water outlets at our Chemical Business facilities should we discontinue the operations of a facility. We also have certain facilities in our Chemical Business that contain asbestos insulation around certain piping and heated surfaces, which we plan to maintain or replace, as needed, with non-asbestos insulation through our standard repair and maintenance activities to prevent deterioration. Since we currently have no plans to discontinue the use of these facilities and the remaining lives of the facilities are indeterminable, an asset retirement liability has not been recognized. Currently, there is insufficient information to

estimate the fair value of the asset retirement obligations. However, we will continue to review these obligations and record a liability when a reasonable estimate of the fair value can be made.

Revenue Recognition - We recognize revenue for substantially all of our operations at the time title to the goods transfers to the buyer and there remain no significant future performance obligations by us. Revenue relating to construction contracts is recognized using the percentage-of-completion method based primarily on contract costs incurred to date compared with total estimated contract costs. Changes to total estimated contract costs or losses, if any, are recognized in the period in which they are determined. Sales of warranty contracts are recognized as

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revenue ratably over the life of the contract. See discussion above under “Accrued Warranty Costs” for our accounting policy for recognizing warranty expense.

Recognition of Insurance Recoveries - If an insurance claim relates to a recovery of our losses, we recognize the recovery when it is probable and reasonably estimable. If our insurance claim relates to a contingent gain, we recognize the recovery when it is realized or realizable and earned. As previously reported and discussed above under “Liquidity and Capital Resources-Recognition of Insurance Recoveries”, we had insurance claims associated with certain of our chemical facilities. At December 31, 2010, there were no insurance claim receivable balances relating to these insurance claims. A notice of an insurance claim for business interruption associated with the Pryor Facility has been filed but the amount has not been determined. A recovery, if any, from our business interruption coverage has not been recognized.

Derivatives, Hedges, Financial Instruments and Carbon Credits - Derivatives are recognized in the balance sheet and are measured at fair value. Changes in fair value of derivatives are recorded in results of operations unless the normal purchase or sale exceptions apply or hedge accounting is elected.

Climate reserve tonnes (“carbon credits”) are recognized in the balance sheet and are measured at fair value. Changes in fair value of carbon credits are recorded in results of operations. Contractual obligations associated with carbon credits are recognized in the balance sheet and are measured at fair value unless we enter into a firm sales commitment to sell the associated carbon credits. When we enter into a firm sales commitment, the sales price, pursuant to the terms of the firm sales commitment, establishes the amount of the associated contractual obligation. Changes in fair value of contractual obligations associated with carbon credits are recorded in results of operations.

We have three classes of contracts that are accounted for on a fair value basis, which are commodities futures/forward contracts (“commodities contracts”), foreign exchange contracts and interest rate contracts. All of these contracts are used as economic hedges for risk management purposes but are not designated as hedging instruments. The valuations of these assets and liabilities were determined based on quoted market prices or, in instances where market quotes are not available, other valuation techniques or models used to estimate fair values.

The valuations of contracts classified as Level 1 are based on quoted prices in active markets for identical contracts. The valuations of contracts classified as Level 2 are based on quoted prices for similar contracts and valuation inputs other than quoted prices that are observable for these contracts. At December 31, 2010, the valuations of contracts classified as Level 2 related to the foreign exchange contracts and interest rate swap contracts. For the foreign exchange contracts, these contracts are valued using the foreign currency exchange rates pursuant to the terms of the contracts and using market information for foreign currency exchange rates. The valuation inputs included the total contractual weighted-average exchange rate of 1.26 and the total estimated market weighted-average exchange rate of 1.34 (U.S. Dollar/Euro). For the foreign exchange contracts and interest rate swap contracts, we utilize valuation software and market data from a third-party provider. These interest rate contracts are valued using a discounted cash flow model that calculates the present value of future cash flows pursuant to the terms of the contracts and using market information for forward interest-rate yield curves. The valuation inputs included the total contractual weighted-average pay rate of 3.42% and the total estimated market weighted-average receive rate of 0.53%. No valuation input adjustments were considered necessary relating to nonperformance risk for the contracts discussed above. The valuations of assets and liabilities classified as Level 3 are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. At December 31, 2010, the valuations (\$3.25 per carbon credit) of the carbon credits and the contractual obligations associated with these carbon credits are classified as Level 3 and are based on the range of ask/bid prices (\$3.00 to \$5.00) per carbon credit obtained from a broker involved in this low volume market, pricing terms included in a sales agreement being negotiated at December 31, 2010, and inquiries from market participants concerning our listed ask price through a broker. The valuations are using undiscounted cash flows based on management’s assumption that the carbon credits

would be sold and the associated contractual obligations would be extinguished in the near term. In addition, no valuation input adjustments were considered necessary relating to nonperformance risk for the carbon credits and associated contractual obligations. At December 31, 2009, there were no valuations of contracts classified at Level 3.

Management's judgment and estimates in these areas are based on information available from internal and external resources at that time. Actual results could differ materially from these estimates and judgments, as additional information becomes known.

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Performance and Payment Bonds

We are contingently liable to sureties in respect of certain insurance bonds issued by the sureties in connection with certain contracts entered into by certain subsidiaries in the normal course of business. These insurance bonds primarily represent guarantees of future performance of certain subsidiaries. As of December 31, 2010, we have agreed to indemnify the sureties for payments, up to \$9.8 million, made by them in respect of such bonds. All of these insurances bonds are expected to expire or be renewed in 2011.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements as defined in Item 303(a)(4)(ii) of Regulation S-K under the Securities Exchange Act of 1934, as amended, except for the following, which was released during 2010:

Cepolk Holdings, Inc. (“CHI”), a subsidiary within the Climate Control Business, is a limited partner and has a 50% equity interest in Cepolk Limited Partnership (“Partnership”), which is accounted for on the equity method. The Partnership owns an energy savings project located at the Ft. Polk Army base in Louisiana (“Project”). During September 2010, the Partnership repaid its indebtedness to a term lender (“Term Lender”) of the Project. CHI had entered into a non-recourse guaranty of the partnership’s indebtedness to the Term Lender and had pledged its limited partnership interest in the Partnership to the Term Lender. As a result of the Partnership repaying in full its indebtedness to the Term Lender, the asset pledged by CHI under the non-recourse guaranty has been released and the lien thereon terminated. In accordance with GAAP, no liability was established for this guaranty since it was entered into prior to January 1, 2003.

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Aggregate Contractual Obligations

Our aggregate contractual obligations as of December 31, 2010 are summarized in the following table (1) (2).

Contractual Obligations	Payments Due in the Year Ending December 31, (In Thousands)						
	Total	2011	2012	2013	2014	2015	Thereafter
Long-term debt:							
5.5% Convertible Senior Subordinated Notes	\$ 26,900	\$ -	\$ 26,900	\$ -	\$ -	\$ -	\$ -
Secured Term Loan due 2012	48,773	-	48,773	-	-	-	-
Capital leases	1,211	462	378	335	36	-	-
Other	18,508	1,866	1,972	2,096	2,214	1,688	8,672
Total long-term debt	95,392	2,328	78,023	2,431	2,250	1,688	8,672
Interest payments on long-term debt (3)	11,709	4,332	3,172	940	785	651	1,829
Interest rate contracts (4)	1,895	1,204	691	-	-	-	-
Capital expenditures (5)	3,467	3,467	-	-	-	-	-
Operating leases	21,856	5,255	4,520	3,457	2,619	1,154	4,851
Futures/forward contracts	6,945	6,945	-	-	-	-	-
Contractual obligations - carbon credits (4)	644	644	-	-	-	-	-

