

INNOSPEC INC.

FORM 10-K (Annual Report)

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Address	8310 SOUTH VALLEY HIGHWAY SUITE 350 ENGLEWOOD, CO, 80112
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2018

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 1-13879

INNOSPEC INC.

(Exact name of registrant as specified in its charter)

DELAWARE

State or other jurisdiction of incorporation or organization

**8310 South Valley Highway
Suite 350
Englewood
Colorado**

(Address of principal executive offices)

98-0181725

(I.R.S. Employer Identification No.)

80112

(Zip Code)

Registrant's telephone number, including area code: **(303) 792 5554**

Securities registered pursuant to Section 12(b) of the Act:

Title of each class
N/A

Name of each exchange on which registered
N/A

Securities registered pursuant to Section 12(g) of the Act: **Common stock, par value \$0.01 per share**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).

Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) 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 the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer
Non-accelerated filer
Emerging growth company

Accelerated filer
Smaller reporting company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial standards provided pursuant to Section 13(a) of the Exchange Act.

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 voting and non-voting common equity held by non-affiliates of the registrant as of the most recently completed second fiscal quarter (June 30, 2018) was approximately \$972 million, based on the closing price of the common shares on the NASDAQ on June 30, 2018. Shares of common stock held by each officer and director and by each beneficial owner who owns 5% or more of the outstanding common stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for any other purpose.

As of February 12, 2019, 24,433,701 shares of the registrant's common stock were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of Innospec Inc.'s Proxy Statement for the Annual Meeting of Stockholders to be held on May 8, 2019 are incorporated by reference into Part III of this Form 10-K.

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CAUTIONARY STATEMENT RELATIVE TO FORWARD-LOOKING STATEMENTS

FORWARD-LOOKING STATEMENTS

This Form 10-K contains certain “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical facts included or incorporated herein may constitute forward-looking statements. Such forward-looking statements include statements (covered by words like “expects,” “estimates,” “anticipates,” “may,” “believes,” “feels” or similar words or expressions, for example,) which relate to earnings, growth potential, operating performance, events or developments that we expect or anticipate will or may occur in the future. Although forward-looking statements are believed by management to be reasonable when made, they are subject to certain risks, uncertainties and assumptions, and our actual performance or results may differ materially from these forward-looking statements. You are urged to review our discussion of risks and uncertainties that could cause actual results to differ from forward-looking statements under the heading “Risk Factors.” Innospec undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

PART I

Item 1 Business

When we use the terms “Innospec,” “the Corporation,” “the Company,” “Registrant,” “we,” “us” and “our,” we are referring to Innospec Inc. and its consolidated subsidiaries unless otherwise indicated or the context otherwise requires.

General

Innospec develops, manufactures, blends, markets and supplies specialty chemicals for use as fuel additives, ingredients for personal care, home care, agrochemical, metal extraction and other applications and oilfield chemicals. Our products are sold primarily to oil and gas exploration and production companies, oil refiners, fuel manufacturers and users, formulators of personal care, home care, agrochemical and metal extraction formulations, and other chemical and industrial companies throughout the world. Our Fuel Specialties business helps improve fuel efficiency, boost engine performance and reduce harmful emissions. Our Oilfield Services business supplies drilling, completion and production chemicals which make exploration and production more effective, cost-efficient and environmentally friendly. Our performance chemicals provide effective technology-based solutions for our customers’ processes or products focused in the personal care, home care, agrochemical and metal extraction markets. Our Octane Additives business manufactures a fuel additive for use in automotive gasoline.

Segment Information

The Company reports its financial performance based on the four reportable segments described as follows:

- Fuel Specialties
- Performance Chemicals
- Oilfield Services
- Octane Additives

The Fuel Specialties, Performance Chemicals and Oilfield Services segments operate in markets where we actively seek growth opportunities although their ultimate customers are different. The Octane Additives segment is expected to further decline in the next twelve months as our one remaining refinery customer transitions to unleaded fuel.

For financial information about each of our segments, see Note 3 of the Notes to the Consolidated Financial Statements.

Fuel Specialties

Our Fuel Specialties segment develops, manufactures, blends, markets and supplies a range of specialty chemical products used as additives to a wide range of fuels. These fuel additive

products help improve fuel efficiency, boost engine performance and reduce harmful emissions; and are used in the efficient operation of automotive, marine and aviation engines, power station generators, and heating oil.

The segment has grown organically through our development of new products to address what we believe are the key drivers in demand for fuel additives. These drivers include increased demand for fuel, focus on fuel economy, changing engine technology and legislative developments. We have also devoted substantial resources towards the development of new and improved products that may be used to improve combustion efficiency.

Our customers in this segment include national oil companies, multinational oil companies and fuel retailers.

Performance Chemicals

Our Performance Chemicals segment provides effective technology-based solutions for our customers' processes or products focused in the Personal Care, Home Care, Agrochemical and Metal Extraction markets.

This segment has grown through acquisitions, and the development and marketing of innovative products. The focus for our Performance Chemicals segment is to develop high performance products from its technology base in a number of targeted markets.

Our customers in this segment include large multinational companies, manufacturers of personal care and household products and specialty chemical manufacturers operating in agrochemical, metal extraction and other industrial applications.

Oilfield Services

Our Oilfield Services segment develops and markets products to prevent loss of mud in drilling operations, chemical solutions for fracturing, stimulation and completion operations and products for oil and gas production which aid flow assurance and maintain asset integrity.

This segment has recently been growing strongly, driven by increased customer activity, as the industry recovers from the significant declines of the last two years.

Our customers in this segment include multinational public and independent companies operating currently principally in the Americas.

Octane Additives

Our Octane Additives segment, which we believe is the world's only producer of tetra ethyl lead ("TEL"), comprises sales of TEL for use in automotive gasoline and provides services in respect of environmental remediation. We are continuing to responsibly manage the decline in the demand for TEL for use in automotive gasoline in line with the transition plans to unleaded gasoline for our one remaining refinery customer. Cost improvement measures continue to be taken to respond to declining market demand.

Sales of TEL for use in automotive gasoline are principally made to state-owned refineries located in North Africa. Our environmental remediation business manages the cleanup of redundant TEL facilities as refineries complete the transition to unleaded gasoline.

Strategy

Our strategy is to develop new and improved products and technologies to continue to strengthen and increase our market positions within our Fuel Specialties, Performance Chemicals and Oilfield Services segments. We also actively continue to assess potential strategic acquisitions, partnerships and other opportunities that would enhance and expand our customer offering. We focus on opportunities that would extend our technology base, geographical coverage or product portfolio. We believe that focusing on the Fuel Specialties, Performance Chemicals and Oilfield Services segments, in which the Company has existing experience, expertise and knowledge, provides opportunities for positive returns on investment with reduced operating risk. We also continue to develop our geographical footprint, consistent with the development of global markets.

Geographical Area Information

Financial information with respect to our domestic and foreign operations is contained in Note 3 of the Notes to the Consolidated Financial Statements.

Working Capital

The nature of our customers' businesses generally requires us to hold appropriate amounts of inventory in order to be able to respond quickly to customers' needs. We therefore require corresponding amounts of working capital for normal operations. We do not believe that this is materially different to what our competitors do, with the exception of cetane number improvers, in which case we maintain high enough levels of inventory, as required, to retain our position as market leader in sales of these products.

The purchase of large amounts of certain raw materials across all our segments can create some variations in working capital requirements, but these are planned and managed by the business.

We do not believe that our terms of sale, or purchase, differ markedly from those of our competitors.

Raw Materials and Product Supply

We use a variety of raw materials and chemicals in our manufacturing and blending processes and believe that sources for these are adequate for our current operations. Our major purchases are cetane number improvers, ethylene, various solvents, amines, alcohols, olefin and polyacrylamides.

These purchases account for a substantial portion of the Company's variable manufacturing costs. These materials are, with the exception of ethylene for one of our operations in Germany, readily available from more than one source. Although ethylene is, in theory, available from several sources, it is not permissible to transport ethylene by road in Germany. As a result, we source ethylene via a direct pipeline from a neighboring site, making it effectively a single source. Ethylene is used as a primary raw material in products representing approximately 5% of Innospec's sales.

We use long-term contracts (generally with fixed or formula-based costs) and advance bulk purchases to help ensure availability and continuity of supply, and to manage the risk of cost increases. From time to time, for some raw materials, the risk of cost increases is managed with commodity swaps.

We continue to monitor the situation and adjust our procurement strategies as we deem appropriate. The Company forecasts its raw material requirements substantially in advance, and seeks to build long-term relationships and contractual positions with supply partners to safeguard its raw material positions. In addition, the Company operates an extensive risk management program which seeks to source key raw materials from multiple sources and to develop suitable contingency plans.

Intellectual Property

Our intellectual property, including trademarks, patents and licenses, forms a significant part of the Company's competitive advantage, particularly in the Fuel Specialties, Oilfield Specialties and Performance Chemicals segments. The Company does not, however, consider its business as a whole to be dependent on any one trademark, patent or license.

The Company has a portfolio of trademarks and patents, both granted and in the application stage, covering products and processes in several jurisdictions. The majority of these patents were developed by the Company and, subject to maintenance obligations including the payment of renewal fees, have at least 10 years life remaining.

The trademark "Innospec and the Innospec device" in Classes 1, 2 and 4 of the "International Classification of Goods and Services for the Purposes of the Registration of Marks" are registered in all jurisdictions in which the Company has a significant market presence. The Company also has trademark registrations for certain product names in all jurisdictions in which it has a significant market presence.

We actively protect our inventions, new technologies, and product developments by filing patent applications and maintaining trade secrets. In addition, we vigorously participate in patent opposition proceedings around the world where necessary to secure a technology base free from infringement of our intellectual property.

We have sales contracts with customers in some markets using fixed or formula-based prices, as appropriate, to maintain our gross profits.

Competition

Certain markets in which the Company operates are subject to significant competition. The Company competes on the basis of a number of factors including, but not limited to, product quality and performance, specialized product lines, customer relationships and service, and regulatory expertise.

Fuel Specialties: Within the Fuel Specialties segment, the market is generally characterized by a small number of competitors, none of which hold a dominant position. We consider our competitive edge to be our proven technical development capacity, independence from major oil companies and strong long-term customer relationships.

Performance Chemicals: Within the Performance Chemicals segment we operate in the Personal Care, Home Care, Agrochemical and Metal Extraction markets which are highly fragmented, and the Company experiences substantial competition from a large number of multinational and specialty chemical suppliers in each geographical market. Our competitive position in these markets is based on us supplying a superior, diverse product portfolio which solves particular customer problems or enhances the performance of new or existing products. In a number of specialty chemicals markets, we also supply niche product lines, where we enjoy market-leading positions.

Oilfield Services: Our Oilfield Services segment is very fragmented and although there are a small number of very large competitors, there are also a large number of smaller players focused on specific technologies or regions. Our competitive strength is our proven technology, broad regional coverage and strong customer relationships.

Octane Additives: We believe our Octane Additives segment is the world's only producer of TEL and accordingly is the only supplier of TEL for use in automotive gasoline. The segment therefore competes with marketers of products and processes that provide alternative ways of enhancing octane performance in automotive gasoline.

Research, Development, Testing and Technical Support

Research, product/application development and technical support ("R&D") provide the basis for the growth of our Fuel Specialties, Performance Chemicals and Oilfield Services segments. Accordingly, the Company's R&D activity has been, and will continue to be, focused on the development of new products and formulations. Our R&D department provides technical support for all of our reporting segments. Expenditures to support R&D services were \$33.4 million, \$31.4 million and \$25.4 million in 2018, 2017 and 2016, respectively.

We believe that our proven technical capabilities provide us with a significant competitive advantage. In the last five years, the Fuel Specialties segment has developed new detergents, cold flow improvers, stabilizers, lubricity and combustion improver products, in addition to the introduction of many new cost effective fuel additive packages. This proven technical capability has also been instrumental in enabling us to produce innovative products including Iselux™ and Statsafe®.

Health, Safety and Environmental Matters

We are subject to environmental laws in the countries in which we operate and conduct business. Management believes that the Company is in material compliance with applicable environmental laws and has made the necessary provisions for the continued costs of compliance with environmental laws.

Our principal site giving rise to environmental remediation liabilities is the Octane Additives manufacturing site at Ellesmere Port in the United Kingdom. There are also environmental remediation liabilities on a much smaller scale in respect of our other manufacturing sites in the U.S. and Europe. At Ellesmere Port there is a continuing asset retirement program related to certain manufacturing units that have been closed.

We recognize environmental remediation liabilities when they are probable and costs can be reasonably estimated, and asset retirement obligations when there is a legal obligation and costs can be reasonably estimated. This involves anticipating the program of work and the associated future expected costs, and so involves the exercise of judgment by management. We regularly review the future expected costs of remediation and the current estimate is reflected in Note 12 of the Notes to the Consolidated Financial Statements.

The European Union legislation known as the Registration, Evaluation and Authorization of Chemical Substances Regulations (“REACH”) requires most of the Company’s products to be registered with the European Chemicals Agency. Under this legislation the Company has to demonstrate that its products are appropriate for their intended purposes. During this registration process, the Company incurs expense to test and register its products. The Company estimates that the cost of complying with REACH will be approximately \$3 million over the next three years based on the current regulatory environment. However, should the United Kingdom exit the European Union under certain terms, these costs may increase.

Employees

The Company had approximately 2000 employees in 23 countries as at December 31, 2018.

Available Information

Our corporate web site is www.innospecinc.com. We make available, free of charge, on or through this web site our annual, quarterly and current reports, and any amendments to those reports, as soon as reasonably practicable after electronically filing such material with, or furnishing it to, the U.S. Securities and Exchange Commission (“SEC”).

The Company routinely posts important information for investors on its web site (under Investor Relations). The Company uses this web site as a means of disclosing material, non-public information and for complying with its disclosure obligations under SEC Regulation FD (“Fair Disclosure”). Accordingly, investors should monitor the Investor Relations portion of the Company’s web site, in addition to following the Company’s press releases, SEC filings, public conference calls, presentations and webcasts.

Item 1A Risk Factors

The factors described below represent the principal risks associated with our business.

Trends in oil and gas prices affect the level of exploration, development and production activity of our customers, and the demand for our services and products, which could have a material adverse impact on our business.

Demand for our services and products in our Oilfield Services business is particularly sensitive to the level of exploration, development and production activity of, and the corresponding capital spending by, oil and gas companies. The level of exploration, development and production activity is directly affected by trends in oil and gas prices, which historically have been volatile and are likely to continue to be volatile. Prices for oil and gas are subject to large fluctuations in response to relatively minor changes in the supply of and demand for oil and gas, market uncertainty, and a variety of other economic and political factors that are beyond our control. Even the perception of longer-term lower oil and gas prices by oil and gas companies can similarly reduce or defer major expenditures given the long-term nature of many large-scale development projects. Factors affecting the prices of oil and gas include the level of supply and demand for oil and gas, governmental regulations, including the policies of governments regarding the exploration for and production and development of their oil and gas reserves, weather conditions and natural disasters, worldwide political, military, and economic conditions, the level of oil and gas production by non-OPEC countries and the available excess production capacity within OPEC, the cost of producing and delivering oil and gas and potential acceleration of the development of alternative fuels and engine technologies. Any prolonged reduction in oil and gas prices will depress the immediate levels of exploration, development, and production activity which could have a material adverse impact on our results of operations, financial position and cash flows.

We face risks related to our foreign operations that may adversely affect our business.

We serve global markets and operate in certain countries with political and economic instability, including the Middle East, Northern Africa, Asia-Pacific, Eastern Europe and South American regions. Our international operations are subject to numerous international business risks including, but not limited to, geopolitical and economic conditions, risk of expropriation, import and export restrictions, trade wars, exchange controls, national and regional labor strikes, high or unexpected taxes, government royalties and restrictions on repatriation of earnings or proceeds from liquidated assets of overseas subsidiaries. Any of these could have a material adverse impact on our results of operations, financial position and cash flows.

We are subject to extensive regulation of our international operations that could adversely affect our business and results of operations.

Due to our global operations, we are subject to many laws governing international commercial activity, conduct and relations, including those that prohibit improper payments to government officials, restrict where and with whom we can do business, and limit the products, software

and technology that we can supply to certain countries and customers. These laws include but are not limited to, the U.S. Foreign Corrupt Practices Act and United Kingdom Bribery Act, sanctions and assets control programs administered by the U.S. Department of the Treasury and/or the European Union from time to time, and the U.S. export control laws such as the regulations under the U.S. Export Administration Act, as well as similar laws and regulations in other countries relevant to our business operations. Violations of any of these laws or regulations, which are often complex in their application, may result in criminal or civil penalties that could have a material adverse effect on our results of operations, financial position and cash flows.

We may not be able to consummate, finance or successfully integrate future acquisitions, partnerships or other opportunities into our business, which could hinder our strategy or result in unanticipated expenses and losses.

Part of our strategy is to pursue strategic acquisitions, partnerships and other opportunities to complement and expand our existing business. The success of these transactions depends on our ability to efficiently complete transactions, integrate assets and personnel acquired in these transactions and apply our internal control processes to these acquired businesses. Consummating acquisitions, partnerships or other opportunities and integrating acquisitions involves considerable expense, resources and management time commitments, and our failure to manage these as intended could result in unanticipated expenses and losses. Post-acquisition integration may result in unforeseen difficulties and may deplete significant financial and management resources that could otherwise be available for the ongoing development or expansion of existing operations. Furthermore, we may not realize the benefits of an acquisition in the way we anticipated when we first entered the transaction. Any of these risks could adversely impact our results of operations, financial position and cash flows.

Competition and market conditions may adversely affect our operating results.

In certain markets, our competitors are larger than us and may have greater access to financial, technological and other resources. As a result, competitors may be better able to adapt to changes in conditions in our industries, fluctuations in the costs of raw materials or changes in global economic conditions. Competitors may also be able to introduce new products with enhanced features that may cause a decline in the demand and sales of our products. Consolidation of customers or competitors, or economic problems of customers in our markets could cause a loss of market share for our products, place downward pressure on prices, result in payment delays or non-payment, or declining plant utilization rates. These risks could adversely impact our results of operations, financial position and cash flows.

Political developments may adversely affect our business

On June 23, 2016, the United Kingdom (U.K.) held a referendum in which voters approved an exit from the European Union (E.U.), commonly referred to as “Brexit”. Subsequently, the U.K. parliament passed the European Union (Notification of Withdrawal) Act 2017, which conferred power on the U.K. government to give notice to the European Council, under

Article 50(2) of the Treaty on European Union, of the U.K.'s intention to withdraw from the E.U.. The U.K. submitted this notice to the European Council on March 29, 2017. On November 14, 2018, the U.K. agreed the draft text of a withdrawal agreement with the E.U. and the other E.U. member states have indicated that the E.U. is not open to any renegotiation of this agreement. Though a draft withdrawal agreement has been agreed, this may not be approved by the U.K. Parliament. If this is not agreed and ratified by March 29, 2019 (or such later date as may be agreed between the U.K. and the European Council), the U.K. may be required to withdraw from the E.U. without a withdrawal agreement being in force, (commonly referred to as the "No Deal" scenario). It is currently expected that the U.K. will leave the E.U. on March 29, 2019, although this deadline could be extended if the U.K. Parliament has not approved the draft withdrawal agreement by that time, subject to agreement by all E.U. member states. If the E.U. member states refuse to agree to an extension, it is also possible that the U.K. could revoke and reserve the notice of its intention to withdraw from the E.U. in order to restart another two year period of negotiations rather than withdraw in a No Deal scenario. If the U.K. withdraws from the E.U. and the draft withdrawal agreement is ratified before March 29, 2019, then a transition period will exist until December 31 2020, during which businesses in the U.K. will trade on essentially very similar if not the same terms as before and E.U. law will continue to apply in the U.K. while the detailed legal agreement on the future relationship between the U.K. and the E.U. is being negotiated. If a future trading relationship is not agreed between the U.K. and the E.U. before the end of the transition period, or if the U.K. leaves in a No Deal scenario, then there are likely to be greater restrictions on imports and exports between the U.K. and E.U. member states and increased regulatory complexities for businesses trading goods and services between those jurisdictions. For example, during the proposed transition period, goods first lawfully put on the market in the E.U. or in the U.K. prior to the end of the transition period can circulate between the two markets before they reach the end user, but following the end of the transition period or in a No Deal scenario, they may not be able to do so without complying with additional requirements first.

These political developments may adversely impact our results of operations, financial position and cash flows.

We could be adversely affected by technological changes in our industry.

Our ability to maintain or enhance our technological capabilities, develop and market products and applications that meet changing customer requirements, and successfully anticipate or respond to technological changes in a cost effective and timely manner will likely impact our future business success. We compete on a number of fronts including, but not limited to, product quality and performance. In the case of some of our products, our competitors are larger than us and may have greater access to financial, technological and other resources. Technological changes include, but are not limited to, the development of electric and hybrid vehicles, and the subsequent impact on the demand for gasoline and diesel. Our inability to maintain a technological edge, innovate and improve our products could cause a decline in the demand and sales of our products, and adversely impact our results of operations, financial position and cash flows.

Having a small number of significant customers may have a material adverse impact on our results of operations.

Our principal customers are oil and gas exploration and production companies, oil refineries, personal care companies, and other chemical and industrial companies. These industries are characterized by a concentration of a few large participants. The loss of a significant customer, a material reduction in demand by a significant customer or termination or non-renewal of a significant customer contract could adversely impact our results of operations, financial position and cash flows.

Our United Kingdom defined benefit pension plan could adversely impact our financial condition, results of operations and cash flows.

Movements in the underlying plan asset value and Projected Benefit Obligation (“PBO”) of our United Kingdom defined benefit pension plan are dependent on actual return on investments as well as our assumptions in respect of the discount rate, annual member mortality rates, future return on assets and future inflation. A change in any one of these assumptions could impact the plan asset value, PBO and pension credit recognized in the income statement. If future plan investment returns prove insufficient to meet future obligations, or should future obligations increase due to actuarial factors or changes in pension legislation, then we may be required to make additional cash contributions. These events could adversely impact our results of operations, financial position and cash flows.

We may have additional tax liabilities.

We are subject to income and other taxes in the U.S. and other jurisdictions. Tax laws are dynamic and subject to change as new laws are passed and new interpretations of the law are issued or applied. Significant judgment is required in estimating our worldwide provision for income taxes. In the ordinary course of our business, there are many transactions and calculations where the ultimate tax determination is uncertain. Although we believe our tax estimates are reasonable, any final determination pursuant to tax audits and any related litigation could be materially different to what is reflected in our consolidated financial statements. Should any tax authority disagree with our estimates and determine any additional tax liabilities, including interest and penalties for us, this could adversely impact our results of operations, financial position and cashflows.

Our success depends on our management team and other key personnel, the loss of any of whom could disrupt our business operations.

Our future success will depend in substantial part on the continued services of our senior management. The loss of the services of one or more of our key executive personnel could affect implementation of our business plan and result in reduced profitability. Our future success also depends on the continued ability to attract, develop, retain and motivate highly-qualified technical, sales and support staff. We cannot guarantee that we will be able to retain our key personnel or attract or retain qualified personnel in the future. If we are unsuccessful in our efforts in this regard, this could adversely impact our results of operations, financial position and cash flows.

Continuing adverse global economic conditions could materially affect our current and future businesses.

Global economic factors affecting our business include, but are not limited to, geopolitical instability in some markets, miles driven by passenger and commercial vehicles, legislation to control fuel quality, impact of alternative propulsion systems, consumer demand for premium personal care and cosmetic products, and oil and gas drilling and production rates. The availability, cost and terms of credit have been, and may continue to be, adversely affected by the foregoing factors and these circumstances have produced, and may in the future result in, illiquid markets and wider credit spreads, which may make it difficult or more expensive for us to obtain credit. Continuing uncertainties in the U.S. and international markets and economies leading to a decline in business and consumer spending could adversely impact our results of operations, financial position and cash flows.

An information technology system failure may adversely affect our business.

We rely on information technology systems to transact our business. Like other global companies, we have, from time to time, experienced threats to our data and systems. Although we have implemented administrative and technical controls and take protective actions to reduce the risk of cyber incidents and protect our information technology, and we endeavor to modify such procedures as circumstances warrant, such measures may be insufficient to prevent physical and electronic break-ins, cyber-attacks or other security breaches to our computer systems. While to date we have not experienced a material cyber security breach, our systems, processes, software and network still may be vulnerable to internal or external security breaches, computer viruses, malware or other malicious code or cyber-attack, catastrophic events, power interruptions, hardware failures, fire, natural disasters, human error, system failures and disruptions, and other events that could have security consequences. Such an information technology failure or disruption could prevent us from being able to process transactions with our customers, operate our manufacturing facilities, and properly report those transactions in a timely manner. A significant, protracted information technology system failure may result in a material adverse effect on our results of operations, financial position and cash flows.

Decline in our TEL business

The remaining sales of the Octane Additives business are now concentrated on one remaining refinery customer. When this customer chooses to cease using TEL as an octane enhancer then the Company's future operating income and cash flows from operating activities will be materially impacted. While we cannot be certain, it is possible that sales will not continue beyond 2019.

The sales of the AvTel product line are recorded within our Fuel Specialties business. The piston aviation industry has been, and is currently, researching a safe replacement fuel to replace leaded fuel. While we expect that at some point in the future a replacement fuel will be identified, trialed and supplied to the industry, there is no currently agreed replacement. In

addition, there is no clear timescale on the legislation of a replacement product. If a suitable product is identified and the use of leaded fuel is prohibited in piston aviation the Company's future operating income and cash flows from operating activities would be adversely impacted.

We are exposed to fluctuations in foreign currency exchange rates, which may adversely affect our results of operations.

We generate a portion of our revenues and incur some operating costs in currencies other than the U.S. dollar. In addition, the financial position and results of operations of some of our overseas subsidiaries are reported in the relevant local currency and then translated to U.S. dollars at the applicable currency exchange rates for inclusion in our consolidated financial statements. Fluctuations in these currency exchange rates affect the recorded levels of our assets and liabilities, results of operations and cash flows.

The primary exchange rate fluctuation exposures we have are with the European Union euro, British pound sterling and Brazilian real. Exchange rates between these currencies and the U.S. dollar have fluctuated in recent years and may continue to do so. We cannot accurately predict future exchange rate variability among these currencies or relative to the U.S. dollar. While we take steps to manage currency exchange rate exposure, including entering into hedging transactions, we cannot eliminate all exposure to future exchange rate variability. These exchange risks could adversely impact our results of operations, financial position and cash flows.

Sharp and unexpected fluctuations in the cost of our raw materials and energy could adversely affect our profit margins.

We use a variety of raw materials, chemicals and energy in our manufacturing and blending processes. Many of these raw materials are derived from petrochemical-based and vegetable-based feedstocks which can be subject to periods of rapid and significant cost instability. These fluctuations in cost can be caused by political instability in oil producing nations and elsewhere, or other factors influencing global supply and demand of these materials, over which we have little or no control. We use long-term contracts (generally with fixed or formula-based costs) and advance bulk purchases to help ensure availability and continuity of supply, and to manage the risk of cost increases. From time to time, we have entered into hedging arrangements for certain utilities and raw materials, but do not typically enter into hedging arrangements for all raw materials, chemicals or energy costs. If the costs of raw materials, chemicals or energy increase, and we are not able to pass on these cost increases to our customers, then profit margins and cash flows from operating activities would be adversely impacted. If raw material costs increase significantly, then our need for working capital could increase. Any of these risks could adversely impact our results of operations, financial position and cash flows.

A disruption in the supply of raw materials or transportation services would have a material adverse impact on our results of operations.

Although we try to anticipate problems with supplies of raw materials or transportation services by building certain inventories of strategic importance, transport operations are exposed to various risks such as extreme weather conditions, natural disasters, technological problems, work stoppages as well as transportation regulations. If the Company experiences transportation problems, or if there are significant changes in the cost of these services, the Company may not be able to arrange efficient alternatives and timely means to obtain raw materials or ship finished products, which could adversely impact our results of operations, financial position and cash flows.

A high concentration of significant stockholders may have a material adverse impact on our stock price.

Approximately 46% of our common stock is held by four stockholders. A decision by any of these stockholders to sell all or a significant part of its holding, or a sudden or unexpected disposition of our stock, could result in a significant decline in our stock price which could in turn adversely impact our ability to access equity markets which in turn could adversely impact our results of operations, financial position and cash flows.

Failure to protect our intellectual property rights could adversely affect our future performance and cash flows.

Failure to maintain or protect our intellectual property rights may result in the loss of valuable technologies, or us having to pay other companies for infringing on their intellectual property rights. Measures taken by us to protect our intellectual property may be challenged, invalidated, circumvented or rendered unenforceable. We may also face patent infringement claims from our competitors which may result in substantial litigation costs, claims for damages or a tarnishing of our reputation even if we are successful in defending against these claims, which may cause our customers to switch to our competitors. Any of these events could adversely impact our results of operations, financial position and cash flows.

Our products are subject to extensive government scrutiny and regulation.

We are subject to regulation by federal, state, local and foreign government authorities. In some cases, we need government approval of our products, manufacturing processes and facilities before we may sell certain products. Many products are required to be registered with the U.S. Environmental Protection Agency (EPA), with the European Chemicals Agency (ECHA) and with comparable government agencies elsewhere. We are also subject to ongoing reviews of our products, manufacturing processes and facilities by government authorities, and must also produce product data and comply with detailed regulatory requirements.

In order to obtain regulatory approval of certain new products we must, among other things, demonstrate that the product is appropriate and effective for its intended uses, and that we are capable of manufacturing the product in accordance with applicable regulations. This approval process can be costly, time consuming, and subject to unanticipated and significant delays. We

cannot be sure that necessary approvals will be granted on a timely basis or at all. Any delay in obtaining, or any failure to obtain or maintain, these approvals would adversely affect our ability to introduce new products and to generate income from those products. New or stricter laws and regulations may be introduced that could result in additional compliance costs and prevent or inhibit the development, manufacture, distribution and sale of our products. Such outcomes could adversely impact our results of operations, financial position and cash flows.

Legal proceedings and other claims could impose substantial costs on us.

We are from time to time involved in legal proceedings that result from, and are incidental to, the conduct of our business, including employee and product liability claims. Although we maintain insurance to protect us against a variety of claims, if our insurance coverage is not adequate to cover such claims, then we may be required to pay directly for such liabilities. Such outcomes could adversely impact our results of operations, financial position and cash flows.

Environmental liabilities and compliance costs could have a substantial adverse impact on our results of operations.

We operate a number of manufacturing sites and are subject to extensive federal, state, local and foreign environmental, health and safety laws and regulations, including those relating to emissions to the air, discharges to land and water, and the generation, handling, treatment and disposal of hazardous waste and other materials on these sites. We operate under numerous environmental permits and licenses, many of which require periodic notification and renewal, which is not automatic. New or stricter laws and regulations could increase our compliance burden or costs and adversely affect our ability to develop, manufacture, blend, market and supply products.

Our operations, and the operations of prior owners of our sites, pose the risk of environmental contamination which may result in fines or criminal sanctions being imposed or require significant amounts in remediation payments.

We anticipate that certain manufacturing sites may cease production over time and on closure, will require safely decommissioning and some environmental remediation. The extent of our obligations will depend on the future use of the sites that are affected and the environmental laws in effect at the time. We currently have made a decommissioning and remediation provision in our consolidated financial statements based on current known obligations, anticipated plans for sites and existing environmental laws. If there were to be unexpected or unknown contamination at these sites, or future plans for the sites or environmental laws change, then current provisions may prove inadequate, which could adversely impact our results of operations, financial position and cash flows.

The inability of counterparties to meet their contractual obligations could have a substantial adverse impact on our results of operations.

We sell products to oil companies, oil and gas exploration and production companies and chemical companies throughout the world. Credit limits, ongoing credit evaluation and

account monitoring procedures are used to minimize bad debt risk. Collateral is not generally required. We have in place a credit facility with a syndicate of banks. From time to time, we use derivatives, including interest rate swaps, commodity swaps and foreign currency forward exchange contracts, in the normal course of business to manage market risks. We enter into derivative instruments with a diversified group of major financial institutions in order to manage the exposure to non-performance of such instruments.

We remain subject to market and credit risks including the ability of counterparties to meet their contractual obligations and the potential non-performance of counterparties to deliver contracted commodities or services at the contracted price. The inability of counterparties to meet their contractual obligations could have an adverse impact on our results of operations, financial position and cash flows.

The provisions of our term loan and revolving credit facility may restrict our ability to incur additional indebtedness or to otherwise expand our business.

Our term loan and revolving credit facility contains restrictive clauses which may limit our activities, and operational and financial flexibility. We may not be able to borrow under the credit facility if an event of default under the terms of the facility occurs. An event of default under the term loan and credit facility includes a material adverse change to our assets, operations or financial condition, and certain other events. The term loan and revolving credit facility also contains a number of restrictions that limit our ability, among other things, and subject to certain limited exceptions, to incur additional indebtedness, pledge our assets as security, guarantee obligations of third parties, make investments, undergo a merger or consolidation, dispose of assets or materially change our line of business.

In addition, the term loan and revolving credit facility requires us to meet certain financial ratios, including ratios based on net debt to earnings before income tax, depreciation and amortization (“EBITDA”) and net interest expense to EBITDA. Net debt, net interest expense and EBITDA are non-GAAP measures of liquidity defined in the credit facility. Our ability to meet these financial covenants depends upon the future successful operating performance of the business. If we fail to comply with financial covenants, we would be in default under the term loan and revolving credit facility and the maturity of our outstanding debt could be accelerated unless we were able to obtain waivers from our lenders. If we were found to be in default under the term loan and revolving credit facility, it could adversely impact our results of operations, financial position and cash flows.

Our business is subject to the risk of manufacturing disruptions, the occurrence of which would adversely affect our results of operations.

We are subject to hazards which are common to chemical manufacturing, blending, storage, handling and transportation. These hazards include fires, explosions, remediation, chemical spills and the release or discharge of toxic or hazardous substances together with the more generic risks of labor strikes or slowdowns, mechanical failure in scheduled downtime, extreme weather or transportation interruptions. These hazards could result in loss of life,

severe injury, property damage, environmental contamination and temporary or permanent manufacturing cessation. Any of these factors could adversely impact our results of operations, financial position and cash flows.

Domestic or international natural disasters or terrorist attacks may disrupt our operations, decrease the demand for our products or otherwise have an adverse impact on our business.

Chemical related assets, and U.S. corporations such as us, may be at greater risk of future terrorist attacks than other possible targets in the U.S., the United Kingdom and throughout the world. Extraordinary events such as natural disasters may negatively affect local economies, including those of our customers or suppliers. The occurrence and consequences of such events cannot be predicted, but they can adversely impact economic conditions in general and in our specific markets. The resulting damage from such events could include loss of life, severe injury and property damage or site closure. Any of these matters could adversely impact our results of operations, financial position and cash flows.

While Innospec maintains business continuity plans that are intended to allow it to continue operations or mitigate the effects of events that could disrupt its business, Innospec cannot provide assurances that its plans would fully protect it from all such events. In addition, insurance maintained by Innospec to protect against property damage, loss of business and other related consequences resulting from catastrophic events is subject to coverage limitations, depending on the nature of the risk insured. This insurance may not be sufficient to cover all of Innospec's damages or damages to others in the event of a catastrophe. In addition, insurance related to these types of risks may not be available now or, if available, may not be available in the future at commercially reasonable rates.

We may be exposed to certain regulatory and financial risks related to climate change

The outcome of new or potential legislation or regulation in the U.S. and other jurisdictions in which we operate may result in new or additional requirements, additional charges to fund energy efficiency activities, fees or restrictions on certain activities. Compliance with these initiatives may also result in additional costs to us, including, among other things, increased production costs, additional taxes, reduced emission allowances or additional restrictions on production or operations. Any adopted future climate change regulations could also negatively impact our ability to compete with companies situated in areas not subject to such limitations. Even without such regulation, increased public awareness and adverse publicity about potential impacts on climate change emanating from us or our industry could harm us. We may not be able to recover the cost of compliance with new or more stringent laws and regulations, which could adversely affect our business and negatively impact our growth. Furthermore, the potential impacts of climate change and related regulation on our customers are highly uncertain and may adversely affect us.

Item 1B Unresolved Staff Comments

None.

Item 2 Properties

A summary of the Company's principal properties is shown in the following table. Each of these properties is owned by the Company except where otherwise noted:

<i>Location</i>	<i>Reporting Segment</i>	<i>Operations</i>
Englewood, Colorado (1)	Fuel Specialties and Performance Chemicals	Corporate Headquarters Business Teams Sales/Administration
Newark, Delaware (1)	Fuel Specialties	Research & Development
Herne, Germany (1)	Fuel Specialties	Sales/Manufacturing/Administration Research & Development
Vernon, France	Fuel Specialties	Sales/Manufacturing/Administration Research & Development
Moscow, Russia (1)	Fuel Specialties	Sales/Administration
Leuna, Germany	Fuel Specialties	Sales/Manufacturing/Administration Research & Development
Ellesmere Port, United Kingdom	Fuel Specialties, Performance Chemicals and Octane Additives	European Headquarters Business Teams Sales/Manufacturing/Administration Research & Development Fuel Technology Center
Beijing, China (1)	Fuel Specialties and Performance Chemicals	Sales/Administration
Singapore (1)	Fuel Specialties and Performance Chemicals	Asia-Pacific Headquarters Business Teams Sales/Administration
Milan, Italy (1)	Fuel Specialties and Performance Chemicals	Sales/Administration
Rio de Janeiro, Brazil (1)	Fuel Specialties and Performance Chemicals	Sales/Administration
High Point, North Carolina	Performance Chemicals	Manufacturing/Administration Research & Development
Salisbury, North Carolina	Performance Chemicals	Manufacturing/Administration Research & Development
Chatsworth, California (1)	Performance Chemicals	Sales/Manufacturing/Administration
Everberg, Belgium (1)	Performance Chemicals	Sales/Administration/Research & Development
Saint Mihiel, France	Performance Chemicals	Manufacturing/Administration/Research & Development
Castiglione, Italy	Performance Chemicals	Manufacturing/Administration/Research & Development
Barcelona, Spain (1)	Performance Chemicals	Manufacturing/Administration/Research & Development

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<i>Location</i>	<i>Reporting Segment</i>	<i>Operations</i>
Oklahoma City, Oklahoma	Oilfield Services	Sales/Manufacturing/Administration
Midland, Texas	Oilfield Services	Sales/Manufacturing/Administration
Pleasanton, Texas	Oilfield Services	Sales/Manufacturing/Administration
Sugar Land, Texas (1)	Oilfield Services	Sales/Administration/Research & Development
The Woodlands, Houston, Texas (1)	Oilfield Services	Sales/Administration/Research & Development
Williston, North Dakota	Oilfield Services	Sales/Warehouse
Casper, Wyoming (1)	Oilfield Services	Warehouse
Zug, Switzerland (1)	Octane Additives	Sales/Administration

(1) *Leased property*

Manufacturing Capacity

We believe that our plants and supply agreements are sufficient to meet current sales levels. Operating rates of the plants are generally flexible and varied with product mix and normal sales demand swings. We believe that all of our facilities are maintained to appropriate levels and in sufficient operating condition though there remains an ongoing need for maintenance and capital investment.

Item 3 Legal Proceedings

Legal matters

While we are involved from time to time in claims and legal proceedings that result from, and are incidental to, the conduct of our business including business and commercial litigation, employee and product liability claims, there are no material pending legal proceedings to which the Company or any of its subsidiaries is a party, or of which any of their property is subject. It is possible, however, that an adverse resolution of an unexpectedly large number of such individual claims or proceedings could in the aggregate have a material adverse effect on results of operations for a particular year or quarter.

Item 4 Mine Safety Disclosures

Not applicable.

PART II

Item 5 Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Market Information and Holders

The Company’s common stock is listed on the NASDAQ under the symbol “IOSP.” As of February 12, 2019 there were 875 registered holders of the common stock.

Unregistered Sales of Equity Securities

There were no unregistered sales of equity securities during the fourth quarter of 2018.

Issuer Purchases of Equity Securities

During 2018 the Company made no repurchases of our common stock.

On November 3, 2015 the Company announced that its board of directors has authorized a share repurchase program which targets to repurchase up to \$90 million of common stock over a three year period which has now ended. During the year ended December 31, 2018, no shares of our common stock were repurchased by the Company under this share repurchase program.

On November 6, 2018 the Company announced that its board of directors had approved a new share repurchase program for the repurchase of up to \$100 million of Innospec’s common stock over the following three years. During the year ended December 31, 2018, no shares of our common stock were repurchased by the Company under this share repurchase program.

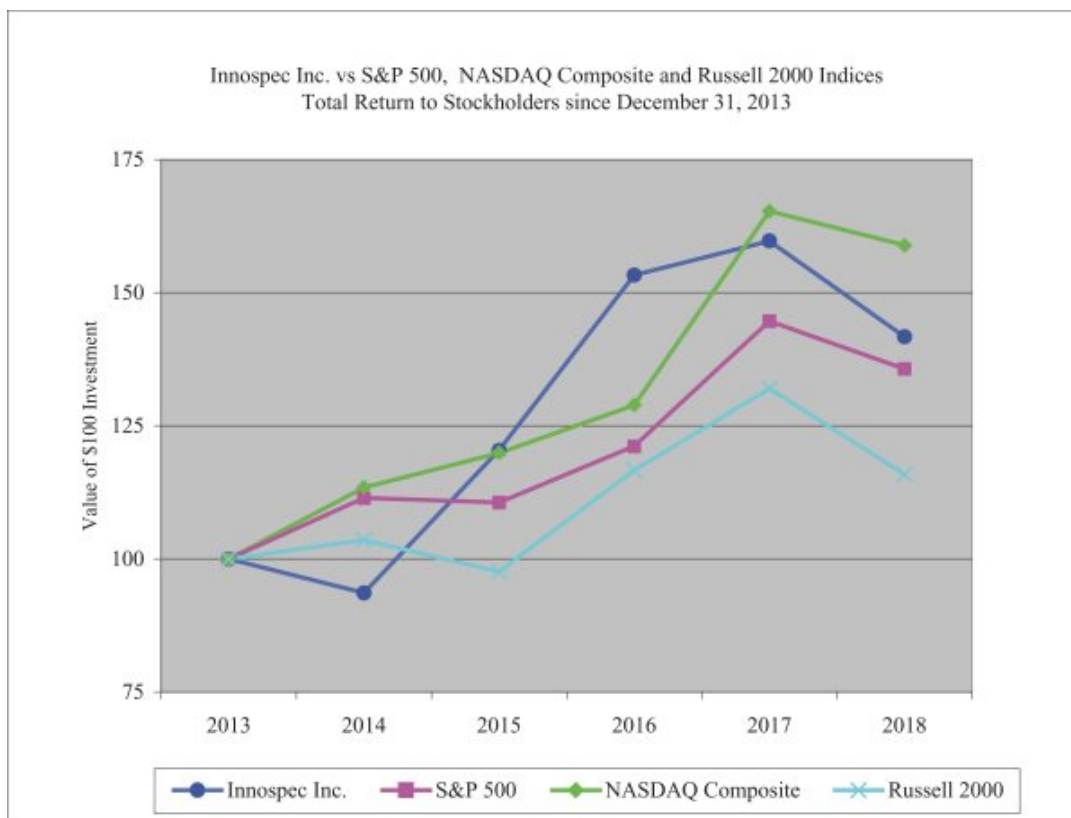
During the quarter ended December 31, 2018 the company has purchased its common stock in connection with the exercising of stock options by employees to satisfy tax withholding obligations. The following table provides information about our repurchases of equity securities in the period.

Issuer Purchases of Equity Securities

<u>Period</u>	<u>Total number of shares purchased</u>	<u>Average price paid per share</u>
November 1, 2018 through November 30, 2018	2,820	\$ 74.57
Total	2,820	\$ 74.57

Stock Price Performance Graph

The graph below compares the cumulative total return to stockholders on the common stock of the Corporation, S&P 500 Index, NASDAQ Composite Index and Russell 2000 Index since December 31, 2013, assuming a \$100 investment and the re-investment of any dividends thereafter.



Value of \$100 Investment made December 31, 2013*

	2013	2014	2015	2016	2017	2018
Innospec Inc.	\$ 100.00	\$ 93.57	\$ 120.35	\$ 153.28	\$ 159.71	\$ 141.72
S&P 500 Index	100.00	111.39	110.58	121.13	144.65	135.63
NASDAQ Composite Index	100.00	113.40	119.89	128.89	165.29	158.87
Russell 2000 Index	\$ 100.00	\$ 103.53	\$ 97.62	\$ 116.63	\$ 131.96	\$ 115.89

* Excludes purchase commissions.

Item 6 Selected Financial Data

FINANCIAL HIGHLIGHTS

(in millions, except financial ratios, share and per share data)

	2018	2017	2016	2015	2014
Summary of performance:					
Net sales	\$1,476.9	\$1,306.8	\$ 883.4	\$1,012.3	\$ 960.9
Operating income	133.5	125.0	98.2	156.3	112.5
Income before income taxes	131.6	128.1	103.1	152.3	110.9
Income taxes	(46.6)	(66.3)	(21.8)	(32.8)	(26.8)
Net income	85.0	61.8	81.3	119.5	84.1
Net income attributable to Innospec Inc.	85.0	61.8	81.3	119.5	84.1
Net cash provided by operating activities	\$ 104.9	\$ 82.7	\$ 105.5	\$ 118.2	\$ 106.3
Financial position at year end:					
Total assets	\$1,473.4	\$1,410.2	\$1,181.4	\$1,028.6	\$ 999.9
Long-term debt including finance leases (including current portion)	210.9	224.3	273.3	134.7	140.5
Cash, cash equivalents, and short-term investments	123.1	90.2	101.9	141.7	46.3
Total equity	\$ 825.5	\$ 794.3	\$ 653.8	\$ 605.3	\$ 515.9
Financial ratios:					
Net income attributable to Innospec Inc. as a percentage of net sales	5.8	4.7	9.2	11.8	8.8
Effective tax rate as a percentage (1)	35.4	51.8	21.1	21.5	24.2
Current ratio (2)	2.2	2.1	2.4	2.2	1.9
Share data:					
Earnings per share attributable to Innospec Inc.					
– Basic	\$ 3.48	\$ 2.56	\$ 3.39	\$ 4.96	\$ 3.45
– Diluted	\$ 3.45	\$ 2.52	\$ 3.33	\$ 4.86	\$ 3.38
Dividend paid per share	\$ 0.89	\$ 0.77	\$ 0.67	\$ 0.61	\$ 0.55
Shares outstanding (basic, thousands)					
– At year end	24,434	24,350	24,071	24,101	24,291
– Average during year	24,401	24,148	23,998	24,107	24,391
Closing stock price					
– High	\$ 82.70	\$ 73.25	\$ 72.75	\$ 58.70	\$ 46.03
– Low	\$ 57.78	\$ 54.25	\$ 42.45	\$ 39.47	\$ 35.55
– At year end	\$ 61.76	\$ 70.60	\$ 68.50	\$ 54.31	\$ 42.70

(1) The effective tax rate is calculated as income taxes as a percentage of income before income taxes. Income taxes are impacted in 2017 by the provisional estimates recorded in respect of the Tax Act, and in 2018 by the finalization and recording of additional taxes due as a consequence of the Tax Act.

(2) Current ratio is defined as current assets divided by current liabilities.

QUARTERLY SUMMARY

<u>(in millions, except per share data)</u>	<u>First Quarter</u>	<u>Second Quarter</u>	<u>Third Quarter</u>	<u>Fourth Quarter</u>
2018				
Net sales	\$ 360.7	\$ 358.1	\$ 363.1	\$ 395.0
Gross profit	104.5	102.8	111.0	116.7
Operating income	28.9	28.3	33.4	42.9
Net income (1)	22.2	21.8	20.6	20.4
Net cash (used in)/provided by operating activities	\$ (2.0)	\$ 0.3	\$ 35.1	\$ 71.5
Per common share:				
Earnings – basic	\$ 0.91	\$ 0.89	\$ 0.84	\$ 0.84
– diluted	\$ 0.90	\$ 0.89	\$ 0.84	\$ 0.83
2017				
Net sales	\$ 294.3	\$ 326.3	\$ 332.4	\$ 353.8
Gross profit	90.9	105.1	98.8	108.5
Operating income	25.3	33.5	29.0	37.2
Net income/(loss) (2)	17.2	26.1	23.3	(4.8)
Net cash (used in)/provided by operating activities	\$ (19.9)	\$ (10.9)	\$ 35.2	\$ 78.3
Per common share:				
Earnings – basic	\$ 0.71	\$ 1.08	\$ 0.97	\$ (0.20)
– diluted	\$ 0.70	\$ 1.06	\$ 0.95	\$ (0.20)

NOTES

- (1) Net income includes the following special items, before tax except for the adjustment of unrecognized tax benefits, during the year ended December 31, 2018:

<u>(in millions)</u>	<u>First Quarter</u>	<u>Second Quarter</u>	<u>Third Quarter</u>	<u>Fourth Quarter</u>
2018				
US Tax Cuts and Jobs Act 2017	\$ 0.0	\$ 0.0	\$ 0.0	\$ 12.3
Restructuring charge	0.0	0.0	4.8	2.3
Amortization of acquired intangible assets	4.6	4.8	4.7	4.7
Adjustment of unrecognized tax benefits	0.0	0.0	(0.6)	1.1
Foreign currency exchange (gains)/losses	(1.0)	(1.6)	2.5	0.7
Acquisition related costs	\$ 0.0	\$ 0.0	\$ 0.0	\$ 0.7

- (2) Net income includes the following special items, before tax except for the adjustment of unrecognized tax benefits, during the year ended December 31, 2017

<u>(in millions)</u>	<u>First Quarter</u>	<u>Second Quarter</u>	<u>Third Quarter</u>	<u>Fourth Quarter</u>
2017				
US Tax Cuts and Jobs Act 2017	\$ 0.0	\$ 0.0	\$ 0.0	\$ 40.6
Amortization of acquired intangible assets	5.1	5.0	5.0	5.5
Adjustment of unrecognized tax benefits	0.0	0.0	(0.5)	0.0
Loss/(gain) on disposal of subsidiary	0.0	1.0	0.0	(0.1)
Foreign currency exchange losses/(gains)	1.0	(2.1)	(1.8)	(3.7)
Foreign exchange loss on liquidation of subsidiary	1.8	0.0	0.0	0.0
Fair value acquisition accounting	\$ 1.7	\$ 0.0	\$ 0.0	\$ 0.0

Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations

This discussion should be read in conjunction with our consolidated financial statements and the notes thereto.

EXECUTIVE OVERVIEW

In 2018, the strategy to focus on the organic growth of our portfolio and build on the integration of our major acquisition delivered in line with our expectations. Sales revenue grew in all strategic business units. New product development and customer adoption of a strong product portfolio helped to drive this revenue growth in both Fuel Specialties and Performance Chemicals.

In Oilfield Services, the business grew as it acquired more customers and improved profitability, reflecting the strength of the market, augmented by the acquisition of BioSuite LLC in May 2018.

Octane Additives continued to supply the one remaining customer in motor gasoline, albeit at reduced levels, consistent with the customer's transition to unleaded fuel.

CRITICAL ACCOUNTING ESTIMATES

Note 2 of the Notes to the Consolidated Financial Statements includes a summary of the significant accounting policies and methods used in the preparation of the consolidated financial statements.

Business combinations

The acquisition method of accounting requires that we recognize the assets acquired and liabilities assumed at their acquisition date fair values. Goodwill is measured as the excess of consideration transferred over the acquisition date net fair values of the assets acquired and the liabilities assumed.

The measurement of the fair values of assets acquired and liabilities assumed requires considerable judgment. Although independent appraisals may be used to assist in the determination of the fair values of certain assets and liabilities, those determinations are usually based on significant estimates provided by management, such as forecast revenue or profit. In determining the fair value of intangible assets, an income approach is generally used and may incorporate the use of a discounted cash flow method. In applying the discounted cash flow method, the estimated future cash flows and residual values for each intangible asset are discounted to a present value using a discount rate appropriate to the business being acquired. These cash flow projections are based on management's estimates of economic and market conditions including revenue growth rates, operating margins, capital expenditures and working capital requirements.

While we use our best estimates and assumptions as part of the process to value assets acquired and liabilities assumed at the acquisition date and contingent consideration at each balance sheet reporting date, our estimates are inherently uncertain and subject to refinement. During the measurement period, which occurs before finalization of the purchase price allocation, changes in assumptions and estimates based on new information that was not previously available, that result in adjustments to the fair values of assets acquired and liabilities assumed will have a corresponding offset to goodwill. Subsequent adjustments will impact our consolidated statements of income.

Environmental Liabilities

We are subject to environmental laws in the countries in which we conduct business. Our principal site giving rise to environmental remediation liabilities is the Octane Additives manufacturing site at Ellesmere Port in the United Kingdom. There are also environmental remediation liabilities on a much smaller scale in respect of our other manufacturing sites in the U.S. and Europe. At Ellesmere Port there is a continuing asset retirement program related to certain manufacturing units that have been closed.

Remediation provisions at December 31, 2018 amounted to \$49.5 million and relate principally to our Ellesmere Port site in the United Kingdom. We recognize environmental liabilities when they are probable and costs can be reasonably estimated, and asset retirement obligations when there is a legal obligation and costs can be reasonably estimated. The Company has to anticipate the program of work required and the associated future expected costs, and comply with environmental legislation in the countries in which it operates or has operated in. The Company views the costs of vacating our Ellesmere Port site as contingent upon if and when it vacates the site because there is no present intention to do so.

Income Taxes

We are subject to income and other taxes in the U.S. and other jurisdictions. Tax laws are dynamic and subject to change as new laws are passed and new interpretations of the law are issued or applied.

The calculation of our tax liabilities involves evaluating uncertainties in the application of accounting principles and complex tax regulations. We recognize liabilities for anticipated tax audit issues based on our estimate of whether, and the extent to which, additional taxes will be required. If we ultimately determine that payment of these amounts is unnecessary, we reverse the liability and recognize a tax benefit during the period in which we determine that the liability is no longer necessary.

We also recognize tax benefits to the extent that it is more likely than not that our positions will be sustained, based on technical merits of the position, when challenged by the taxing authorities. To the extent that we prevail in matters for which liabilities have been established, or are required to pay amounts in excess of our liabilities, our effective tax rate in a given period may be materially affected. An unfavourable tax settlement may require cash payments and result in an increase in our effective tax rate in the year of resolution. We report interest

and penalties related to uncertain tax positions as income taxes. For additional information regarding uncertain income tax positions, see Note 10 of the Notes to the Consolidated Financial Statements.

On December 22, 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (the “Tax Act”). The Tax Act makes broad and complex changes to the U.S. tax code, including, but not limited to, (1) reducing the U.S. federal corporate tax rate from 35 per cent to 21 per cent; (2) requiring companies to pay a one-time transition tax on certain unrepatriated earnings of foreign subsidiaries; (3) generally eliminating U.S. federal income taxes on dividends from foreign subsidiaries; (4) requiring a current inclusion in U.S. federal taxable income of certain earnings of controlled foreign corporations; (5) creating a new limitation on deductible interest expense; and (6) changing rules related to uses and limitations of NOL carry forwards created in tax years beginning after December 31, 2017.

On December 22, 2017, the SEC staff issued Staff Accounting Bulletin No. 118 (“SAB 118”), which provides guidance on accounting for the tax effects of the Tax Act. SAB 118 provided a measurement period that was not to extend beyond one year from the Tax Act enactment date for companies to complete their accounting under ASC 740, *Income Taxes*. As a result of the Tax Act, we recorded provisional amounts in relation to the accounting of the transition tax in 2017. At December 31, 2018, we consider the accounting of the transition tax and other items as further disclosed in Note 10 to now be complete.

Pensions

The Company maintains a defined benefit pension plan covering a number of its current and former employees in the United Kingdom. The Company also has other much smaller pension arrangements in the U.S. and overseas, but the obligations under those plans are not material. The United Kingdom plan is closed to future service accrual, but has a large number of deferred and current pensioners.

Movements in the underlying plan asset value and Projected Benefit Obligation (“PBO”) are dependent on actual return on investments as well as our assumptions in respect of the discount rate, annual member mortality rates, future return on assets and future inflation. A change in any one of these assumptions could impact the plan asset value, PBO and pension charge recognized in the income statement. Such changes could adversely impact our results of operations and financial position. For example, a 0.25% change in the discount rate assumption would change the PBO by approximately \$21 million while the net pension credit for 2019 would change by approximately \$0.5 million. A 0.25% change in the level of price inflation assumption would change the PBO by approximately \$14 million and the net pension credit for 2019 would change by approximately \$0.6 million.

Further information is provided in Note 9 of the Notes to the Consolidated Financial Statements.

Goodwill

The Company's reporting units, the level at which goodwill is assessed for potential impairment, are consistent with the reportable segments. The components in each segment (including products, markets and competitors) have similar economic characteristics and the segments, therefore, reflect the lowest level at which operations and cash flows can be sufficiently distinguished, operationally and for financial reporting purposes, from the rest of the Company.

Initially the Company performs a qualitative assessment to determine whether it is more likely than not that the fair value of a segment is less than the carrying amount prior to performing the two-step goodwill impairment test. If a two-step test is required we assess the fair value based on projected post-tax cash flows discounted at the Company's weighted average cost of capital.

At December 31, 2018 we had \$364.9 million of goodwill relating to our Fuel Specialties, Performance Chemicals and Oilfield Services segments. Our impairment assessment concluded that there had been no impairment of goodwill in respect of those reporting segments.

While we believe our assumptions for impairment assessments are reasonable, they are subjective judgments, and it is possible that variations in any of the assumptions may result in materially different calculations of any potential impairment charges.

Property, Plant and Equipment and Other Intangible Assets (Net of Depreciation and Amortization, respectively)

As at December 31, 2018 we had \$196.4 million of property, plant and equipment and \$136.3 million of other intangible assets (net of depreciation and amortization, respectively), that are discussed in Notes 6 and 8 of the Notes to the Consolidated Financial Statements, respectively. These long-lived assets relate to all of our reporting segments and are being amortized or depreciated straight-line over periods of up to 17 years in respect of the other intangible assets and up to 25 years in respect of the property, plant and equipment.

We continually assess the markets and products related to these long-lived assets, as well as their specific carrying values, and have concluded that these carrying values, and amortization and depreciation periods, remain appropriate.

We also test these long-lived assets for any potential impairment when events occur or circumstances change which suggests that impairment may have occurred. These types of events or changes in circumstances could include, but are not limited to:

- introduction of new products with enhanced features by our competitors;
- loss of, material reduction in purchases by, or non-renewal of a contract by a significant customer;

- prolonged decline in business or consumer spending;
- sharp and unexpected rise in raw material, chemical or energy costs; and
- new laws or regulations inhibiting the development, manufacture, distribution or sale of our products.

In order to facilitate this testing the Company groups together assets at the lowest possible level for which cash flow information is available. Undiscounted future cash flows expected to result from the asset groups are compared with the carrying value of the assets and, if such cash flows are lower, an impairment loss may be recognized. The amount of the impairment loss is the difference between the fair value and the carrying value of the assets. Fair values are determined using post-tax cash flows discounted at the Company's weighted average cost of capital. If events occur or circumstances change it may cause a reduction in periods over which these long-lived assets are amortized or depreciated, or result in a non-cash impairment of a portion of their carrying value. A reduction in amortization or depreciation periods would have no effect on cash flows.

RESULTS OF OPERATIONS

The following table provides operating income by reporting segment:

(in millions)	2018	2017	2016
Net sales:			
Fuel Specialties	\$ 574.5	\$ 523.8	\$ 509.6
Performance Chemicals	468.1	419.5	138.7
Oilfield Services	400.6	304.4	191.7
Octane Additives	33.7	59.1	43.4
	<u>\$1,476.9</u>	<u>\$1,306.8</u>	<u>\$ 883.4</u>
Gross profit:			
Fuel Specialties	\$ 195.0	\$ 188.2	\$ 186.4
Performance Chemicals	97.5	75.8	43.4
Oilfield Services	130.4	109.3	76.4
Octane Additives	12.1	30.0	26.1
	<u>\$ 435.0</u>	<u>\$ 403.3</u>	<u>\$ 332.3</u>
Operating income:			
Fuel Specialties	\$ 116.3	\$ 107.7	\$ 111.1
Performance Chemicals	44.7	32.6	16.0
Oilfield Services	22.1	9.5	(4.7)
Octane Additives	9.9	26.7	22.7
Corporate costs	(52.4)	(48.8)	(54.9)
Restructuring charge	(7.1)	0.0	0.0
Adjustment to fair value of contingent consideration	0.0	0.0	9.4
Loss on disposal of subsidiary	0.0	(0.9)	(1.4)
Foreign exchange loss on liquidation of subsidiary	0.0	(1.8)	0.0
Total operating income	<u>\$ 133.5</u>	<u>\$ 125.0</u>	<u>\$ 98.2</u>
Others included in net income:			
Other income, net	\$ 5.0	\$ 11.3	\$ 8.1
Interest expense, net	(6.9)	(8.2)	(3.2)
Income before income taxes	131.6	128.1	103.1
Income taxes	(46.6)	(66.3)	(21.8)
Net income	<u>\$ 85.0</u>	<u>\$ 61.8</u>	<u>\$ 81.3</u>

Results of Operations – Fiscal 2018 compared to Fiscal 2017:

(in millions, except ratios)	2018	2017	Change	
Net sales:				
Fuel Specialties	\$ 574.5	\$ 523.8	\$ 50.7	+10%
Performance Chemicals	468.1	419.5	48.6	+12%
Oilfield Services	400.6	304.4	96.2	+32%
Octane Additives	33.7	59.1	(25.4)	-43%
	<u>\$1,476.9</u>	<u>\$1,306.8</u>	<u>\$170.1</u>	+13%
Gross profit:				
Fuel Specialties	\$ 195.0	\$ 188.2	\$ 6.8	+4%
Performance Chemicals	97.5	75.8	21.7	+29%
Oilfield Services	130.4	109.3	21.1	+19%
Octane Additives	12.1	30.0	(17.9)	-60%
	<u>\$ 435.0</u>	<u>\$ 403.3</u>	<u>\$ 31.7</u>	+8%
Gross margin (%):				
Fuel Specialties	33.9	35.9	-2.0	
Performance Chemicals	20.8	18.1	+2.7	
Oilfield Services	32.6	35.9	-3.3	
Octane Additives	35.9	50.8	-14.9	
Aggregate	29.5	30.9	-1.4	
Operating expenses:				
Fuel Specialties	\$ (78.7)	\$ (80.5)	\$ 1.8	-2%
Performance Chemicals	(52.8)	(43.2)	(9.6)	+22%
Oilfield Services	(108.3)	(99.8)	(8.5)	+9%
Octane Additives	(2.2)	(3.3)	1.1	-33%
Corporate costs	(52.4)	(48.8)	(3.6)	+7%
Restructuring charge	(7.1)	0.0	(7.1)	n/a
Loss on disposal of subsidiary	0.0	(0.9)	0.9	+100%
Foreign exchange loss on liquidation of subsidiary	0.0	(1.8)	1.8	+100%
	<u>\$ (301.5)</u>	<u>\$ (278.3)</u>	<u>\$ (23.2)</u>	-8.3%

We have recast certain prior period amounts to confirm to new accounting standards.

Fuel Specialties

Net sales: the table below details the components which comprise the year on year change in net sales spread across the markets in which we operate:

<u>Change (%)</u>	<u>Americas</u>	<u>EMEA</u>	<u>ASPAC</u>	<u>AvTel</u>	<u>Total</u>
Volume	+15	+3	+1	+1	+7
Price and product mix	+1	0	0	0	0
Exchange rates	0	+6	+1	0	+3
	<u>+16</u>	<u>+9</u>	<u>+2</u>	<u>+1</u>	<u>+10</u>

Volumes in all our regions were higher, driven by increased demand for our products and technology. Price and product mix in the Americas benefited from increased sales of higher margin products. AvTel volumes were higher than the prior year due to variations in the timing and level of demand from customers. EMEA and ASPAC benefited from favorable exchange rate movements year over year, driven by a strengthening of the British pound sterling and the European Union euro against the U.S. dollar.

Gross margin: the year on year decrease of 2.0 percentage points was adversely affected by the mix of product sales when compared to a strong prior year comparative.

Operating expenses: the year on year decrease of \$1.8 million was driven by a reduction in the provisions for doubtful debts and lower accruals for agents' commissions, partly offset by increased other expenses to support the business growth.

Performance Chemicals

Net sales: the table below details the components which comprise the year on year change in net sales spread across the markets in which we operate:

<u>Change (%)</u>	<u>Americas</u>	<u>EMEA</u>	<u>ASPAC</u>	<u>Total</u>
Volume	+14	+4	+9	+7
Price and product mix	+4	0	-1	+1
Exchange rates	0	+5	+2	+4
	<u>+18</u>	<u>+9</u>	<u>+10</u>	<u>+12</u>

Increased demand for our Personal Care products led to significantly higher volumes in the Americas, together with a favorable price and product mix from increased sales of higher margin products. EMEA benefited from higher volumes in both Personal Care and Home Care, while ASPAC volumes were higher due to increased demand for Personal Care being partly offset by lower demand for Home Care. ASPAC was impacted by adverse price and product mix due to lower sales of higher margin products. EMEA and ASPAC benefited from favorable exchange rate movements year over year, driven by a strengthening of the British pound sterling and the European Union euro against the U.S. dollar.

Gross margin: the year on year increase of 2.7 percentage points was driven by the benefit of several improvement projects and favorable manufacturing variances due to higher production volumes.

Operating expenses: the year on year increase of \$9.6 million is due to additional personnel-related expenses to support the business growth, including increased performance-related compensation accruals, together with additional amortization for our new information system platform and the adverse impact of exchange rate movements year over year.

Oilfield Services

Net sales: the year on year increase of \$96.2 million was due to increased customer activity in stimulation and completion, following the rise in crude oil prices in the first nine months of the year. Overall volumes increased by 26 percent year on year, together with a favorable price and product mix of 6 percent.

Gross margin: the year on year decrease of 3.3 percentage points, was due to the mix of sales to customers, adverse raw material pricing and higher transportation and labor costs.

Operating expenses: the year on year increase of \$8.5 million was due to higher selling and technical support expenses required to deliver the increase in customer demand partly offset by a reduction in other expenses. The reduction in other expenses is driven by lower general and administration costs due to effective cost control, together with lower amortization of acquisition related intangible assets as some of the acquired assets have become fully amortized.

Octane Additives

Net sales: decreased by \$25.4 million compared to the prior year, due to the expected reduction in the demand from our one remaining refinery customer.

Gross margin: the year on year decrease of 14.9 percentage points was due to higher manufacturing costs as a result of lower production volumes to align with reduced customer demand.

Operating expenses: the year on year decrease of \$1.1 million was driven by the release of historic provisions which are no longer required, either due to the settlement of disputed liabilities or to the passing of the relevant time limit under statute of limitations.

Other Income Statement Captions

Corporate costs: the year on year increase of \$3.6 million relates to higher personnel-related compensation accruals including a new long-term incentive plan and higher costs for the additional corporate services required to support our enlarged group following our growth through acquisitions in recent years. There has also been the adverse effect of a stronger British pound sterling against the U.S. dollar for our United Kingdom cost base.

Restructuring charge: a charge of \$7.1 million primarily relates to the closure costs including redundancies and onerous leases for our operation in Belgium.

Loss on disposal of subsidiary: there was a loss in the prior year of \$0.9 million for an indemnity claim in relation to residual testing in the Aroma Chemicals business which was sold in 2015.

Foreign exchange loss on liquidation of subsidiary: the \$1.8 million loss in the prior year related to the reclassification of historic foreign exchange translations of net assets from accumulated other comprehensive losses, for our captive insurance company which was liquidated. There has been no corresponding charge in the current year.

Other net income/(expense): for 2018 and 2017, includes the following:

(in millions)	2018	2017	Change
United Kingdom pension credit	\$ 6.3	\$ 5.3	\$ 1.0
German pension charge	(0.6)	(0.6)	0.0
Foreign exchange (losses)/gains on translation	(5.9)	7.5	(13.4)
Foreign currency forward contracts gains/(losses)	5.2	(0.9)	6.1
	<u>\$ 5.0</u>	<u>\$11.3</u>	<u>\$ (6.3)</u>

Interest expense, net: was \$6.9 million in 2018 compared to \$8.2 million in 2017 driven by lower average net debt as the business generated cash inflows.

Income taxes: The effective tax rate was 35.4% and 51.8% in 2018 and 2017, respectively. The adjusted effective tax rate, once adjusted for the items set out in the following table, was 23.7% in 2018 compared with 20.2% in 2017. The Company believes that this adjusted effective tax rate, a non-GAAP financial measure, provides useful information to investors and may assist them in evaluating the Company's underlying performance and identifying operating trends. In addition, management uses this non-GAAP financial measure internally to evaluate the performance of the Company's operations and for planning and forecasting in subsequent periods.

(in millions, except ratios)	2018	2017
Income before income taxes	\$131.6	\$128.1
Adjustment to acquisition accounting for inventory fair valuation	0.0	1.7
Loss on disposal of subsidiary	0.0	0.9
Foreign exchange loss on liquidation of subsidiary	0.0	1.8
Adjustment for stock compensation	4.8	4.0
Indemnification asset regarding tax audit	(1.2)	0.0
Site closure provision	6.8	0.0
	<u>\$142.0</u>	<u>\$136.5</u>
Income taxes	\$ 46.6	\$ 66.3
Adjustment of income tax provisions	(1.8)	0.5
Tax on stock compensation	0.2	3.1
Tax on adjustment to fair value accounting	0.0	0.3
Tax Cuts & Jobs Act 2017 impact	(12.3)	(40.6)
Tax on site closure provision	1.9	0.0
Deduct other discrete items	(0.9)	(2.0)
	<u>\$ 33.7</u>	<u>\$ 27.6</u>
GAAP effective tax rate	<u>35.4%</u>	<u>51.8%</u>
Adjusted effective tax rate	<u>23.7%</u>	<u>20.2%</u>

The most significant factor impacting our effective tax rate in 2018 and 2017 is the recognized implications of the Tax Act.

On December 22, 2017, the U.S. government enacted comprehensive tax legislation, being the Tax Act. On the same date, SEC staff issued Staff Accounting Bulletin No. 118 (“SAB 118”), which provided guidance on accounting for the tax effects of the Tax Act. SAB 118 provides a measurement period that should not extend beyond one year from the Tax Act enactment date for companies to complete their accounting under ASC 740, Income Taxes. Our accounting for the impact of the Tax Act under SAB 118 is now complete.

The deemed repatriation transition tax (“Transition Tax”) is a tax on certain previously untaxed accumulated earnings and profits (“E&P”) of the Company’s non-U.S. subsidiaries. At December 31, 2017, we were able to reasonably estimate the Transition Tax and recorded a provisional Transition Tax obligation of \$47.7 million. On the basis of revised E&P computations that were completed during the reporting period, we adjusted our Transition Tax estimate to \$61.1 million. Net of related consequential impacts recorded in our 2017 U.S. federal income tax return, we have recorded an additional \$12.3 million income tax expense in the fourth quarter. Our accounting in relation to the Transition Tax is now complete.

Further details regarding accounting for the Tax Act and the Transition Tax are given in Note 10 of the Notes to the Consolidated Financial Statements.

Results of Operations – Fiscal 2017 compared to Fiscal 2016:

(in millions, except ratios)	2017	2016	Change	
Net sales:				
Fuel Specialties	\$ 523.8	\$ 509.6	\$ 14.2	+3%
Performance Chemicals	419.5	138.7	280.8	n/a
Oilfield Services	304.4	191.7	112.7	+59%
Octane Additives	59.1	43.4	15.7	+36%
	<u>\$1,306.8</u>	<u>\$ 883.4</u>	<u>\$423.4</u>	+48%
Gross profit:				
Fuel Specialties	\$ 188.2	\$ 186.4	\$ 1.8	+1%
Performance Chemicals	75.8	43.4	32.4	+75%
Oilfield Services	109.3	76.4	32.9	+43%
Octane Additives	30.0	26.1	3.9	+15%
	<u>\$ 403.3</u>	<u>\$ 332.3</u>	<u>\$ 71.0</u>	+21%
Gross margin (%):				
Fuel Specialties	35.9	36.6	-0.7	
Performance Chemicals	18.1	31.3	-13.2	
Oilfield Services	35.9	39.9	-4.0	
Octane Additives	50.8	60.1	-9.3	
Aggregate	30.9	37.6	-6.7	
Operating expenses:				
Fuel Specialties	\$ (80.5)	\$ (75.3)	\$ (5.2)	+7%
Performance Chemicals	(43.2)	(27.4)	(15.8)	+58%
Oilfield Services	(99.8)	(81.1)	(18.7)	+23%
Octane Additives	(3.3)	(3.4)	0.1	-3%
Corporate costs	(48.8)	(54.9)	6.1	-11%
Adjustment to fair value of contingent consideration	0.0	9.4	(9.4)	100%
Loss on disposal of subsidiary	(0.9)	(1.4)	0.5	+36%
Foreign exchange loss on disposal of subsidiary	(1.8)	0.0	(1.8)	n/a
	<u>\$ (278.3)</u>	<u>\$(234.1)</u>	<u>\$ (44.2)</u>	+19%

We have recast certain prior period amounts to confirm to new accounting standards.

Fuel Specialties

Net sales: the table below details the components which comprise the year on year change in net sales spread across the markets in which we operate:

<u>Change (%)</u>	<u>Americas</u>	<u>EMEA</u>	<u>ASPAC</u>	<u>AvTel</u>	<u>Total</u>
Volume	+11	-10	-1	-16	-3
Price and product mix	-6	+11	+6	+7	+5
Exchange rates	0	+2	0	0	+1
	<u>+5</u>	<u>+3</u>	<u>+5</u>	<u>-9</u>	<u>+3</u>

Volumes in the Americas were higher as a result of increased demand following a slower than normal end to 2016. Price and product mix in the Americas was adversely impacted by increased sales of lower margin products. Volumes in EMEA and ASPAC decreased due to customer reformulation to our new technologies. Price and product mix in EMEA and ASPAC benefited from increased sales of higher margin products. AvTel volumes were lower than the prior year due to variations in the timing and level of demand from customers, together with a favorable price mix. EMEA benefited from favorable exchange rate movements year over year, driven by a strengthening of the European Union euro against the U.S. dollar.

Gross margin: the year on year decrease of 0.7 percentage points was adversely impacted by lower sales of higher margin products compared to a strong prior year, partly offset by the benefit of a stronger European Union euro versus the U.S. dollar towards the end of the year.

Operating expenses: the year on year increase of \$5.2 million was driven by \$3.3 million higher selling and administrative expenses and \$1.9 million higher research and development expenses. Higher performance based personnel-related compensation has increased expenses year on year.

Performance Chemicals

Net sales: the table below details the components which comprise the year on year change in net sales spread across the markets in which we operate:

<u>Change (%)</u>	<u>Americas</u>	<u>EMEA</u>	<u>ASPAC</u>	<u>Aroma Chemicals</u>	<u>Total</u>
Volume	+16	+5	+11	0	+13
Disposals	0	0	0	+195	+195
Price and product mix	-8	+4	-7	0	-6
Exchange rates	0	0	-1	0	0
	<u>+8</u>	<u>+9</u>	<u>+3</u>	<u>+195</u>	<u>+202</u>

Excluding the Huntsman acquisition, increased Personal Care demand led to higher volumes in all our markets. Price and product mix in the Americas and ASPAC was adversely affected by pricing pressures in Personal Care, while EMEA benefited from favorable price and

product mix in Personal Care. ASPAC was adversely impacted by exchange rate movements' year over year, driven by a weakening of the British pound sterling against the U.S. dollar. Sales growth from the acquisition of our Huntsman business at the end of 2016 has been excluded from the market analysis above and included as one variance for the segment total.

Gross margin: the year on year decrease of 13.2 percentage points was driven by the dilutive effect of the lower margins for our acquired Huntsman business together with some one-off events for an unplanned plant outage and raw materials purchasing and pricing issues in the second quarter for the acquired business.

Operating expenses: the year on year increase of \$15.8 million is due to \$17.6 million additional expenses within our acquired Huntsman business, partly offset by a reduction in performance based personnel-related compensation and the favorable impact of a \$1.0 million one-off commercial legal settlement in the prior year.

Oilfield Services

Net sales: the year on year increase of \$112.7 million was due to an improvement in customer demand for all our product lines following the rising customer activity as oil prices have recovered. Overall volumes increased by 60 percent year on year, partly offset by an adverse price and product mix of 1 percent.

Gross margin: the year on year decrease of 4.0 percentage points, compared with a strong prior year, is driven by the mix of customer activity and the adverse effect of Hurricane Harvey on raw material prices and availability.

Operating expenses: the year on year increase of \$18.7 million was primarily driven by \$15.3 million higher selling and technical support expenses required to service the increase in customer demand, together with \$1.2 million additional research and development expenses and \$2.2 million higher administration costs to support the business growth.

Octane Additives

Net sales: have increased by \$15.7 million compared to the prior year, due to the phasing of orders from our one remaining refinery customer.

Gross margin: the year on year decrease of 9.3 percentage points was due to lower volumes of production in the current year leading to higher manufacturing costs per tonne.

Operating expenses: the year on year decrease of \$0.1 million was primarily due to a reduction in the provisions for doubtful debts.

Other Income Statement Captions

Corporate costs: the year on year decrease of \$6.1 million related to \$4.4 million non-recurring acquisition-related costs in the prior year for our Huntsman business, partly

offset by \$1.9 million of integration related costs in the current year; together with lower performance based personnel-related compensation and the benefit of the weaker British pound sterling against the U.S. dollar for our Ellesmere Port cost base over the year.

Adjustment to fair value of contingent consideration: in the prior year there was a contingent consideration credit of \$9.4 million related to an acquisition in 2014.

Loss on disposal of subsidiary: the loss of \$0.9 million relates to an indemnity claim in relation to residual testing in the Aroma Chemicals business which was sold in 2015.

Foreign exchange loss on liquidation of subsidiary: the \$1.8 million loss relates to the reclassification of historic foreign exchange translations of net assets from accumulated other comprehensive losses, for our captive insurance company which was liquidated in the first quarter of 2017.

Other net income/(expense): for 2017 and 2016, includes the following:

(in millions)	2017	2016	Change
United Kingdom pension credit	\$ 5.3	\$ 7.6	\$ (2.3)
German pension charge	(0.6)	(0.4)	(0.2)
Foreign exchange gains/(losses) on translation	7.5	(3.5)	11.0
Foreign currency forward contracts (losses)/gains	(0.9)	4.4	(5.3)
	<u>\$11.3</u>	<u>\$ 8.1</u>	<u>\$ 3.2</u>

Interest expense, net: was \$8.2 million in 2017 compared to \$3.2 million in 2016, driven by the additional term loan related to the Huntsman acquisition, increased working capital requirements funded by our credit facility and the recent rise in LIBOR impacting our revolving credit facility borrowing.

Income taxes: The effective tax rate was 51.8% and 21.1% in 2017 and 2016, respectively. The adjusted effective tax rate, once adjusted for the items set out in the following table, was 20.2% in 2017 compared with 22.4% in 2016. The Company believes that this adjusted effective tax rate, a non-GAAP financial measure, provides useful information to investors and may assist them in evaluating the Company's underlying performance and identifying operating trends. In addition, management uses this non-GAAP financial measure internally to evaluate the performance of the Company's operations and for planning and forecasting in subsequent periods.

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(in millions, except ratios)	2017	2016
Income before income taxes	\$128.1	\$103.1
Adjustment to fair value of contingent consideration	0.0	(9.4)
Adjustment to acquisition accounting for inventory fair valuation	1.7	0.0
Loss on disposal of subsidiary	0.9	1.4
Foreign exchange loss on liquidation of subsidiary	1.8	0.0
Adjustment for stock compensation	4.0	0.0
	<u>\$136.5</u>	<u>\$ 95.1</u>
Income taxes	\$ 66.3	\$ 21.8
Adjustment of income tax provisions	0.5	1.6
Tax on adjustments to fair value of contingent consideration	0.0	(3.6)
Tax on stock compensation	3.1	0.0
Tax on adjustment to fair value accounting	0.3	0.0
Tax Cuts & Jobs Act 2017 provisional impact	(40.6)	0.0
(Deduct)/add back other discrete items	(2.0)	1.5
	<u>\$ 27.6</u>	<u>\$ 21.3</u>
GAAP effective tax rate	<u>51.8%</u>	<u>21.1%</u>
Adjusted effective tax rate	<u>20.2%</u>	<u>22.4%</u>

The most significant factor impacting our effective rate is the recognized implications of the Tax Act. As a result of the Act, we accrued a provisional estimate of the mandatory transition tax on our accumulated earnings as of December 31, 2017, resulting in an increase to income tax expense of \$47.7 million. In addition, our U.S. deferred tax assets and liabilities were re-measured from 35% to 21% at the same date, which resulted in \$7.1 million of deferred income tax benefit.

In addition to the factors mentioned above, the mix of taxable profits in the different geographical jurisdictions in which the Group operates continues to have a significant positive impact on the effective tax rate.

The foreign tax rate differential arising from profits being earned in foreign jurisdictions with lower tax rates in 2017 was \$17.5 million (2016 – \$17.1 million). In 2017, the Company’s income tax expense benefited to a greater degree from a proportion of its overall profits arising in Switzerland than in 2016. This resulted in an \$8.2 million benefit in Switzerland (2016 – \$7.8 million). In addition, there was an \$8.3 million benefit in relation to the United Kingdom (2016 – \$8.4 million), a \$0.7 million benefit in relation to Germany (2016 – \$0.5 million), and a \$0.3 million benefit in other jurisdictions (2016 – \$0.3 million benefit).

Foreign income inclusions arise each year from certain types of income earned overseas being taxable under U.S. tax regulations. The Tax Act will substantially change the U.S. taxation of income earned overseas in 2018 and future years. In 2017, income earned overseas and taxable under U.S. regulations includes Subpart F income, principally from foreign based company sales in the United Kingdom, and the associated Section 78 tax gross up, and also

from the income earned by certain overseas subsidiaries taxable under the U.S. tax regime. In 2017, Subpart F income and the associated Section 78 gross up resulted in U.S. taxation of \$7.1 million (2016 – \$5.7 million). Certain overseas subsidiaries taxable under the U.S. tax regime generated taxable income of \$2.4 million (2016 – \$0.2 million loss).

Foreign tax credits can fully or partially offset these incremental U.S. taxes from foreign income inclusions. The utilization of foreign tax credits varies year on year as this is dependent on a number of variable factors which are difficult to predict and may in certain years prevent any offset of foreign tax credits. In total, \$5.6 million of foreign tax credits were utilized during 2017 to offset the incremental U.S. taxes arising from foreign income inclusions in the year, excluding those associated with the one-time mandatory transition tax inclusion (2016 – \$6.1 million), all generated during 2017.

Further details are given in Note 10 of the Notes to the Consolidated Financial Statements.

LIQUIDITY AND FINANCIAL CONDITION

Working Capital

The Company believes that adjusted working capital, a non-GAAP financial measure, provides useful information to investors in evaluating the Company's underlying performance and identifying operating trends. Management uses this non-GAAP financial measure internally to allocate resources and evaluate the performance of the Company's operations. Items excluded from the adjusted working capital calculation are listed in the table below and represent factors which do not fluctuate in line with the day to day working capital needs of the business.

<u>(in millions)</u>	<u>2018</u>	<u>2017</u>
Total current assets	\$ 663.9	\$ 561.5
Total current liabilities	(296.6)	(261.5)
Working capital	367.3	300.0
Less cash and cash equivalents	(123.1)	(90.2)
Less prepaid income taxes	(1.5)	(2.8)
Less other current assets	0.0	(1.1)
Add back current portion of accrued income taxes	8.6	15.8
Add back current portion of long-term debt	21.4	15.8
Add back current portion of finance leases	1.8	2.7
Add back current portion of plant closure provisions	5.9	5.2
Adjusted working capital	<u>\$ 280.4</u>	<u>\$ 245.4</u>

In 2018 our working capital increased by \$67.3 million, while our adjusted working capital has increased by \$35.0 million. The difference is primarily due to the exclusion of cash and cash equivalents from the adjusted working capital measure.

We had a \$35.2 million increase in trade and other accounts receivable. Increased sales in all our segments have increased receivables balances together with higher indirect taxes

receivable in our European businesses. Days' sales outstanding in our Fuel Specialties segment increased from 51 days to 52 days; decreased in our Performance Chemicals segment from 68 days to 65 days; and decreased from 58 days to 56 days in our Oilfield Services segment.

We had a \$38.2 million increase in inventories, which is primarily related to higher inventory in our Oilfield Services businesses to support the strong sales growth. Days' sales in inventory in our Fuel Specialties segment decreased from 100 days to 90 days; increased in our Performance Chemicals segment from 51 days to 59 days; and increased from 63 days to 82 days in our Oilfield Services segment.

Prepaid expenses decreased \$1.5 million, from \$13.1 million to \$11.6 million due to reduced payments in advance and the timing of invoices received.

We had a \$36.9 million increase in accounts payable and accrued liabilities driven by increases in our Fuel Specialties and Oilfield Services segments in line with customer demand. Creditor days in our Fuel Specialties segment decreased from 32 days to 29 days; decreased in our Performance Chemicals segment from 50 days to 49 days; and decreased from 51 days to 48 days in our Oilfield Services segment.

Operating Cash Flows

We generated cash from operating activities of \$104.9 million in 2018 compared to \$82.7 million in 2017. Year over year cash from operating activities has benefitted from the effective control of working capital in all our businesses.

Cash

At December 31, 2018 and 2017, we had cash and cash equivalents of \$123.1 million and \$90.2 million, respectively, of which \$101.4 million and \$74.1 million, respectively, were held by non-U.S. subsidiaries principally in the United Kingdom. The increase in cash and cash equivalents in 2018, has been driven by our strong operating cash flows and the effective control of working capital.

Debt

On December 14, 2016, Innospec and certain subsidiaries of the Company entered into a Third Amendment and Restatement Agreement with various lenders which amends and restates the Company's credit facility agreement dated December 14, 2011, as amended and restated on August 28, 2013 and November 6, 2015 (the "Pre-Existing Credit Agreement;" the Pre-Existing Credit Agreement, as amended and restated pursuant to the Third Amendment and Restatement Agreement, being the "Amended Credit Agreement.")

The Amended Credit Agreement retains the \$200.0 million revolving credit facility available to the Company and adds a term loan facility of \$110.0 million. The termination date of the revolving facility remains November 6, 2020. Repayments for the term loan of \$11.0 million

and \$16.5 million were made on December 29, 2017 and December 28, 2018, respectively. A further installment of \$22.0 million is due on December 28, 2019, with the outstanding balance due on November 6, 2020.

The term loan and credit facility contains terms which, if breached, would result in it becoming repayable on demand. It requires, among other matters, compliance with the following financial covenant ratios measured on a quarterly basis: (1) our ratio of net debt to EBITDA must not be greater than 3.0:1 and (2) our ratio of EBITDA to net interest must not be less than 4.0:1. Management has determined that the Company has not breached these covenants throughout the period to December 31, 2018 and does not expect to breach these covenants for the next 12 months. The credit facility is secured by a number of fixed and floating charges over certain assets which include key operating sites of the Company and its subsidiaries.

The current credit facility contains restrictions which may limit our activities, and operational and financial flexibility. We may not be able to borrow if an event of default is outstanding, which includes a material adverse change to our assets, operations or financial condition. The credit facility contains a number of restrictions that limit our ability, among other things, and subject to certain limited exceptions, to incur additional indebtedness, pledge our assets as security, guarantee obligations of third parties, make investments, effect a merger or consolidation, dispose of assets, or materially change our line of business.

At December 31, 2018, we had \$126.0 million of debt outstanding under the revolving credit facility, \$82.5 million of debt outstanding on our term loan and \$3.3 million of obligations under finance leases relating to certain fixed assets within our Fuel Specialties and Oilfield Services segments.

At December 31, 2018, our maturity profile of long-term debt and finance leases is set out below (net of deferred finance costs capitalized of \$0.9 million):

(in millions)	
2019	\$ 23.2
2020	187.2
2021	0.4
2022	0.1
Total debt	210.9
Current portion of long-term debt and finance leases	(23.2)
Long-term debt and finance leases, net of current portion	<u>\$187.7</u>

The fair value of long-term debt approximates to the carrying value, as the discounting to its present value is offset by the interest rate swaps.

Outlook

2018 was a very positive year for Innospec, which we believe has laid the foundations for future growth. We have met our expectations and generated strong cash flow, further strengthening our balance sheet.

The continued development of new products and technologies for all of our strategic business units has helped grow sales in 2018, but also generated good momentum for what we expect to be further increases in revenue in 2019 and further into the future.

We will maintain our strategic focus, concentrating on our key competencies of technology and customer service. This will require continued investment in new product development.

Market conditions will continue to be challenging in all our strategic businesses, and there will be specific challenges in Oilfield Services if commodity prices soften further. However, we feel confident that we are well placed to continue to deliver profitable growth in our chosen markets.

We anticipate a decline and possible conclusion of revenues from our Octane Additives segment. Although we cannot be definitive, it is possible that sales in this segment will not continue beyond the first half of 2019.

Contractual Commitments

The following represents contractual commitments at December 31, 2018 and the effect of those obligations on future cash flows:

<u>(in millions)</u>	<u>Total</u>	<u>2019</u>	<u>2020-21</u>	<u>2022-23</u>	<u>Thereafter</u>
<u>Operating activities</u>					
Planned funding of pension obligations	\$ 5.0	\$ 1.0	\$ 2.0	\$ 2.0	\$ 0.0
Remediation payments	49.5	5.9	9.9	6.2	27.5
Operating lease commitments	23.0	6.5	7.7	4.4	4.4
Raw material purchase obligations	17.2	8.0	6.6	2.6	0.0
Interest payments on debt	12.3	6.9	5.4	0.0	0.0
<u>Investing activities</u>					
Capital commitments	6.0	6.0	0.0	0.0	0.0
<u>Financing activities</u>					
Long-term debt obligations	207.6	21.4	186.2	0.0	0.0
Finance leases	3.3	1.8	1.4	0.1	0.0
Total	<u>\$323.9</u>	<u>\$57.5</u>	<u>\$219.2</u>	<u>\$ 15.3</u>	<u>\$ 31.9</u>

Operating activities

The amounts related to pension obligations refer to the likely levels of funding of our United Kingdom defined benefit pension plan (the "Plan"). The Plan is closed to future service

accrual, but has a large number of deferred and current pensioners. The Company expects its annual cash contribution to be \$1.0 million in 2019, \$2.0 million in 2020-21 and \$2.0 million in 2022-23. It is not considered meaningful to predict amounts beyond 2023 since there are too many uncertainties including future returns on assets, pension increases and inflation which are evaluated when the plan undertakes an actuarial valuation every three years.

Remediation payments represent those cash flows that the Company is currently obligated to pay in respect of environmental remediation of current and former facilities. It does not include any discretionary remediation costs that the Company may choose to incur.

Operating lease commitments relate primarily to office space, motor vehicles and various items of computer and office equipment which are expected to be renewed and replaced in the normal course of business.

Raw material purchase obligations relate to certain long-term raw material contracts which stipulate fixed or minimum quantities to be purchased; fixed, minimum or variable cost provisions; and the approximate timing of the transaction. Purchase obligations exclude agreements that are cancelable without penalty.

The estimated payments included in the table above reflect the variable interest charge on long-term debt obligations. Estimated commitment fees are also included and interest income is excluded.

Due to the uncertainty regarding the nature of tax audits, particularly those which are not currently underway, it is not meaningful to predict the outcome of obligations related to unrecognized tax benefits. Further disclosure is provided in Note 10 of the Notes to the Consolidated Financial Statements.

Investing activities

Capital commitments relate to certain capital projects that the Company has committed to undertake.

Financing activities

On December 14, 2016, Innospec and certain subsidiaries of the Company entered into a Third Amendment and Restatement Agreement with various lenders which amends and restates the Company's credit facility agreement dated December 14, 2011, as amended and restated on August 28, 2013 and November 6, 2015 (the "Pre-Existing Credit Agreement" the Pre-Existing Credit Agreement, as amended and restated pursuant to the Third Amendment and Restatement Agreement, being the "Amended Credit Agreement.")

The Amended Credit Agreement retains the \$200.0 million revolving credit facility available to the Company and added a term loan facility of \$110.0 million. The termination date of the revolving facility remains November 6, 2020. Repayments for the term loan of \$11.0 million and \$16.5 million were made on December 29, 2017 and December 28, 2018, respectively. A further installment of \$22.0 million is due on December 28, 2019, with the outstanding balance due on November 6, 2020.

Finance leases relate to the financing of certain fixed assets in our Fuel Specialties and Oilfield Services segments.

Environmental Matters and Plant Closures

Under certain environmental laws the Company is responsible for the remediation of hazardous substances or wastes at currently or formerly owned or operated properties.

As most of our manufacturing operations have been conducted outside the U.S., we expect that liability pertaining to the investigation and remediation of contaminated properties is likely to be determined under non-U.S. law.

We evaluate costs for remediation, decontamination and demolition projects on a regular basis. Full provision is made for those costs to which we are committed under environmental laws amounting to \$49.5 million at December 31, 2018. Remediation expenditure utilizing these provisions was \$3.1 million, \$2.4 million and \$2.7 million in the years 2018, 2017 and 2016, respectively.

Item 7A Quantitative and Qualitative Disclosures about Market Risk

The Company uses floating rate debt to finance its global operations. The Company is subject to business risks inherent in non-U.S. activities, including political and economic uncertainty, import and export limitations, and market risk related to changes in interest rates and foreign currency exchange rates. The political and economic risks are mitigated by the stability of the countries in which the Company's largest operations are located. Credit limits, ongoing credit evaluation and account monitoring procedures are used to minimize bad debt risk. Collateral is not generally required.

From time to time, the Company uses derivatives, including interest rate swaps, commodity swaps and foreign currency forward exchange contracts, in the normal course of business to manage market risks. The derivatives used in hedging activities are considered risk management tools and are not used for trading purposes. In addition, the Company enters into derivative instruments with a diversified group of major financial institutions in order to manage the exposure to non-performance of such instruments. The Company's objective in managing the exposure to changes in interest rates is to limit the impact of such changes on earnings and cash flows and to lower overall borrowing costs. The Company's objective in managing the exposure to changes in foreign currency exchange rates is to reduce volatility on earnings and cash flows associated with such changes.

The Company offers fixed prices for some long-term sales contracts. As manufacturing and raw material costs are subject to variability the Company may use commodity swaps to hedge the cost of some raw materials thus reducing volatility on earnings and cash flows. The derivatives are considered risk management tools and are not used for trading purposes. The Company's objective is to manage its exposure to fluctuating costs of raw materials.

Interest Rate Risk

From time to time, the Company uses interest rate swaps to manage interest rate exposure. As at December 31, 2018 the Company had cash and cash equivalents of \$123.1 million, and long-term debt and finance leases of \$210.9 million (including current portion). Long-term debt comprises a \$200.0 million revolving credit facility available to the Company and a remaining term loan facility of \$82.5 million. The credit facilities carry an interest rate based on U.S. dollar LIBOR plus a margin of between 1.20% and 2.45% which is dependent on the Company's ratio of net debt to EBITDA. Net debt and EBITDA are non-GAAP measures of liquidity defined in the credit facility.

At December 31, 2018, \$126.0 million was drawn under the revolving credit facility and the term loan facility of \$82.5 million was drawn. Repayments for the term loan of \$11.0 million and \$16.5 million were made on December 29, 2017 and December 28, 2018, respectively. A further installment of \$22.0 million is due on December 28, 2019, with the outstanding balance due on November 6, 2020.

The Company has taken out interest rate swaps to hedge interest rate risk on core debt. As at December 31, 2018, interest rate swaps with a notional value of \$132.5 million were in place.

Fixed interest rates payable under the interest rate swaps vary from 1.42% to 1.67%. Interest rate swaps in place to hedge interest rate risk on the term loan have an amortizing profile matching the amortization of the term loan.

The Company has \$210.9 million long-term debt and finance leases (including the current portion) which is partly offset by \$123.1 million cash and cash equivalents. The interest payable on long-term debt (excluding the margin) exceeds the interest receivable on positive cash balances and after deducting interest rate hedging. On a gross basis, assuming no additional interest on the cash balances and after deducting interest rate hedging, a hypothetical absolute change of 1% in U.S. base interest rates for a one-year period would impact net income and cash flows by approximately \$0.8 million before tax. On a net basis, assuming additional interest on the cash balances, a hypothetical absolute change of 1% in U.S. base interest rates for a one-year period would impact net income and cash flows by approximately \$0.5 million before tax.

The above does not consider the effect of interest or exchange rate changes on overall activity nor management action to mitigate such changes. As at December 31, 2018, Innospec has interest rate swaps which mitigate a proportion of the risk identified above.

Exchange Rate Risk

The Company generates an element of its revenues and incurs some operating costs in currencies other than the U.S. dollar. The reporting currency of the Company is the U.S. dollar.

The Company evaluates the functional currency of each reporting unit according to the economic environment in which it operates. Several major subsidiaries of the Company operating outside of the U.S. have the U.S. dollar as their functional currency due to the nature of the markets in which they operate. In addition, the financial position and results of operations of some of our overseas subsidiaries are reported in the relevant local currency and then translated to U.S. dollars at the applicable currency exchange rate for inclusion in our consolidated financial statements.

The primary foreign currencies in which we have exchange rate fluctuation exposure are the European Union euro, British pound sterling and Brazilian Real. Changes in exchange rates between these foreign currencies and the U.S. dollar will affect the recorded levels of our assets and liabilities, to the extent that such figures reflect the inclusion of foreign assets and liabilities which are translated into U.S. dollars for presentation in our consolidated financial statements, as well as our results of operations.

The Company's objective in managing the exposure to foreign currency fluctuations is to reduce earnings and cash flow volatility associated with foreign currency exchange rate changes. Accordingly, the Company enters into various contracts that change in value as foreign currency exchange rates change to protect the U.S. dollar value of its existing foreign currency denominated assets, liabilities, commitments, and cash flows. The Company also uses foreign currency forward exchange contracts to offset a portion of the Company's

exposure to certain foreign currency denominated revenues so that gains and losses on these contracts offset changes in the U.S. dollar value of the related foreign currency denominated revenues. The objective of the hedging program is to reduce earnings and cash flow volatility related to changes in foreign currency exchange rates.

The trading of our Fuel Specialties, Performance Chemicals and Oilfield Services segments is inherently naturally hedged and accordingly changes in exchange rates would not be material to our earnings or financial position. The cost base of our Octane Additives reporting segment and corporate costs, however, are largely denominated in British pound sterling. A 5% strengthening in the U.S. dollar against British pound sterling would increase reported operating income by approximately \$2.3 million for a one-year period excluding the impact of any foreign currency forward exchange contracts. Where a 5% strengthening of the U.S. dollar has been used as an illustration, a 5% weakening would be expected to have the opposite effect on operating income.

Raw Material Cost Risk

We use a variety of raw materials, chemicals and energy in our manufacturing and blending processes. Many of the raw materials that we use are derived from petrochemical-based and vegetable-based feedstocks which can be subject to periods of rapid and significant cost instability. These fluctuations in cost can be caused by political instability in oil producing nations and elsewhere, or other factors influencing global supply and demand of these materials, over which we have no or little control. We use long-term contracts (generally with fixed or formula-based costs) and advance bulk purchases to help ensure availability and continuity of supply, and to manage the risk of cost increases. From time to time we enter into hedging arrangements for certain raw materials, but do not typically enter into hedging arrangements for all raw materials, chemicals or energy costs. Should the costs of raw materials, chemicals or energy increase, and should we not be able to pass on these cost increases to our customers, then operating margins and cash flows from operating activities would be adversely impacted. Should raw material costs increase significantly, then the Company's need for working capital could similarly increase. Any of these risks could adversely impact our results of operations, financial position and cash flows.

Item 8 Financial Statements and Supplementary Data

Report of Independent Registered Public Accounting Firm

To the Stockholders and Board of Directors

Innospec, Inc.:

Opinions on the Consolidated Financial Statements and Internal Control Over Financial Reporting

We have audited the accompanying consolidated balance sheet of Innospec, Inc. and subsidiaries (the Company) as of December 31, 2018, the related consolidated statements of income, comprehensive income, accumulated other comprehensive loss, cash flows, and equity for the year then ended, and the related notes (collectively, the consolidated financial statements). We also have audited the Company's internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control – Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2018, and the results of its operations and its cash flows for the year then ended, in conformity with U.S. generally accepted accounting principles. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2018 based on criteria established in Internal Control – Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Basis for Opinions

The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's consolidated financial statements and an opinion on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audit of the consolidated financial statements included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audit also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

Definition and Limitations of Internal Control Over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

KPMG LLP

We have served as the Company's auditor since 2011.

Manchester, United Kingdom
February 20, 2019

Report of Independent Registered Public Accounting Firm

To the Stockholders and Board of Directors

Innospec, Inc.:

Opinion on the Consolidated Financial Statements

We have audited the accompanying consolidated balance sheet of Innospec, Inc. and subsidiaries (the Company) as of December 31, 2017, the related consolidated statements of income, comprehensive income, accumulated other comprehensive loss, cash flows and equity for each of the years in the two year period ended December 31, 2017, and the related notes (collectively, the consolidated financial statements). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2017, and the results of its operations and its cash flows for each of the years in the two year period ended December 31, 2017, in conformity with U.S. generally accepted accounting principles.

Basis for Opinion

These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audits provide a reasonable basis for our opinion.

KPMG Audit Plc

We have served as the Company's auditor since 2011.

Manchester, United Kingdom
February 15, 2018

CONSOLIDATED STATEMENTS OF INCOME
(in millions, except share and per share data)

	Years ended December 31		
	2018	2017	2016
Net sales	\$ 1,476.9	\$1,306.8	\$ 883.4
Cost of goods sold	(1,041.9)	(903.5)	(551.1)
Gross profit	<u>435.0</u>	<u>403.3</u>	<u>332.3</u>
Operating expenses:			
Selling, general and administrative	(261.0)	(244.2)	(216.7)
Research and development	(33.4)	(31.4)	(25.4)
Restructuring charge	(7.1)	0.0	0.0
Adjustment to fair value of contingent consideration	0.0	0.0	9.4
Loss on disposal of subsidiary	0.0	(0.9)	(1.4)
Foreign exchange loss on liquidation of subsidiary	0.0	(1.8)	0.0
Total operating expenses	<u>(301.5)</u>	<u>(278.3)</u>	<u>(234.1)</u>
Operating income	133.5	125.0	98.2
Other income, net	5.0	11.3	8.1
Interest expense, net	(6.9)	(8.2)	(3.2)
Income before income tax expense	131.6	128.1	103.1
Income tax expense	(46.6)	(66.3)	(21.8)
Net income	<u>\$ 85.0</u>	<u>\$ 61.8</u>	<u>\$ 81.3</u>
Earnings per share:			
Basic	<u>\$ 3.48</u>	<u>\$ 2.56</u>	<u>\$ 3.39</u>
Diluted	<u>\$ 3.45</u>	<u>\$ 2.52</u>	<u>\$ 3.33</u>
Weighted average shares outstanding (in thousands):			
Basic	<u>24,401</u>	<u>24,148</u>	<u>23,998</u>
Diluted	<u>24,603</u>	<u>24,486</u>	<u>24,442</u>
Dividend declared per common share	<u>\$ 0.89</u>	<u>\$ 0.77</u>	<u>\$ 0.67</u>

We have recast certain prior period amounts to conform to new accounting standards, as disclosed in Note 19 of the Notes to the Consolidated Financial Statements.

The accompanying notes are an integral part of these statements.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(in millions)

Total comprehensive income for the years ended December 31	2018	2017	2016
Net income	\$ 85.0	\$ 61.8	\$ 81.3
Changes in cumulative translation adjustment, net of tax of \$2.7 million, \$(3.3) million and \$1.5 million, respectively	(22.6)	44.0	(20.5)
Unrealized gains on derivative instruments, net of tax of \$(0.1) million, \$(0.2) million and \$(0.1) million, respectively	0.3	0.9	0.3
Amortization of prior service credit, net of tax of \$0.2 million, \$0.2 million and \$0.2 million, respectively	(0.9)	(0.8)	(0.9)
Amortization of actuarial net losses, net of tax of \$(0.3) million, \$(0.9) million and \$(0.5) million, respectively	1.7	4.1	2.1
Actuarial net (losses)/gains arising during the year, net of tax of \$3.3 million, \$(8.8) million and \$(0.8) million, respectively	(15.7)	39.5	3.7
Total comprehensive income	\$ 47.8	\$149.5	\$ 66.0

CONSOLIDATED STATEMENTS OF ACCUMULATED OTHER COMPREHENSIVE LOSS
(in millions)

Accumulated other comprehensive loss for the years ended December 31	2018	2017	2016
Cumulative translation adjustment, net of tax	\$(59.1)	\$(36.5)	\$(80.5)
Unrealized gains on derivative instruments, net of tax of \$(0.4) million, \$(0.3) million and \$(0.1) million, respectively	1.5	1.2	0.3
Unrecognized actuarial net losses, net of tax of \$13.0 million, \$9.9 million and \$19.4 million, respectively	(18.1)	(3.2)	(46.0)
Accumulated other comprehensive loss	\$(75.7)	\$(38.5)	\$(126.2)

The accompanying notes are an integral part of these statements.

CONSOLIDATED BALANCE SHEETS
(in millions, except share and per share data)

	At December 31	
	2018	2017
Assets		
Current assets:		
Cash and cash equivalents	\$ 123.1	\$ 90.2
Trade and other accounts receivable (less allowances of \$2.9 million and \$4.1 million, respectively)	279.7	244.5
Inventories (less allowances of \$13.6 million and \$12.6 million, respectively):		
Finished goods	180.2	145.9
Raw materials	67.8	63.9
Total inventories	248.0	209.8
Prepaid expenses	11.6	13.1
Prepaid income taxes	1.5	2.8
Other current assets	0.0	1.1
Total current assets	663.9	561.5
Net property, plant and equipment	196.4	196.0
Goodwill	364.9	361.8
Other intangible assets	136.3	163.3
Deferred tax assets	8.8	6.5
Pension asset	95.9	116.0
Other non-current assets	7.2	5.1
Total assets	<u>\$1,473.4</u>	<u>\$1,410.2</u>
Liabilities and Equity		
Current liabilities:		
Accounts payable	\$ 126.8	\$ 117.9
Accrued liabilities	132.1	104.1
Current portion of long-term debt	21.4	15.8
Current portion of finance leases	1.8	2.7
Current portion of plant closure provisions	5.9	5.2
Current portion of accrued income taxes	8.6	15.8
Total current liabilities	296.6	261.5
Long-term debt, net of current portion	186.2	202.6
Finance leases, net of current portion	1.5	3.2
Plant closure provisions, net of current portion	43.6	40.9
Accrued income taxes, net of current portion	40.0	41.7
Unrecognized tax benefits, net of current portion	14.0	2.5
Deferred tax liabilities	48.2	45.0
Pension liabilities and post-employment benefits	15.7	16.5
Other non-current liabilities	2.1	2.0
Equity:		
Common stock, \$0.01 par value, authorized 40,000,000 shares, issued 29,554,500 shares	0.3	0.3
Additional paid-in capital	324.9	320.4
Treasury stock (5,120,799 and 5,204,181 shares at cost, respectively)	(92.8)	(93.3)
Retained earnings	668.3	605.0
Accumulated other comprehensive loss	(75.7)	(38.5)
Total Innospec stockholders' equity	825.0	793.9
Non-controlling interest	0.5	0.4
Total equity	825.5	794.3
Total liabilities and equity	<u>\$1,473.4</u>	<u>\$1,410.2</u>

The accompanying notes are an integral part of these statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS
(in millions)

	Years ended December 31		
	2018	2017	2016
Cash Flows from Operating Activities			
Net income	\$ 85.0	\$ 61.8	\$ 81.3
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	49.6	50.4	38.1
Adjustment to fair value of contingent consideration	0.0	0.0	(9.4)
Loss on disposal of subsidiary	0.0	0.9	1.4
Foreign exchange loss on liquidation of subsidiary	0.0	1.8	0.0
Deferred tax expense/(benefit)	5.5	(6.7)	0.9
Cash contributions to defined benefit pension plans	(1.0)	(1.0)	(1.1)
Non-cash income of defined benefit pension plans	(4.3)	(3.6)	(6.2)
Stock option compensation	4.9	4.1	3.3
Changes in assets and liabilities, net of effects of acquired and divested companies:			
Trade and other accounts receivable	(40.1)	(83.2)	(6.0)
Inventories	(42.2)	(30.8)	7.7
Prepaid expenses	0.5	(6.8)	0.5
Accounts payable and accrued liabilities	38.4	48.6	(3.4)
Accrued income taxes	(6.1)	47.5	(2.0)
Plant closure provisions	3.6	3.8	1.9
Unrecognized tax benefits	11.5	(0.5)	(1.6)
Other assets and liabilities	(0.4)	(3.6)	0.1
Net cash provided by operating activities	104.9	82.7	105.5
Cash Flows from Investing Activities			
Capital expenditures	(28.9)	(23.3)	(16.5)
Business combinations, net of cash acquired	(5.4)	2.6	(197.4)
Acquisition of intangible asset	0.0	(4.2)	0.0
Internally developed software	(1.2)	(4.7)	0.0
Sale of short-term investments	0.0	0.0	4.8
Net cash used in investing activities	(35.5)	(29.6)	(209.1)
Cash Flows from Financing Activities			
Proceeds from revolving credit facility	10.0	10.0	48.0
Repayments of revolving credit facility	(5.0)	(50.0)	(20.0)
(Payment)/receipt of term loans	(16.5)	(11.0)	110.0
Repayment of finance leases and term loans	(2.7)	(2.5)	(1.1)
Refinancing costs	0.0	0.0	(1.2)
Payment for acquisition-related contingent consideration	0.0	0.0	(44.0)
Dividend paid	(21.7)	(18.6)	(15.9)
Issue of treasury stock	1.1	6.8	2.1
Repurchase of common stock	(1.4)	(1.1)	(8.4)
Net cash (used in)/provided by financing activities	(36.2)	(66.4)	69.5
Effect of foreign currency exchange rate changes on cash	(0.3)	1.6	(0.9)
Net change in cash and cash equivalents	32.9	(11.7)	(35.0)
Cash and cash equivalents at beginning of year	90.2	101.9	136.9
Cash and cash equivalents at end of year	\$ 123.1	\$ 90.2	\$ 101.9

Amortization of deferred finance costs of \$0.7 million (2017 – \$0.6 million, 2016 – \$0.4 million) for the year are included in depreciation and amortization in the cash flow statement but in interest expense in the income statement. Cash payments/receipts in respect of income taxes and interest are disclosed in Note 10 and Note 11, respectively, of the Notes to the Consolidated Financial Statements.

The accompanying notes are an integral part of these statements.

CONSOLIDATED STATEMENTS OF EQUITY
(in millions)

	Common Stock	Additional Paid-In Capital	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Loss	Non- controlling Interest	Total Equity
Balance at December 31, 2015	\$ 0.3	\$ 311.0	\$ (91.8)	\$ 496.4	\$ (110.9)	\$ 0.3	\$ 605.3
Net income				81.3			81.3
Dividend paid (\$0.67 per share)				(15.9)			(15.9)
Changes in cumulative translation adjustment, net of tax					(20.5)		(20.5)
Unrealized gains on derivative instruments, net of tax					0.3		0.3
Treasury stock re-issued		(0.2)	2.7				2.5
Treasury stock repurchased			(8.4)				(8.4)
Excess tax benefit from stock-based payment arrangements		1.0					1.0
Stock option compensation		3.3					3.3
Amortization of prior service credit, net of tax					(0.9)		(0.9)
Amortization of actuarial net losses, net of tax					2.1		2.1
Actuarial net gains arising during the year, net of tax					3.7		3.7
Balance at December 31, 2016	\$ 0.3	\$ 315.1	\$ (97.5)	\$ 561.8	\$ (126.2)	\$ 0.3	\$ 653.8
Net income				61.8			61.8
Dividend paid (\$0.77 per share)				(18.6)			(18.6)
Changes in cumulative translation adjustment, net of tax					44.0		44.0
Non-controlling interest						0.1	0.1
Unrealized gains on derivative instruments, net of tax					0.9		0.9
Treasury stock re-issued		1.1	5.3				6.4
Treasury stock repurchased			(1.1)				(1.1)
Stock option compensation		4.2					4.2
Amortization of prior service credit, net of tax					(0.8)		(0.8)
Amortization of actuarial net losses, net of tax					4.1		4.1
Actuarial net gains arising during the year, net of tax					39.5		39.5
Balance at December 31, 2017	\$ 0.3	\$ 320.4	\$ (93.3)	\$ 605.0	\$ (38.5)	\$ 0.4	\$ 794.3
Net income				85.0			85.0
Dividend paid (\$0.89 per share)				(21.7)			(21.7)
Changes in cumulative translation adjustment, net of tax					(22.6)		(22.6)
Non-controlling interest						0.1	0.1
Unrealized gains on derivative instruments, net of tax					0.3		0.3
Treasury stock re-issued		(0.4)	1.9				1.5
Treasury stock repurchased			(1.4)				(1.4)
Stock option compensation		4.9					4.9
Amortization of prior service credit, net of tax					(0.9)		(0.9)
Amortization of actuarial net losses, net of tax					1.7		1.7
Actuarial net gains arising during the year, net of tax					(15.7)		(15.7)
Balance at December 31, 2018	\$ 0.3	\$ 324.9	\$ (92.8)	\$ 668.3	\$ (75.7)	\$ 0.5	\$ 825.5

The accompanying notes are an integral part of these statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Nature of Operations

Innospec develops, manufactures, blends, markets and supplies fuel additives, oilfield chemicals, personal care products and other specialty chemicals. Our products are sold primarily to oil and gas exploration and production companies, oil refineries, personal care and home care companies, formulators of agrochemical and metal extraction preparations and other chemical and industrial companies throughout the world. Our fuel additives help improve fuel efficiency, boost engine performance and reduce harmful emissions. Our Oilfield Services business supplies drilling and production chemicals which make exploration and production more cost-efficient, and more environmentally-friendly. Our Performance Chemicals business provides effective technology-based solutions for our customers' processes or products focused in the personal care, home care, agrochemical and metal extraction markets. Our Octane Additives business manufactures a fuel additive for use in automotive gasoline and provides services in respect of environmental remediation. Our principal reportable segments are Fuel Specialties, Performance Chemicals, Oilfield Services and Octane Additives.

Note 2. Accounting Policies

Basis of preparation: The consolidated financial statements have been prepared in accordance with generally accepted accounting principles ("GAAP") in the United States of America on a going concern basis and include all subsidiaries of the Company where the Company has a controlling financial interest. All significant intercompany accounts and balances have been eliminated upon consolidation. In accordance with GAAP in the United States of America, the results of operations of an acquired or disposed business are included or excluded from the consolidated financial statements from the date of acquisition or disposal.

Use of estimates: The preparation of the consolidated financial statements, in accordance with GAAP in the United States of America, requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

Cash equivalents: Investment securities with maturities of three months or less when purchased are considered to be cash equivalents.

Trade and other accounts receivable: The Company records trade and other accounts receivable at net realizable value and maintains allowances for customers not making required payments. The Company determines the adequacy of allowances by periodically evaluating each customer receivable considering our customer's financial condition, credit history and current economic conditions.

Inventories: Inventories are stated at the lower of cost (FIFO method) or market value. Cost includes materials, labor and an appropriate proportion of plant overheads. The Company accrues volume discounts where it is probable that the required volume will be attained and

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

the amount can be reasonably estimated. The discounts are recorded as a reduction in the cost of materials based on projected purchases over the period of the agreement. Inventories are adjusted for estimated obsolescence and written down to market value based on estimates of future demand and market conditions.

Property, plant and equipment: Property, plant and equipment are stated at cost less accumulated depreciation. Depreciation is provided over the estimated useful lives of the assets using the straight-line method and is allocated between cost of goods sold and operating expenses. The cost of additions and improvements are capitalized. Maintenance and repairs are charged to expenses as incurred. When assets are sold or retired the associated cost and accumulated depreciation are removed from the consolidated financial statements and any related gain or loss is included in earnings. The estimated useful lives of the major classes of depreciable assets are as follows:

Buildings	7 to 25 years
Equipment	3 to 10 years

Goodwill and other intangible assets: Goodwill and other intangible assets deemed to have indefinite lives are subject to at least annual impairment assessments. Initially we perform a qualitative assessment to determine whether it is more likely than not that the fair value of a segment is less than the carrying amount prior to performing the two-step goodwill impairment test. If a two-step test is required we assess the fair value based on projected post-tax cash flows discounted at the Company's weighted average cost of capital. The annual measurement date for impairment assessment of the goodwill relating to the Fuel Specialties, Performance Chemicals and Oilfield Services segments is December 31 each year. The Company capitalizes software development costs, including licenses, subsequent to the establishment of technological feasibility. Other intangible assets deemed to have finite lives, including software development costs and licenses, are amortized using the straight-line method over their estimated useful lives and tested for any potential impairment when events occur or circumstances change which suggest that an impairment may have occurred.

Deferred finance costs: The costs relating to debt financing are capitalized, offset against long-term debt in the consolidated balance sheets and amortized using the effective interest method over the expected life of the debt financing facility. The amortization charge is included in interest expense in the income statement. See Note 11 of the Notes to the Consolidated Financial Statements.

Impairment of long-lived assets: The Company reviews the carrying value of its long-lived assets, including buildings and equipment, whenever changes in circumstances suggest that the carrying values may be impaired. In order to facilitate this test the Company groups together assets at the lowest possible level for which cash flow information is available. Undiscounted future cash flows expected to result from the asset groups are compared with the carrying value of the asset groups and if they are lower an impairment loss may be

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

recognized. The amount of the impairment loss is the difference between the fair value and the carrying value of the asset groups. Fair values are determined using post-tax cash flows discounted at the Company's weighted average cost of capital.

Derivative instruments: From time to time, the Company uses various derivative instruments including forward currency contracts, options, interest rate swaps and commodity swaps to manage certain exposures. These instruments are entered into under the Company's corporate risk management policy to minimize exposure and are not for speculative trading purposes. The Company recognizes all derivatives as either current or non-current assets or liabilities in the consolidated balance sheet and measures those instruments at fair value. Changes in the fair value of derivatives that are not designated as hedges, or do not meet the requirements for hedge accounting, are recognized in earnings. Derivatives which are designated as hedges are tested for effectiveness on a quarterly basis, and marked to market. The ineffective portion of the derivative's change in value is recognized in earnings. The effective portion is recognized in other comprehensive income until the hedged item is recognized in earnings.

Environmental compliance and remediation: Environmental compliance costs include ongoing maintenance, monitoring and similar costs. We recognize environmental liabilities when they are probable and the costs can be reasonably estimated, and asset retirement obligations when there is a legal obligation and the costs can be reasonably estimated. Such accruals are adjusted as further information develops or circumstances change. Costs of future obligations are discounted to their present values using the Company's historic credit-adjusted risk-free rate.

Revenue recognition: On January 1, 2018 we adopted Accounting Standard Update (ASU) 2014-09, Revenue from Contracts with Customers (Topic 606) using the modified retrospective method. The impact of adopting ASC 606 did not result in a change to income, and therefore we are not reflecting a cumulative effect to the opening balance of retained earnings due to the adoption of ASC 606. The comparative periods have not been adjusted and continue to be reported under the accounting standards in effect for those periods.

Our revenues are primarily derived from the manufacture and sale of specialty chemicals. We recognize revenue when control of the product is transferred to our customer and for an amount that reflects the consideration we expect to collect from the customer. Control is generally transferred to the customer when title transfers (which may include physical possession by the customer), we have a right to payment from the customer, the customer has accepted the product, and the customer has assumed the risks and rewards of ownership. We have supplier managed inventory arrangements with some of our customers to facilitate on-demand product availability. In some cases, the inventory resides at a customer site, although title has not transferred, we are not entitled to payment, and we have not invoiced for the product. We have evaluated the contract terms under these arrangements and have determined that control transfers when the customer uses the product, at which time revenue is recognized. Our contracts generally include one performance obligation, which is providing

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

specialty chemicals. The performance obligation is satisfied at a point in time when products are shipped, delivered, or consumed by the customer, depending on the underlying contracts.

While some of our customers have payment terms beyond 30 days, we do not provide extended payment terms of a year or more, nor do our contracts include a financing component. Some of our contracts include variable consideration in the form of rebates. We record rebates at the point of sale as a reduction in sales when we can reasonably estimate the amount of the rebate. The estimates are based on our best judgment at the time of sale, which includes anticipated as well as historical performance.

Taxes assessed by a governmental authority which are concurrent with sales to our customers, including sales, use, value-added, and revenue-related excise taxes, are collected by us from the customer and are not included in net sales, but are reflected in accrued expenses until remitted to the appropriate governmental authority. When we are responsible for shipping and handling costs after title has transferred, we account for those as fulfillment costs and include them in cost of goods sold.

Components of net sales: All amounts billed to customers relating to shipping and handling are classified as net sales. Shipping and handling costs incurred by the Company are classified as cost of goods sold.

Components of cost of goods sold: Cost of goods sold is comprised of raw material costs including inbound freight, duty and non-recoverable taxes, inbound handling costs associated with the receipt of raw materials, packaging materials, manufacturing costs including labor costs, maintenance and utility costs, plant and engineering overheads, amortization expense for certain other intangible assets, warehousing and outbound shipping costs and handling costs. Inventory losses and provisions and the costs of customer claims are also recognized in the cost of goods line item.

Components of selling, general and administrative expenses: Selling expenses comprise the costs of the direct sales force, and the sales management and customer service departments required to support them. It also comprises commission charges, the costs of sales conferences and trade shows, the cost of advertising and promotions, amortization expense for certain other intangible assets, and the cost of bad and doubtful debts. General and administrative expenses comprise the cost of support functions including accounting, human resources, information technology and the cost of group functions including corporate management, finance, tax, treasury, investor relations and legal departments. Provision of management's best estimate of legal and settlement costs for litigation in which the Company is involved is accounted for in the administrative expense line item.

Research and development expenses: Research, development and testing costs are expensed to the income statement as incurred.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Earnings per share: Basic earnings per share is based on the weighted average number of common shares outstanding during the period. Diluted earnings per share includes the effect of options that are dilutive and outstanding during the period.

Foreign currencies: The Company's policy is that foreign exchange differences arising on the translation of the balance sheets of entities that have functional currencies other than the U.S. dollar are taken to a separate equity reserve, the cumulative translation adjustment. In entities where the U.S. dollar is the functional currency no gains or losses on translation occur, and gains or losses on monetary assets relating to currencies other than the U.S. dollar are taken to the income statement in other income/(expense), net. Gains and losses on intercompany foreign currency loans which are long-term in nature, which the Company does not intend to settle in the foreseeable future, are also recorded in accumulated other comprehensive loss. Other foreign exchange gains or losses are also included in other income, net in the income statement.

Stock-based compensation plans: The Company accounts for employee stock options and stock equivalent units under the fair value method. Stock options are fair valued at the grant date and the fair value is recognized straight-line over the vesting period of the option. Stock equivalent units are fair valued at each balance sheet date and the fair value is spread over the remaining vesting period of the unit.

Pension plans and other post-employment benefits: The Company recognizes the funded status of defined benefit post-retirement plans on the consolidated balance sheets and changes in the funded status in comprehensive income. The measurement date of the plan's funded status is the same as the Company's fiscal year-end. The service costs are recognized as employees render the services necessary to earn the post-employment benefits. Prior service costs and credits and actuarial gains and losses are amortized over the average remaining life expectancy of the inactive participants using the corridor method.

Income taxes: The Company provides for income taxes by recognizing deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the financial statement carrying amounts and the relevant tax bases of the assets and liabilities. Then the Company evaluates the need for a valuation allowance to reduce deferred tax assets to the amount more likely than not to be realized. The effect on deferred taxes of a change in tax rates is recognized in the period that includes the enactment date. The Company recognizes the tax benefit from a tax position only if it is more likely than not the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such positions are then measured based on the largest benefit that has greater than 50 percent likelihood of being realized upon settlement. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs. The Company recognizes accrued interest and penalties associated with unrecognized tax benefits as part of income taxes in our consolidated statements of income.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Note 3. Segment Reporting and Geographical Area Data

The Fuel Specialties, Performance Chemicals and Oilfield Services segments operate in markets where we actively seek growth opportunities although their ultimate customers are different. The Octane Additives segment is expected to further decline in the next twelve months as our one remaining refinery customer transitions to unleaded fuel.

Our Fuel Specialties segment develops, manufactures, blends, markets and supplies a range of specialty chemicals products used as additives to a wide range of fuels.

Our Performance Chemicals segment provides effective technology-based solutions for our customers' processes or products focused in the Personal Care, Home Care, Agrochemical and Metal Extraction markets.

Our Oilfield Services segment develops and markets products to prevent loss of mud in drilling operations, chemical solutions for fracturing and stimulation operations and products for oil and gas production which aid flow assurance and asset integrity.

Our Octane Additives segment, which we believe is the world's only producer of tetra ethyl lead ("TEL"), comprises sales of TEL for use in automotive gasoline and provides services in respect of environmental remediation.

There are no significant customers with sales greater than 10% of our net group sales in the last three financial years.

The Company evaluates the performance of its segments based on operating income. The following table analyzes sales and other financial information by the Company's reportable segments:

<u>(in millions)</u>	<u>2018</u>	<u>2017</u>	<u>2016</u>
Net Sales:			
<i>Refinery and Performance</i>	\$ 432.1	\$ 397.0	\$388.9
<i>Other</i>	142.4	126.8	120.7
Fuel Specialties	<u>574.5</u>	<u>523.8</u>	<u>509.6</u>
<i>Personal Care</i>	241.4	206.5	126.8
<i>Home Care</i>	109.1	103.4	2.0
<i>Other</i>	<u>117.6</u>	<u>109.6</u>	<u>9.9</u>
Performance Chemicals	<u>468.1</u>	<u>419.5</u>	<u>138.7</u>
Oilfield Services	400.6	304.4	191.7
Octane Additives	<u>33.7</u>	<u>59.1</u>	<u>43.4</u>
	<u>\$1,476.9</u>	<u>\$1,306.8</u>	<u>\$883.4</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

(in millions)	2018	2017	2016
Gross profit:			
Fuel Specialties	\$ 195.0	\$ 188.2	\$ 186.4
Performance Chemicals	97.5	75.8	43.4
Oilfield Services	130.4	109.3	76.4
Octane Additives	12.1	30.0	26.1
	<u>\$ 435.0</u>	<u>\$ 403.3</u>	<u>\$ 332.3</u>
Operating income/(expense):			
Fuel Specialties	\$ 116.3	\$ 107.7	\$ 111.1
Performance Chemicals	44.7	32.6	16.0
Oilfield Services	22.1	9.5	(4.7)
Octane Additives	9.9	26.7	22.7
Corporate costs	(52.4)	(48.8)	(54.9)
Restructuring charge	(7.1)	0.0	0.0
Adjustment to fair value of contingent consideration	0.0	0.0	9.4
Loss on disposal of subsidiary	0.0	(0.9)	(1.4)
Foreign exchange loss on liquidation of subsidiary	0.0	(1.8)	0.0
Total operating income	<u>\$ 133.5</u>	<u>\$ 125.0</u>	<u>\$ 98.2</u>
Identifiable assets at year end:			
Fuel Specialties	\$ 470.5	\$ 437.0	\$ 397.2
Performance Chemicals	463.9	480.8	340.0
Oilfield Services	296.1	256.6	240.0
Octane Additives	39.6	41.7	38.1
Corporate	203.3	194.1	166.1
	<u>\$1,473.4</u>	<u>\$1,410.2</u>	<u>\$1,181.4</u>

We have recast certain prior period amounts to conform to new accounting standards.

The Company includes within the corporate costs line item the costs of:

- managing the Group as a company with securities listed on the NASDAQ and registered with the SEC;
- the President/CEO's office, group finance, group human resources, group legal and compliance counsel, and investor relations;
- running the corporate offices in the U.S. and Europe;
- the corporate development function since they do not relate to the current trading activities of our other reporting segments; and
- the corporate share of the information technology, accounting and human resources departments.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The following tables analyze sales and other financial information by location:

(in millions)	2018	2017	2016
Net sales by source:			
United States & North America	\$ 803.1	\$ 615.7	\$ 474.4
United Kingdom	797.5	730.9	428.2
Rest of Europe	143.7	143.4	118.5
Rest of World	29.5	39.2	31.1
Sales between areas	(296.9)	(222.4)	(168.8)
	<u>\$1,476.9</u>	<u>\$1,306.8</u>	<u>\$ 883.4</u>
Income before income taxes:			
United States & North America	\$ 37.1	\$ 11.5	\$ 16.8
United Kingdom	59.5	51.9	42.6
Rest of Europe	32.8	63.1	39.2
Rest of World	2.2	1.6	4.5
	<u>\$ 131.6</u>	<u>\$ 128.1</u>	<u>\$ 103.1</u>
Long-lived assets at year end:			
United States & North America	\$ 148.6	\$ 149.7	\$ 155.3
United Kingdom	71.6	45.7	45.9
Rest of Europe	112.2	163.5	207.5
Rest of World	0.3	0.3	0.5
	<u>\$ 332.7</u>	<u>\$ 359.2</u>	<u>\$ 409.2</u>
Identifiable assets at year end:			
United States & North America	\$ 402.5	\$ 452.2	\$ 377.3
United Kingdom	504.7	258.4	257.6
Rest of Europe	173.1	317.5	156.0
Rest of World	28.2	20.3	15.7
Goodwill	364.9	361.8	374.8
	<u>\$1,473.4</u>	<u>\$1,410.2</u>	<u>\$1,181.4</u>

Sales by geographical area are reported by source, being where the transactions originated. Intercompany sales are priced using an appropriate pricing methodology and are eliminated in the consolidated financial statements.

Identifiable assets are those directly associated with the operations of the geographical area.

Goodwill has not been allocated by geographical location on the grounds that it would be impracticable to do so.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Note 4. Acquisition of BioSuite, LLC

On May 31, 2018, the Company acquired BioSuite, LLC (“BioSuite”), a specialized formulator of biocide and biostat solutions for the oil and gas industry. We purchased BioSuite for total consideration of \$8.6 million, with an initial payment at closing of \$5.8 million funded from existing cash and debt facilities followed by a reduction for working capital adjustments of \$0.4 million in the third quarter. The remaining payment is performance related based on a multiple of BioSuite’s earnings before interest, taxes, depreciation and amortization over a twelve month period. Based on the current forecast we anticipate a further payment of \$3.2 million payable on November 30, 2019.

The following table summarizes the calculations of the total purchase price and the estimated allocation of the purchase price to the assets acquired and liabilities assumed for the business:

<u>(in millions)</u>	<u>BioSuite</u>
Goodwill	\$ 7.5
Receivables	0.4
Inventory	0.5
Payables	(1.9)
Extinguishment of existing liabilities	2.1
Purchase price, net of cash acquired	<u>\$ 8.6</u>

Of the \$7.5 million goodwill recorded, \$4.3 million is amortizable for income tax purposes over a 15 year period.

We have finalized our review of the valuation of assets acquired and liabilities assumed with no measurement period adjustments required.

Note 5. Earnings per Share

Basic earnings per share is based on the weighted average number of common shares outstanding during the period. Diluted earnings per share includes the effect of options that are dilutive and outstanding during the period. Per share amounts are computed as follows:

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Numerator (in millions):			
Net income available to common stockholders	<u>\$ 85.0</u>	<u>\$ 61.8</u>	<u>\$ 81.3</u>
Denominator (in thousands):			
Weighted average common shares outstanding	24,401	24,148	23,998
Dilutive effect of stock options and awards	<u>202</u>	<u>338</u>	<u>444</u>
Denominator for diluted earnings per share	<u>24,603</u>	<u>24,486</u>	<u>24,442</u>
Net income per share, basic:	<u>\$ 3.48</u>	<u>\$ 2.56</u>	<u>\$ 3.39</u>
Net income per share, diluted:	<u>\$ 3.45</u>	<u>\$ 2.52</u>	<u>\$ 3.33</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

In 2018, 2017 and 2016 the average number of anti-dilutive options excluded from the calculation of diluted earnings per share were 0, 9,422 and 0 respectively.

Note 6. Property, Plant and Equipment

Property, plant and equipment consists of the following:

<u>(in millions)</u>	<u>2018</u>	<u>2017</u>
Land	\$ 18.6	\$ 17.7
Buildings	57.0	51.0
Equipment	311.7	311.1
Work in progress	16.0	16.1
	<u>403.3</u>	<u>395.9</u>
Less accumulated depreciation	<u>(206.9)</u>	<u>(199.9)</u>
	<u>\$ 196.4</u>	<u>\$ 196.0</u>

The prior year cost and accumulated depreciation comparatives have been restated. There is no impact on the net book value.

Of the total net book value of equipment at December 31, 2018 \$3.6 million (2017 – \$6.2 million) are in respect of assets held under finance leases.

Depreciation charges were \$22.6 million, \$21.4 million and \$13.5 million in 2018, 2017 and 2016, respectively.

The estimated additional cost to complete work in progress at December 31, 2018 is \$6.0 million (2017 – \$2.3 million).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Note 7. Goodwill

The following table analyzes goodwill movement for 2018 and 2017.

(in millions)	Fuel Specialties	Performance Chemicals	Oilfield Services	Octane Additives	Total
At December 31, 2016					
Gross cost (1)	\$ 207.9	\$ 129.6	\$ 37.3	\$ 236.5	\$ 611.3
Accumulated impairment losses	0.0	0.0	0.0	(236.5)	(236.5)
Net book amount	<u>\$ 207.9</u>	<u>\$ 129.6</u>	<u>\$ 37.3</u>	<u>\$ 0.0</u>	<u>\$ 374.8</u>
Exchange effect	0.0	10.2	0.0	0.0	10.2
Measurement period adjustment	0.0	(23.1)	0.0	0.0	(23.1)
At December 31, 2017					
Gross cost (1)	\$ 207.9	\$ 116.6	\$ 37.3	\$ 236.5	\$ 598.3
Accumulated impairment losses	0.0	0.0	0.0	(236.5)	(236.5)
Net book amount	<u>\$ 207.9</u>	<u>\$ 116.6</u>	<u>\$ 37.3</u>	<u>\$ 0.0</u>	<u>\$ 361.8</u>
Exchange effect	0.0	(4.4)	0.0	0.0	(4.4)
Acquisition	0.0	0.0	7.5	0.0	7.5
At December 31, 2018					
Gross cost (1)	\$ 207.9	\$ 112.2	\$ 44.8	\$ 236.5	\$ 601.4
Accumulated impairment losses	0.0	0.0	0.0	(236.5)	(236.5)
Net book amount	<u>\$ 207.9</u>	<u>\$ 112.2</u>	<u>\$ 44.8</u>	<u>\$ 0.0</u>	<u>\$ 364.9</u>

(1) Gross cost is net of \$8.7 million, \$0.3 million and \$289.5 million of historical accumulated amortization in respect of the Fuel Specialties, Performance Chemicals and Octane Additives reporting segments, respectively.

For information regarding the acquisition in 2018 as shown above, see Note 4 of the Notes to the Consolidated Financial Statements.

The Company's reporting units, the level at which goodwill is tested for impairment, are consistent with the reportable segments: Fuel Specialties, Performance Chemicals, Oilfield Services and Octane Additives. The components in each segment (including products, markets and competitors) have similar economic characteristics and the segments, therefore, reflect the lowest level at which operations and cash flows can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the Company.

The Company assesses goodwill for impairment on at least an annual basis, initially based on a qualitative assessment to determine whether it is more likely than not that the fair value of a segment is less than the carrying amount. If a potential impairment is identified then a two-step impairment test is followed.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The Company performed its annual impairment assessment in respect of goodwill as at December 31, 2018, 2017 and 2016. Our impairment assessment concluded that there had been no impairment of goodwill in respect of those reporting units.

We believe that where appropriate the assumptions used in our impairment assessments are reasonable, but that they are judgmental, and variations in any of the assumptions may result in materially different calculations of any potential impairment charges.

Note 8. Other Intangible Assets

Other intangible assets comprise the following:

<u>(in millions)</u>	<u>2018</u>	<u>2017</u>
Gross cost:		
– Product rights	\$ 34.0	\$ 34.0
– Brand names	8.9	8.9
– Technology	55.1	55.1
– Customer and distributor relationships	125.6	127.5
– Patents	2.9	2.9
– Non-compete agreements	4.1	4.1
– Marketing related	22.1	22.1
– Internally developed software	41.9	41.2
	<u>294.6</u>	<u>295.8</u>
Accumulated amortization:		
– Product rights	(20.1)	(16.4)
– Brand names	(5.4)	(4.4)
– Technology	(19.1)	(15.7)
– Customer and distributor relationships	(53.5)	(43.2)
– Patents	(2.9)	(2.9)
– Non-compete agreements	(4.1)	(4.1)
– Marketing related	(22.1)	(22.1)
– Internally developed software	(31.1)	(23.7)
	<u>(158.3)</u>	<u>(132.5)</u>
	<u>\$ 136.3</u>	<u>\$ 163.3</u>

Product rights

Following the acquisition of Chemsil on August 30, 2013, the Company recognized an intangible asset of \$34.0 million in respect of Chemsil’s product rights portfolio. This asset has an expected life of 9 years and is being amortized on a straight-line basis over this period.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

An amortization expense of \$3.7 million was recognized in 2018 (2017 – \$3.8 million) in selling, general and administrative expenses.

Brand names

Following the acquisition of Independence on October 27, 2014, the Company recognized an intangible asset of \$6.0 million in respect of Independence's brand name. This asset has an expected life of 10 years and is being amortized on a straight-line basis over this period.

Following the acquisition of Bachman on November 4, 2013, the Company recognized an intangible asset of \$2.9 million in respect of Bachman's brand names. This asset had an expected life of 5 years and is now fully amortized.

An amortization expense of \$1.0 million was recognized in 2018 (2017 – \$1.2 million) in selling, general and administrative expenses.

Technology

Following the acquisition of Independence on October 27, 2014, the Company recognized an intangible asset of \$26.0 million in respect of Independence's product formulations. This asset has an expected life of 15 years and is being amortized on a straight-line basis over this period.

Following the acquisition of Bachman on November 4, 2013, the Company recognized an intangible asset of \$8.5 million in respect of Bachman's core chemistry know-how of oilfield chemicals. This asset has an expected life of 15 years and is being amortized on a straight-line basis over this period.

Following the acquisition of Strata on December 24, 2012, the Company recognized an intangible asset of \$18.3 million in respect of technological know-how of the mixing and manufacturing process, patents which protect the technology and the associated product branding. This asset has an expected life of 16.5 years and is being amortized on a straight-line basis over this period.

An amortization expense of \$3.4 million was recognized in 2018 (2017 – \$3.4 million) in cost of goods sold.

Customer and distributor relationships

On August 9, 2017, the Company acquired an intangible asset from Huntsman Holland B.V. for \$4.2 million in respect of long-term customer and distributor relationships in ASPAC and America. This asset has a weighted average expected life of 10 years and is being amortized on a straight-line basis over this period.

On March 31, 2017 the Company recognized an intangible asset of \$33.5 million in respect of long-term customer relationships relating to the Huntsman acquisition on December 30, 2016.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

This asset has a weighted average expected life of 10 years and is being amortized on a straight-line basis over this period.

Following the acquisition of Independence on October 27, 2014, the Company recognized an intangible asset of \$29.2 million in respect of Independence's long-term customer relationships. This asset has a weighted average expected life of 10 years and is being amortized on a straight-line basis over this period.

Following the acquisition of Bachman on November 4, 2013, the Company recognized an intangible asset of \$14.5 million in respect of Bachman's long-term customer relationships. This asset has a weighted average expected life of 14.5 years and is being amortized on a straight-line basis over this period.

Following the acquisition of Strata on December 24, 2012, the Company recognized an intangible asset of \$28.2 million in respect of long-term customer relationships. This asset has an expected life of 11.5 years and is being amortized on a straight-line basis over this period.

Following the acquisition of Finetex (now merged into Innospec Active Chemicals LLC) in January 2005, the Company recognized an intangible asset of \$4.2 million in relation to customer lists acquired. This asset had an expected life of 13 years and is now fully amortized.

An amortization expense of \$10.7 million was recognized in 2018 (2017 – \$10.7 million) in selling, general and administrative expenses. The impact of foreign exchange translation on the balance sheet amortization is recognized as a cumulative translation adjustment within equity.

Non-compete agreements

Following the acquisition of Independence on October 27, 2014, the Company recognized an intangible asset of \$2.6 million in respect of a non-compete agreement. This asset had an expected life of 3 years and is now fully amortized.

Following the acquisition of Strata on December 24, 2012, the Company recognized an intangible asset of \$1.5 million in respect of a non-compete agreement. This asset had an expected life of 2 years and is now fully amortized.

An amortization expense of \$0.0 million was recognized in 2018 (2017 – \$0.7 million) in selling, general and administrative expenses.

Marketing related

An intangible asset of \$28.4 million was recognized in the second quarter of 2007 in respect of Ethyl Corporation foregoing their entitlement effective April 1, 2007 to a share of the future income stream under the sales and marketing agreements to market and sell TEL. In 2008, contract provisions no longer deemed necessary of \$6.3 million were offset against the intangible asset. The amount attributed to the Octane Additives reporting segment was

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

amortized on a straight-line basis to December 31, 2013 and the amount attributed to the Fuel Specialties reporting segment was amortized on a straight-line basis to December 31, 2017. The asset is now fully amortized.

An amortization expense of \$0.0 million was recognized in 2018 (2017 - \$0.9 million) in cost of goods sold.

Internally developed software

In 2018 we have completed the implementation of our new information system platform for our acquired Huntsman businesses. At December 31, 2018 we had capitalized \$5.2 million (2017 – \$4.4 million) in relation to this internally developed software. This asset has an expected life of 5 years and is being amortized on a straight-line basis over this period.

At December 31, 2018 we had capitalized \$36.7 million (2017 – \$36.7 million) in relation to the phased deployment of our company-wide information system platform to the majority of entities in the group which began in 2013. This asset has an expected life of 5 years from the point in time each deployment is completed and is being amortized on a straight-line basis over these periods.

An amortization expense of \$7.5 million was recognized in 2018 (2017 – \$7.6 million) in selling, general and administrative expenses.

Amortization expense

The aggregate of other intangible asset amortization expense was \$26.3 million (excluding the impact of foreign exchange translation on the balance sheet), \$28.3 million and \$24.2 million in 2018, 2017 and 2016, respectively, of which \$3.4 million, \$4.3 million and \$4.3 million, respectively, was recognized in cost of goods sold, and the remainder was recognized in selling, general and administrative expenses.

Future amortization expense is estimated to be as follows for the next five years:

<u>(in millions)</u>	
2019	\$23.2
2020	\$22.7
2021	\$19.5
2022	\$17.8
2023	\$14.5

Note 9. Pension and Post-Employment Benefits**United Kingdom plan**

The Company maintains a defined benefit pension plan (the “Plan”) covering a number of its current and former employees in the United Kingdom, although it does also have other much

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

smaller pension arrangements in the U.S. and overseas. The Plan is closed to future service accrual but has a large number of deferred and current pensioners. The Projected Benefit Obligation (“PBO”) is based on final salary and years of credited service reduced by social security benefits according to a plan formula. Normal retirement age is 65 but provisions are made for early retirement. The Plan’s assets are invested by several investment management companies in funds holding United Kingdom and overseas equities, United Kingdom and overseas fixed interest securities, index linked securities, property unit trusts and cash or cash equivalents. The trustees’ investment policy is to seek to achieve specified objectives through investing in a suitable mixture of real and monetary assets. The trustees recognize that the returns on real assets, while expected to be greater over the long-term than those on monetary assets, are likely to be more volatile. A mixture across asset classes should nevertheless provide the level of returns required by the Plan to meet its liabilities at an acceptable level of risk for the trustees and an acceptable level of cost to the Company.

In 2018, the Company contributed \$1.0 million in cash to the Plan in accordance with an agreement with the trustees.

The net service cost for the twelve months ended December 31, 2018 was \$1.2 million (twelve months ended December 31, 2017 – \$0.9 million and twelve months ended December 31, 2016 – \$1.0 million) and has been recognized in selling, general and administrative expenses within corporate costs. The following table shows the income statement effect recognized within other income, net:

<u>(in millions)</u>	<u>2018</u>	<u>2017</u>	<u>2016</u>
<i>Plan net pension (credit)/charge:</i>			
Interest cost on PBO	\$ 15.0	\$ 15.2	\$ 20.8
Expected return on plan assets	(22.2)	(24.5)	(29.9)
Amortization of prior service credit	(1.1)	(1.0)	(1.1)
Amortization of actuarial net losses	2.0	5.0	2.6
	<u>\$ (6.3)</u>	<u>\$ (5.3)</u>	<u>\$ (7.6)</u>
<i>Plan assumptions at December 31, (%):</i>			
Discount rate	2.78	2.56	2.48
Inflation rate	2.25	2.20	2.25
Rate of return on plan assets – overall on bid-value	3.05	2.75	3.20
<i>Plan asset allocation by category (%):</i>			
Equity securities	12	38	25
Debt securities	83	53	66
Cash	5	9	9
	<u>100</u>	<u>100</u>	<u>100</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The discount rate used represents the annualized yield based on a cash flow matched methodology with reference to an AA corporate bond spot curve and having regard to the duration of the Plan's liabilities. The inflation rate is derived using a similar cash flow matched methodology as used for the discount rate but having regard to the difference between yields on fixed interest and index linked United Kingdom government gilts. A 0.25% change in the discount rate assumption would change the PBO by approximately \$21 million and the net pension credit for 2018 would change by approximately \$0.5 million. A 0.25% change in the level of price inflation assumption would change the PBO by approximately \$14 million and the net pension credit for 2018 by approximately \$0.6 million.

Movements in PBO and fair value of Plan assets are as follows:

(in millions)	2018	2017
Change in PBO:		
Opening balance	\$721.4	\$710.2
Interest cost	15.0	15.2
Service cost	1.2	0.9
Benefits paid	(43.7)	(37.8)
Actuarial gains	(14.6)	(32.7)
Plan amendments	3.3	0.0
Exchange effect	(39.4)	65.6
Closing balance	<u>\$643.2</u>	<u>\$721.4</u>
Fair value of plan assets:		
Opening balance	\$837.4	\$758.2
Actual benefits paid	(43.7)	(37.8)
Actual contributions by employer	1.1	1.0
Actual return on assets	(10.3)	43.0
Exchange effect	(45.4)	73.0
Closing balance	<u>\$739.1</u>	<u>\$837.4</u>

The current investment strategy of the Plan is to obtain an asset allocation of approximately 85% debt securities and 15% equity securities in order to achieve a more predictable return on assets.

Due to the change in the Plan's investment strategy in 2018 the Plan's assets no longer include index-tracking funds with one investment management company (December 31, 2017 – 30%). The Plan continues to hold approximately 9% (December 31, 2017 – 10%) of the Plan's assets in United Kingdom government gilts. No more than 5% of the Plan's assets were invested in any one individual company's investment funds.

For the vast majority of assets, a market approach is adopted to assess the fair value of the assets, with the inputs being the quoted market prices for the actual securities held in the relevant fund.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Equity securities

Common and preferred stock for which market prices are readily available at the measurement date are valued at the last reported sale price or official closing price on the primary market or exchange on which they are actively traded and are classified in Level 1.

Fixed income securities

Fixed income securities are valued based on quotations received from independent pricing services or from dealers who make markets in such securities and are classified as Level 1.

Insurance contracts

The Company has invested in insurance contracts, known as buy-in contracts. The value of the insurance contract is based on significant unobservable inputs including plan participant medical data, in addition to observable inputs which include expected return on assets and estimated value premium. Therefore, we have classified the contracts as Level 3 investments. Fair value estimates are provided by the external parties and are subsequently reviewed and approved by management.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The fair values of pension assets by level of input were as follows:

(in millions)	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
At December 31, 2018				
Fixed income securities:				
Debt securities issued by non-U.S. governments and government agencies	\$ 67.2	\$	\$	\$ 67.2
Corporate debt securities		406.4		406.4
Other asset-backed securities				
Other financial derivatives		0.5		0.5
Real estate	31.4			31.4
Insurance contracts			142.5	142.5
Investments measured at net asset value ⁽¹⁾				53.0
Total assets at fair value	98.6	406.9	142.5	701.0
Cash	38.1			38.1
Total plan assets	<u>\$ 136.7</u>	<u>\$ 406.9</u>	<u>\$ 142.5</u>	<u>\$ 739.1</u>
At December 31, 2017				
Fixed income securities:				
Debt securities issued by non-U.S. governments and government agencies	\$ 86.0	\$	\$	\$ 86.0
Corporate debt securities	194.5	232.3		426.8
Other asset-backed securities				
Equity securities held for proprietary investment purposes	0.1			0.1
Real estate	34.4			34.4
Insurance contracts			162.8	162.8
Investments measured at net asset value ⁽¹⁾				52.3
Total assets at fair value	315.0	232.3	162.8	762.4
Cash	75.0			75.0
Total plan assets	<u>\$ 390.0</u>	<u>\$ 232.3</u>	<u>\$ 162.8</u>	<u>\$ 837.4</u>

- (1) Certain investments that are measured at fair value using the net asset value per share (or its equivalent) have not been categorized in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The reconciliation of the fair value of the Plan assets measured using significant unobservable inputs was as follows:

<u>(in millions)</u>	<u>Other Assets</u>
Balance at December 31, 2016	\$152.9
Realized/unrealized gains/(losses):	
Relating to assets still held at the reporting date	2.8
Relating to assets sold during the period	0.0
Purchases, issuances and settlements	(7.4)
Exchange effect	14.5
Balance at December 31, 2017	<u>162.8</u>
Realized/unrealized gains/(losses):	
Relating to assets still held at the reporting date	(4.8)
Relating to assets sold during the period	0.0
Purchases, issuances and settlements	(6.7)
Exchange effect	(8.8)
Balance at December 31, 2018	<u>\$142.5</u>

The projected net service cost for the year ending December 31, 2019 is \$0.9 million and will be recognized in selling, general and administrative expenses. The following will be recognized in other income and expense:

<u>(in millions)</u>	
Interest cost on PBO	\$ 15.2
Expected return on plan assets	(21.9)
Amortization of prior service credit	(0.9)
	<u>\$ (7.6)</u>

In total, there will be a net pension credit of \$6.7 million to the Innospec's net income for the year ending December 31, 2019.

The following benefit payments are expected to be made:

<u>(in millions)</u>	
2019	\$ 38.5
2020	\$ 36.6
2021	\$ 36.1
2022	\$ 35.4
2023	\$ 34.3
2024-2028	\$168.7

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

German plan

The Company also maintains an unfunded defined benefit pension plan covering a number of its current and former employees in Germany (the “German plan”). The German plan is closed to new entrants and has no assets.

The net service cost for the German plan for the twelve months ended December 31, 2018 was \$0.2 million (twelve months ended December 31, 2017 – \$0.2 million and twelve months ended December 31, 2016 – \$0.2 million). The following table shows the income statement effect recognized within other income and expense:

<u>(in millions)</u>	<u>2018</u>	<u>2017</u>	<u>2016</u>
<i>Plan net pension charge:</i>			
Interest cost on PBO	\$ 0.2	\$ 0.2	\$ 0.2
Amortization of actuarial net loss	0.4	0.4	0.2
	<u>\$ 0.6</u>	<u>\$ 0.6</u>	<u>\$ 0.4</u>
<i>Plan assumptions at December 31, (%):</i>			
Discount rate	1.90	1.70	1.80
Inflation rate	1.75	1.75	1.75
Rate of increase in compensation levels	2.75	2.75	2.75

Movements in PBO of the German plan are as follows:

<u>(in millions)</u>	<u>2018</u>	<u>2017</u>
<i>Change in PBO:</i>		
Opening balance	\$11.8	\$10.1
Service cost	0.2	0.2
Interest cost	0.2	0.2
Benefits paid	(0.3)	(0.2)
Actuarial losses	0.0	0.2
Exchange effect	(0.6)	1.3
Closing balance	<u>\$11.3</u>	<u>\$11.8</u>

The amount of unrecognized actuarial net losses in other comprehensive loss in respect of the German plan is \$2.1 million, net of tax of \$0.7 million.

Other plans

Company contributions to defined contribution schemes during 2018 were \$8.6 million (2017 – \$7.9 million).

As at December 31, 2018, we have post-employment obligations in our European businesses with a liability of \$4.4 million (December 31, 2017 – \$4.7 million).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Note 10. Income Taxes

A roll-forward of unrecognized tax benefits and associated accrued interest and penalties is as follows:

(in millions)	Interest and Penalties	Unrecognised Tax Benefits	Total
Opening balance at January 1, 2016	\$ 0.3	\$ 3.6	\$ 3.9
Reductions for tax positions of prior periods	(0.1)	(0.6)	(0.7)
Additions for tax positions of prior periods	0.0	0.0	0.0
Additions for current year tax positions	0.0	0.0	0.0
Reductions due to lapsed statute of limitations	(0.1)	(0.8)	(0.9)
Closing balance at 31 December, 2016	0.1	2.2	2.3
Current	0.0	0.0	0.0
Non-current	<u>\$ 0.1</u>	<u>\$ 2.2</u>	<u>\$ 2.3</u>
Opening balance at January 1, 2017	\$ 0.1	\$ 2.2	\$ 2.3
Reductions for tax positions of prior periods	0.0	0.0	0.0
Additions for tax positions of prior periods	0.2	0.5	0.7
Additions for current year tax positions	0.0	0.0	0.0
Reductions due to lapsed statute of limitations	0.0	(0.5)	(0.5)
Closing balance at 31 December, 2017	0.3	2.2	2.5
Current	0.0	0.0	0.0
Non-current	<u>\$ 0.3</u>	<u>\$ 2.2</u>	<u>\$ 2.5</u>
Opening balance at January 1, 2018	\$ 0.3	\$ 2.2	\$ 2.5
Reductions for tax positions of prior periods	0.0	0.0	0.0
Additions for tax positions of prior periods	0.4	11.7	12.1
Additions for current year tax positions	0.0	0.0	0.0
Reductions due to lapsed statute of limitations	(0.1)	(0.5)	(0.6)
Closing balance at 31 December, 2018	0.6	13.4	14.0
Current	0.0	0.0	0.0
Non-current	<u>\$ 0.6</u>	<u>\$ 13.4</u>	<u>\$14.0</u>

All of the \$13.4 million of unrecognized tax benefits would impact our effective tax rate if recognized.

As previously disclosed, the Company and certain U.S. subsidiaries were subject to a federal income tax examination in respect of 2015. The examination was completed in the first quarter of 2018 with no additional cost to the company.

As previously disclosed, tax audits have been opened by the Italian tax authorities in respect of Innospec Performance Chemicals Italia Srl, acquired as part of the Huntsman business, in relation to the period 2011 to 2013 inclusive. The Company believes that additional tax of

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

approximately \$0.5 million, together with associated interest of \$0.2 million, may arise as a result of the 2011 audit. This amount was recorded at December 31, 2017. During 2018, the Company determined that additional tax of approximately \$0.9 million, together with associated interest of \$0.3 million, may arise as a result of the 2012 and 2013 audits collectively. As any additional tax arising as a consequence of the tax audit would be reimbursed by the previous owner under the terms of the sale and purchase agreement, an unrecognized tax benefit of \$1.9 million is recorded, together with an indemnification asset of the same amount to reflect the fact that the final liability would be reimbursed by the previous owner.

In the fourth quarter of 2018, the Company has recorded an uncertain tax position of \$10.8 million. This portion primarily relates to a potential adjustment that could arise as a consequence of the Tax Act, but for which retrospective adjustment to the filed 2017 U.S. federal income tax returns are not permissible.

The Company and its U.S. subsidiaries remain open to examination by the IRS for years 2016 onwards. The Company's subsidiaries in foreign tax jurisdictions are open to examination including Spain (2014 onwards), France (2015 onwards), Germany (2015 onwards), Switzerland (2016 onwards) and the United Kingdom (2017 onwards).

The sources of income before income taxes were as follows:

<u>(in millions)</u>	<u>2018</u>	<u>2017</u>	<u>2016</u>
Domestic	\$ 37.1	\$ 3.1	\$ 16.8
Foreign	94.5	125.0	86.3
	<u>\$131.6</u>	<u>\$128.1</u>	<u>\$103.1</u>

The components of income tax expense are summarized as follows:

<u>(in millions)</u>	<u>2018</u>	<u>2017</u>	<u>2016</u>
Current:			
Federal	\$12.5	\$51.2	\$ 4.4
State and local	2.0	0.9	1.1
Foreign	26.6	21.0	15.3
	<u>41.1</u>	<u>73.1</u>	<u>20.8</u>
Deferred:			
Federal	4.2	(8.1)	(0.7)
State and local	0.3	0.7	(0.3)
Foreign	1.0	0.6	2.0
	<u>5.5</u>	<u>(6.8)</u>	<u>1.0</u>
	<u>\$46.6</u>	<u>\$66.3</u>	<u>\$21.8</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Cash payments for income taxes were \$35.4 million, \$24.2 million and \$23.1 million during 2018, 2017 and 2016, respectively.

The effective tax rate varies from the U.S. federal statutory rate because of the factors indicated below:

(in percent)	2018	2017	2016
Statutory rate	21.0%	35.0%	35.0%
Foreign income inclusions	0.7	2.1	1.0
Foreign tax rate differential	(0.5)	(13.7)	(16.6)
Tax charge/(credit) from previous years	0.7	1.1	(0.7)
Net charge/(credit) from unrecognized tax benefits	0.3	(0.4)	(1.6)
Foreign currency transactions	1.4	(0.9)	2.4
United Kingdom income tax rate reduction	0.0	0.0	(0.6)
Effect of U.S. tax law change	9.3	31.7	0.0
Tax on unremitted earnings	0.9	0.0	0.0
Non-deductible foreign interest	1.3	1.1	0.0
Other items and adjustments, net	0.3	(4.2)	2.2
	<u>35.4%</u>	<u>51.8%</u>	<u>21.1%</u>

The most significant factor impacting our effective tax rate in 2018 is the recognized implications of the Tax Act. On December 22, 2017 the U.S. government enacted comprehensive tax legislation, being the Tax Act. U.S. GAAP requires that the impact of tax legislation is recognized in the period in which the law is enacted. On the same date, SEC staff issued Staff Accounting Bulletin No. 118 (“SAB 118”), which provided guidance on accounting for the tax effects of the Tax Act. SAB 118 provides a measurement period that should not extend beyond one year from the Tax Act enactment date for companies to complete their accounting under ASC 740, *Income Taxes*.

Our accounting for the impact of the Tax Act is now complete:

The FASB has released guidance on the accounting for tax on the global intangible low-taxed income (“GILTI”) provisions of the Tax Act. The guidance indicates that either treating taxes on GILTI inclusions as current period costs, or accounting for deferred taxes on GILTI inclusions are both acceptable subject to an accounting policy election. The Company has elected to account for GILTI as a period cost in the year incurred.

Deemed Repatriation Transition Tax: The deemed repatriation transition tax (“Transition Tax”) is a tax on certain previously untaxed accumulated earnings and profits (“E&P”) of the Company’s non-U.S. subsidiaries. At December 31, 2017, we were able to reasonably estimate the Transition Tax and recorded a provisional Transition Tax obligation of \$47.7 million. On the basis of revised E&P computations that were completed during the reporting period we adjusted our Transition Tax estimate to \$61.1 million. Net of related

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

consequential impacts recorded in our 2017 U.S. federal income tax return, we have recorded an additional \$12.3 million income tax expense in the fourth quarter. Our accounting in relation to the Transition Tax is now complete.

Reduction of U.S. federal income tax rate: The Tax Act reduced the federal income tax rate from 35 per cent to 21 per cent, effective January 1, 2018. We were able to reasonably estimate the effect of the reduction in the tax rate on our U.S. deferred tax assets and liabilities, and recorded a net provisional reduction in our deferred income tax liabilities of \$7.1 million with a corresponding net adjustment of \$7.1 million of deferred income tax benefit at December 31, 2017. No changes have been made to these adjustments during 2018 and our accounting for the reduction in the rate is now complete.

Indefinite reinvestment assertion: In previous periods, the Company did not recognize a deferred tax liability related to unremitted foreign earnings as the Company did not expect to make a repatriation in the foreseeable future. At December 31, 2018, the Company has changed its assertion with respect to the excess of the amount for financial reporting over the tax basis of investments in foreign subsidiaries. Additional deferred income taxes of \$1.1 million have been recorded, with a corresponding adjustment of \$1.1 million to deferred income tax expense.

As a consequence of the Company having operations outside of the U.S., it is exposed to foreign currency fluctuations. These have had a negative impact on the effective tax rate in 2018.

In the United Kingdom, tax legislation prohibits a tax deduction in relation to certain intercompany interest expense arising. This has also had a negative impact on the effective tax rate in 2018.

Other items do not have a material impact on the effective tax rate.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Details of deferred tax assets and liabilities are analysed as follows:

<u>(in millions)</u>	<u>2018</u>	<u>2017</u>
Deferred tax assets:		
Stock compensation	\$ 4.9	\$ 4.3
Net operating loss carry forwards	8.8	15.9
Other intangible assets	5.6	4.8
Accretion expense	3.3	3.3
Restructuring provision	1.9	0.0
Other	4.8	4.5
Subtotal	<u>29.3</u>	<u>32.8</u>
Less valuation allowance	0.0	0.0
Total net deferred tax assets	<u>\$ 29.3</u>	<u>\$ 32.8</u>
Deferred tax liabilities:		
Property, plant and equipment	\$(17.1)	\$(16.7)
Intangible assets including goodwill	(28.1)	(27.0)
Pension asset	(15.0)	(18.3)
Investment impairment recapture	(2.0)	(3.5)
Customer relationships	(4.9)	(5.8)
Unremitted overseas earnings	(1.1)	0.0
Other	(0.5)	0.0
Total deferred tax liabilities	<u>\$(68.7)</u>	<u>\$(71.3)</u>
Net deferred tax liability	<u>\$(39.4)</u>	<u>\$(38.5)</u>
Deferred tax assets	\$ 8.8	\$ 6.5
Deferred tax liabilities	(48.2)	(45.0)
	<u>\$(39.4)</u>	<u>\$(38.5)</u>

The Company evaluates deferred tax assets to determine whether it is more likely than not that they will be realized. Deferred tax assets are reviewed each period on a tax jurisdiction by tax jurisdiction basis to analyze whether there is sufficient positive evidence to support realizability. As a result of the Company's assessment of its deferred tax assets at December 31, 2018, the Company considers it more likely than not it will recover the full benefit of its deferred tax assets and no valuation allowance is required.

Should it be determined in the future that it is no longer more likely than not that these assets will be realized, a valuation allowance would be required, and the Company's operating results would be adversely affected during the period in which such a determination would be made.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Gross net operating loss carry forwards of \$36.8 million result in a deferred tax asset of \$8.8 million. The net operating loss carry forwards arose in the U.S. and in four of the Company's foreign subsidiaries. Net operating loss carry forwards of \$2.3 million arose from state and federal tax losses in prior periods in certain of the Company's U.S. subsidiaries. It is expected that sufficient taxable profits will be generated in the U.S. against which the federal net operating loss carry forwards of \$1.0 million can be relieved prior to their expiration in 2037, and the state net operating loss carry forwards of \$1.3 million can be relieved before their expiration in the period 2022 to 2037. The net operating loss carry forward in four of the Company's foreign subsidiaries totalling \$34.4 million arose in prior and current periods and it is expected that sufficient taxable profits will be generated against which these net operating loss carry forwards can be relieved. These losses can be carried forward indefinitely without expiration.

Note 11. Long-Term Debt

Long-term debt consists of the following:

<u>(in millions)</u>	<u>2018</u>	<u>2017</u>
Revolving credit facility	\$126.0	\$121.0
Term loan	82.5	99.0
Deferred finance costs	(0.9)	(1.6)
	207.6	218.4
Less current portion	(21.4)	(15.8)
	<u>\$186.2</u>	<u>\$202.6</u>

On December 14, 2016, Innospec and certain subsidiaries of the Company entered into a Third Amendment and Restatement Agreement with various lenders which amends and restates the Company's credit facility agreement dated December 14, 2011, as amended and restated on August 28, 2013 and November 6, 2015 (the "Pre-Existing Credit Agreement" the Pre-Existing Credit Agreement, as amended and restated pursuant to the Third Amendment and Restatement Agreement, being the "Amended Credit Agreement.")

The Amended Credit Agreement retains the \$200.0 million revolving credit facility available to the Company and adds a term loan facility of \$110.0 million. The termination date of the revolving facility remains November 6, 2020. Repayments for the term loan of \$11.0 million and \$16.5 million were made on December 29, 2017 and December 28, 2018, respectively. A further installment of \$22.0 million is due on December 28, 2019, with the outstanding balance due on November 6, 2020.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

<u>(in millions)</u>	<u>2018</u>	<u>2017</u>
Gross cost at January 1	<u>\$ 2.7</u>	<u>\$ 2.7</u>
Accumulated amortization at January 1	<u>\$(1.1)</u>	<u>\$(0.5)</u>
Amortization in the year	<u>(0.7)</u>	<u>(0.6)</u>
	<u>\$(1.8)</u>	<u>\$(1.1)</u>
Net book value at December 31	<u>\$ 0.9</u>	<u>\$ 1.6</u>

Amortization expense was \$0.7 million, \$0.6 million and \$0.4 million in 2018, 2017 and 2016, respectively. The charge is included in interest expense, see Note 2 of the Notes to the Consolidated Financial Statements.

The obligations of the Company under the credit facilities are secured obligations and guaranteed by certain subsidiaries of the Company. Amounts available under the revolving facility may be borrowed in U.S. dollars, Euros, British pounds and other freely convertible currencies.

The Company's credit facilities contain restrictive clauses which may constrain our activities and limit our operational and financial flexibility. The facility obliges the lenders to comply with a request for utilization of finance unless there is an event of default outstanding. Events of default are defined in the credit facility and include a material adverse change to our assets, operations or financial condition. The facility contains a number of restrictions that limit our ability, amongst other things, and subject to certain limited exceptions, to incur additional indebtedness, pledge our assets as security, guarantee obligations of third parties, make investments, undergo a merger or consolidation, dispose of assets, or materially change our line of business.

In addition, the credit facilities contain terms which, if breached, would result in it becoming repayable on demand. It requires, among other matters, compliance with the following financial covenant ratios measured on a quarterly basis: (1) the ratio of net debt to EBITDA shall not be greater than 3.0:1 and (2) the ratio of EBITDA to net interest shall not be less than 4.0:1.

Management has determined that the Company has not breached these covenants throughout the period to December 31, 2018 and does not expect to breach these covenants for the next 12 months. The credit facility is secured by a number of fixed and floating charges over certain assets which include key operating sites of the Company and its subsidiaries.

The weighted average rate of interest on borrowings was 3.32% at December 31, 2018 and 2.59% at December 31, 2017. Payments of interest on long-term debt were \$6.5 million, \$7.2 million and \$2.6 million in 2018, 2017 and 2016, respectively.

The net cash outflows in respect of refinancing costs were \$0.0 million, \$0.0 million and \$1.2 million in 2018, 2017 and 2016, respectively.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Note 12. Plant Closure Provisions

The principal site giving rise to environmental remediation liabilities is the manufacturing site at Ellesmere Port in the United Kingdom, which management believes is the last ongoing manufacturer of TEL. There are also environmental remediation liabilities on a much smaller scale in respect of our other manufacturing sites in the U.S. and Europe. The liability for estimated closure costs of Innospec’s manufacturing facilities includes costs for decontamination and environmental remediation activities (“remediation”) when demand for TEL diminishes.

Movements in the provisions are summarized as follows:

<u>(in millions)</u>	<u>2018</u>	<u>2017</u>	<u>2016</u>
Total at January 1	\$46.1	\$39.5	\$37.7
Charge for the period	6.8	5.9	4.7
Measurement period adjustment on acquisition	0.0	2.8	0.0
Utilized in the period	(3.1)	(2.4)	(2.7)
Exchange effect	(0.3)	0.3	(0.2)
Total at December 31	49.5	46.1	39.5
Due within one year	(5.9)	(5.2)	(6.7)
Due after one year	<u>\$43.6</u>	<u>\$40.9</u>	<u>\$32.8</u>

Amounts due within one year refer to provisions where expenditure is expected to arise within one year of the balance sheet date. Remediation costs are recognized in cost of goods sold.

The provisions for remediation represent the Company’s liability for environmental liabilities and asset retirement obligations. The charge for the period in 2018 represents the accretion expense recognized of \$4.0 million and a further \$2.8 million primarily in respect of changes in the expected cost and scope of future remediation activities.

In 2017, we recognized \$2.8 million of asset retirement obligations, in relation to the acquisition of our European Performance Chemicals business, as an increase in the value of the tangible assets acquired. This is being depreciated over the remaining useful economic life of those assets.

We recognize environmental liabilities when they are probable and costs can be reasonably estimated, and asset retirement obligations when there is a legal obligation and costs can be reasonably estimated. The Company has to anticipate the program of work required and the associated future expected costs, and comply with environmental legislation in the countries in which it operates or has operated in.

Remediation expenditure utilized provisions of \$3.1 million, \$2.4 million and \$2.7 million in 2018, 2017 and 2016, respectively.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)**Note 13. Fair Value Measurements**

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). The Company utilizes a mid-market pricing convention for valuing the majority of its assets and liabilities measured and reported at fair value. The Company utilizes market data or assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborated or generally unobservable. The Company primarily applies the market approach for recurring fair value measurements and endeavors to utilize the best available information. Accordingly, the Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. The Company is able to classify fair value balances based on the observability of those inputs. The Company gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurement) and the lowest priority to unobservable inputs (Level 3 measurement). Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The Company's assessment of the significance of a particular input to the fair value measurement requires judgment and may affect the valuation of fair value assets and liabilities and their placement within the fair value hierarchy Levels. In 2018, the Company evaluated the fair value hierarchy levels assigned to its assets and liabilities, and concluded that there should be no transfers into or out of Levels 1, 2 and 3.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The following table presents the carrying amount and fair values of the Company's assets and liabilities measured on a recurring basis:

(in millions)	December 31, 2018		December 31, 2017	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Assets				
Non-derivatives:				
Cash and cash equivalents	\$ 123.1	\$123.1	\$ 90.2	\$ 90.2
Derivatives (Level 1 measurement):				
Other current and non-current assets:				
Foreign currency forward exchange contracts	0.0	0.0	1.1	1.1
Interest rate swaps	1.9	1.9	1.5	1.5
Liabilities				
Non-derivatives:				
Long-term debt (including current portion)	\$ 207.6	\$207.6	\$ 218.4	\$218.4
Finance leases (including current portion)	3.3	3.3	5.9	5.9
Derivatives (Level 1 measurement):				
Other non-current liabilities:				
Foreign currency forward exchange contracts	0.7	0.7	0.0	0.0
Non-financial liabilities (Level 3 measurement):				
Stock equivalent units	15.1	15.1	13.6	13.6

The following methods and assumptions were used to estimate the fair values of financial instruments:

Cash and cash equivalents: The carrying amount approximates fair value because of the short-term maturities of such instruments.

Long-term debt and finance leases: Long-term debt principally comprises the term loan and revolving credit facility, which are shown net of deferred finance costs that have been capitalized. The fair value of long-term debt approximates to the carrying value, as the discounting to its present value is offset by the interest rate swaps. Finance leases relate to certain fixed assets in our fuel specialties and oilfield services businesses. The carrying amount of long-term debt and finance leases approximates to the fair value.

Derivatives: The fair value of derivatives relating to foreign currency forward exchange contracts and interest rate swaps are derived from current settlement prices and comparable contracts using current assumptions. Foreign currency forward exchange contracts primarily

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

relate to contracts entered into to hedge future known transactions or hedge balance sheet net cash positions. The movements in the carrying amounts and fair values of these contracts are largely due to changes in exchange rates against the U.S. dollar. Interest rate swaps relate to contracts taken out to hedge interest rate risk on a portion of our credit facilities borrowing.

Stock equivalent units: The fair values of stock equivalent units are calculated at each balance sheet date using either the Black-Scholes or Monte Carlo method.

Note 14. Derivative Instruments and Risk Management

The Company has limited involvement with derivative instruments and does not trade them. The Company does use derivatives to manage certain interest rate, foreign currency exchange rate and raw material cost exposures, as the need arises.

The Company enters into interest rate swap contracts to reduce interest rate risk on its core debt. As at December 31, 2018, interest rate swaps with a notional value of \$132.5 million were in place. Fixed interest rates payable under the interest rate swaps vary from 1.42% to 1.67%. Interest rate swaps in place to hedge interest rate risk on the term loan are for a notional value that matches the repayment profile of the term loan. These interest rate swap contracts have been designated as hedging instruments, and their impact on other comprehensive loss for 2018 was a gain of \$0.4 million (2017 – gain \$1.1 million).

The Company enters into various foreign currency forward exchange contracts to minimize currency exchange rate exposure from expected future cash flows. As at December 31, 2018, foreign currency forward exchange contracts with a notional value of \$108.7 million were in place, with maturity dates of up to one year from the date of inception. These foreign currency forward exchange contracts have not been designated as hedging instruments, and their impact on the income statement for 2018 was a loss of \$1.8 million (2017 – loss \$0.9 million).

As at December 31, 2018 and December 31, 2017 the Company did not hold any raw material derivatives.

The Company sells a range of specialty chemicals to major oil refineries and chemical companies throughout the world. Credit limits, ongoing credit evaluation and account monitoring procedures are intended to minimize bad debt risk. Collateral is not generally required.

Note 15. Commitments and Contingencies

Operating leases

The Company has commitments under operating leases primarily for office space, motor vehicles and various items of computer and office equipment. The leases are expected to be renewed and replaced in the normal course of business. Rental expense was \$6.1 million in

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

2018, \$5.5 million in 2017 and \$5.2 million in 2016. Future commitments under non-cancelable operating leases are as follows:

<u>(in millions)</u>	
2019	\$ 6.5
2020	4.5
2021	3.2
2022	2.3
2023	2.1
Thereafter	4.4
	<u>\$23.0</u>

Environmental remediation obligations

Commitments in respect of environmental remediation obligations are disclosed in Note 12 of the Notes to the Consolidated Financial Statements.

Contingencies***Legal matters***

While we are involved from time to time in claims and legal proceedings that result from, and are incidental to, the conduct of our business including business and commercial litigation, employee and product liability claims, there are no material pending legal proceedings to which the Company or any of its subsidiaries is a party, or of which any of their property is subject. It is possible however, that an adverse resolution of an unexpectedly large number of such individual items could in the aggregate have a material adverse effect on results of operations for a particular year or quarter.

Guarantees

The Company and certain of the Company's consolidated subsidiaries are contingently liable for certain obligations of affiliated companies primarily in the form of guarantees of debt and performance under contracts entered into as a normal business practice. This includes guarantees of non-U.S. excise taxes and customs duties. As at December 31, 2018, such guarantees which are not recognized as liabilities in the consolidated financial statements amounted to \$5.0 million (December 31, 2017 – \$3.5 million).

Under the terms of the guarantee arrangements, generally the Company would be required to perform should the affiliated company fail to fulfill its obligations under the arrangements. In some cases, the guarantee arrangements have recourse provisions that would enable the Company to recover any payments made under the terms of the guarantees from securities held of the guaranteed parties' assets.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The Company and its affiliates have numerous long-term sales and purchase commitments in their various business activities, which are expected to be fulfilled with no adverse consequences material to the Company.

Note 16. Stockholders' Equity

<u>(number of shares in thousands)</u>	<u>Common Stock</u>			<u>Treasury Stock</u>		
	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2018</u>	<u>2017</u>	<u>2016</u>
At January 1	29,555	29,555	29,555	5,204	5,483	5,453
Exercise of options	0	0	0	(103)	(296)	(152)
Stock purchases	0	0	0	20	17	182
At December 31	<u>29,555</u>	<u>29,555</u>	<u>29,555</u>	<u>5,121</u>	<u>5,204</u>	<u>5,483</u>

At December 31, 2018, the Company had authorized common stock of 40,000,000 shares (2017 - 40,000,000).

Note 17. Stock-Based Compensation PlansStock option plans

The Company has two stock option plans, the Omnibus Long-Term Incentive Plan and the Sharesave Plan 2008 under which it can currently grant awards. The stock options have vesting periods ranging from 24 months to 5 years and in all cases stock options granted expire within 10 years of the date of grant. All grants are at the sole discretion of the Compensation Committee of the Board of Directors. Grants may be priced at market value or at a premium or discount. The aggregate number of shares of common stock reserved for issuance which can be granted under the plans is 2,550,000.

The fair value of stock options is measured on the grant date using either the Black-Scholes model, or in cases where performance criteria are dependent upon external factors such as the Company's stock price, using a Monte Carlo model. The following weighted average assumptions were used to determine the grant-date fair value of options:

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Dividend yield	1.11%	0.96%	1.38%
Expected life	5 years	5 years	5 years
Volatility	25.6%	25.3%	25.1%
Risk free interest rate	2.74%	1.50%	0.91%

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The following table summarizes the transactions of the Company's stock option plans for the year ended December 31, 2018:

	Number of Options	Weighted Average Exercise Price	Weighted Average Grant-Date Fair Value
Outstanding at December 31, 2017	357,666	\$ 13.74	\$ 35.69
Granted – at discount	287,966	\$ 45.21	\$ 34.98
– at market value	18,850	\$ 68.20	\$ 16.23
Exercised	(103,562)	\$ 11.00	\$ 29.78
Forfeited	(15,671)	\$ 24.35	\$ 25.38
Outstanding at December 31, 2018	<u>545,249</u>	\$ 32.46	\$ 36.06

At December 31, 2018, there were 41,014 stock options that were exercisable, 1,600 had performance conditions attached.

The Company's policy is to issue shares from treasury stock to holders of stock options who exercise those options, but if sufficient treasury stock is not available, the Company will issue previously unissued shares of stock to holders of stock options who exercise options.

The stock option compensation cost for 2018, 2017 and 2016 was \$4.9 million, \$4.2 million and \$3.3 million, respectively. The total intrinsic value of options exercised in 2018, 2017 and 2016 was \$3.2 million, \$2.9 million and \$2.8 million, respectively.

The total compensation cost related to non-vested stock options not yet recognized at December 31, 2018 was \$10.7 million and this cost is expected to be recognized over the weighted-average period of 2.19 years.

In 2018, the Company recorded a current tax benefit of \$1.2 million in respect of stock option compensation (2017 – \$3.0 million). This amount is inclusive of excess tax benefits.

No stock options awards were modified in 2018, 2017 or 2016.

Stock equivalent units

The Company awards Stock Equivalent Units ("SEUs") from time to time as a long-term performance incentive. SEUs are cash settled equity instruments conditional on certain performance criteria and linked to the Innospec Inc. share price. SEUs have vesting periods ranging from 11 months to 4 years and in all cases SEUs granted expire within 10 years of the date of grant. Grants may be priced at market value or at a premium or discount. There is no limit to the number of SEUs that can be granted. As at December 31, 2018 the liability for SEUs of \$15.1 million is located in accrued liabilities in the consolidated balance sheets until they are cash settled.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The fair value of SEUs is measured at the balance sheet date using either the Black-Scholes model, or in cases where performance criteria are dependent upon external factors such as the Company's stock price, using a Monte Carlo model. The following assumptions were used to determine the fair value of SEUs at the balance sheet dates:

	<u>2018</u>	<u>2017</u>	<u>2016</u>
Dividend yield	1.44%	1.09%	0.98%
Volatility	27.2%	25.4%	25.2%
Risk free interest rate	2.46%	1.98%	1.47%

The following table summarizes the transactions of the Company's SEUs for the year ended December 31, 2018:

	<u>Number of SEUs</u>	<u>Weighted Average Exercise Price</u>	<u>Weighted Average Grant-Date Fair Value</u>
Outstanding at December 31, 2017	400,342	\$ 3.10	\$ 46.65
Granted – at discount	115,229	\$ 2.36	\$ 57.16
– at market value	5,658	\$ 68.20	\$ 16.23
Exercised	(78,239)	\$ 5.40	\$ 30.44
Forfeited	(24,054)	\$ 0.96	\$ 41.58
Outstanding at December 31, 2018	<u>418,936</u>	\$ 3.47	\$ 52.45

At December 31, 2018, there were 34,710 SEUs that were exercisable, 32,005 had performance conditions attached.

The charges for SEUs are spread over the life of the award subject to a revaluation to fair value each quarter. The revaluation may result in a charge or a credit to the income statement in the quarter dependent upon our share price and other performance criteria.

The SEU compensation cost for 2018, 2017 and 2016 was \$5.7 million, \$6.6 million and \$4.7 million, respectively. The total intrinsic value of SEUs exercised in 2018, 2017 and 2016 was \$2.7 million, \$1.7 million and \$1.8 million, respectively.

The weighted-average remaining vesting period of non-vested SEUs is 1.73 years.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Note 18. Reclassifications out of Accumulated Other Comprehensive Loss

Reclassifications out of accumulated other comprehensive loss for 2018 were:

(in millions)	Amount Reclassified from AOCL	Affected Line Item in the Statement where Net Income is Presented
Details about AOCL Components		
Defined benefit pension plan items:		
Amortization of prior service credit	\$ (1.1)	See (1) below
Amortization of actuarial net losses	2.0	See (1) below
	0.9	Total before tax
	(0.1)	Income tax expense
Total reclassifications	<u>\$ 0.8</u>	Net of tax

(1) These items are included in the computation of net periodic pension cost. See Note 9 of the Notes to the Consolidated Financial Statements for additional information.

Changes in accumulated other comprehensive loss for 2018, net of tax, were:

(in millions)	Derivative Instruments	Defined Benefit Pension Plan Items	Cumulative Translation Adjustments	Total
Balance at December 31, 2017	<u>\$ 1.2</u>	<u>\$ (3.2)</u>	<u>\$ (36.5)</u>	<u>\$(38.5)</u>
Other comprehensive income before reclassifications	0.3	0.0	(22.6)	(22.3)
Amounts reclassified from AOCL	0.0	0.8	0.0	0.8
Actuarial net gains arising during the year	0.0	(15.7)	0.0	(15.7)
Net current period other comprehensive income	<u>0.3</u>	<u>(14.9)</u>	<u>(22.6)</u>	<u>(37.2)</u>
Balance at December 31, 2018	<u>\$ 1.5</u>	<u>\$ (18.1)</u>	<u>\$ (59.1)</u>	<u>\$(75.7)</u>

Note 19. Recently Issued Accounting Pronouncements

In March 2017, the FASB issued ASU 2017-07, Compensation-Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. ASU 2017-07 requires companies to present the service cost component of net benefit cost in the same line items in which they report compensation cost. All other components of net benefit cost are presented outside operating income. The new standard is effective for annual periods beginning after December 15, 2017, including interim periods within those fiscal years. Adopting the new standard on January 1, 2018 has resulted in a restatement of the prior period comparatives with a reduction to operating income for the year ending December 31, 2017 and 2016 of \$4.7 million and \$7.2 million, respectively and a corresponding increase in other non-operating income.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

In February 2016, the FASB issued Accounting Standards Update (ASU) 2016-02, Revision to Lease Accounting, ASC Topic 842 which amends ASC Topic 840, Leases. The ASU requires lessees to recognize a right-of-use asset and a lease liability for virtually all of their leases (other than leases that meet the definition of a short-term lease). The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. In July 2018, the FASB issued ASU 2018-11: Leases – Targeted Improvements, to provide entities with relief from the costs of implementing certain aspects of the new leasing standard, ASU 2016-02. Innospec has evaluated ASU 2018-11 and intends to use the optional transitional method, which allows companies to use the effective date as the date of the initial application on transition and not adjust comparative financial information or make the new required disclosures for periods prior to the effective date. Due to the number of leases the Company has, we believe the Standard will have a material impact on our consolidated balance sheet. The most significant impact will be the recognition of Right-of-use assets and lease liabilities for operating leases. The Company does not believe adoption of the standard will have a significant impact on its consolidated statements of income, equity and cash flows. The Company is still assessing the effect of the standard on its ongoing financial reporting.

Note 20. Related Party Transactions

Mr. Robert I. Paller has been a non-executive director of the Company since November 1, 2009. The Company has retained and continues to retain Smith, Gambrell & Russell, LLP (“SGR”), a law firm with which Mr. Paller holds a position. In 2018, 2017 and 2016 the Company incurred fees payable to SGR of \$0.3 million, \$0.4 million and \$0.5 million, respectively. As at December 31, 2018 and at December 31, 2017, the Company did not have any amounts outstanding due to SGR.

Mr. David F. Landless is a non-executive director of Ausurus Group Limited which owns European Metal Recycling Limited (“EMR”). The Company has sold scrap metal to EMR in 2018 for a value of \$0.3 million. A tendering process is operated to select the best buyer for the scrap metal. As at December 31, 2018 EMR owed \$0.1 million for scrap metal purchased in the last quarter of 2018.

Note 21. Subsequent Events

The Company has evaluated subsequent events through the date that the consolidated financial statements were issued, and has concluded that no additional disclosures are required in relation to events subsequent to the balance sheet date.

Item 9 Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Item 9A Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Based on an evaluation carried out as of the end of the period covered by this report, under the supervision and with the participation of our management, our Chief Executive Officer and our Chief Financial Officer concluded that the Company's "disclosure controls and procedures" (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934) were effective as of December 31, 2018.

Management's Report on Internal Control Over Financial Reporting

Our management, including the Chief Executive Officer and the Chief Financial Officer, is responsible for establishing and maintaining adequate internal control over financial reporting (within the meaning of Rule 13a-15(f) under the Securities Exchange Act of 1934). The Company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the United States of America.

Internal control over financial reporting includes those policies and procedures that:

- pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of our assets;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America and that our receipts and expenditures are being made only in accordance with authorization of our management and directors; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of assets that could have a material effect on the consolidated financial statements.

Due to its inherent limitations, management does not believe that internal control over financial reporting will prevent or detect all errors or fraud. In addition, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Based on criteria in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission the evaluation of our management,

including the Chief Executive Officer and the Chief Financial Officer, concluded that the Company did maintain effective internal control over financial reporting as of December 31, 2018.

Our independent registered public accounting firm KPMG LLP, has audited our consolidated financial statements and the effectiveness of our internal control over financial reporting as of December 31, 2018. Their report is included in Item 8 of this Annual Report on Form 10-K.

Changes in Internal Controls over Financial Reporting

The Company is continuously seeking to improve the efficiency and effectiveness of its operations and of its internal controls. This is intended to result in refinements to processes throughout the Company.

There were no changes to our internal control over financial reporting which were identified in connection with the evaluation required by paragraph (d) of Rules 13a-15 and 15d-15 under the Securities Exchange Act of 1934, have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Item 9B Other Information

None.

PART III

Item 10 Directors, Executive Officers and Corporate Governance

The information set forth under the headings “Re-Election of Three Class III Directors”, “Information about the Board of Directors,” “Information about the Executive Officers” and “Section 16(a) Beneficial Ownership Reporting Compliance” in the Proxy Statement for the Annual Meeting of Stockholders to be held on May 8, 2019 (“the Proxy Statement”) is incorporated herein by reference.

The Board of Directors has adopted a Code of Ethics that applies to the Company’s directors, officers and employees, including the Chief Executive Officer, Chief Financial Officer and Principal Accounting Officer. Any stockholder who would like to receive a copy of our Code of Ethics, our Corporate Governance Guidelines or any charters of our Board’s committees may obtain them without charge by writing to the General Counsel and Chief Compliance Officer, Innospec Inc., 8310 South Valley Highway, Suite 350, Englewood, Colorado, 80112, e-mail investor@innospecinc.com. These and other documents can also be accessed via the Company’s web site, www.innospecinc.com.

The Company intends to disclose on its’ web site www.innospecinc.com any amendments to, or waivers from, its’ Code of Ethics that are required to be publicly disclosed pursuant to the rules of the SEC or NASDAQ.

Information regarding the Audit Committee of the Board of Directors, including membership and requisite financial expertise, set forth under the headings “Corporate Governance – Board Committees – Audit Committee” in the Proxy Statement is incorporated herein by reference.

Information regarding the procedures by which stockholders may recommend nominees to the Board of Directors set forth under the heading “Corporate Governance – Board Committees – Nominating and Governance Committee” in the 2019 Proxy Statement is incorporated herein by reference.

Item 11 Executive Compensation

The information set forth under the headings “Executive Compensation,” “Corporate Governance – Board Committees – Compensation Committee – Compensation Committee Interlocks and Insider Participation” and “Compensation Committee Report” in the Proxy Statement is incorporated herein by reference.

Item 12 Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information set forth under the heading “Information About our Common Stock Ownership” in the Proxy Statement is incorporated herein by reference.

Shares Authorized for Issuance Under Equity Compensation Plans

The information set forth in the table under the heading “Equity Compensation Plans” in the Proxy Statement is incorporated herein by reference.

Item 13 Certain Relationships and Related Transactions, and Director Independence

The information set forth under the headings “Related Person Transactions and Relationships”, “Related Person Transactions Approval Policy” and “Corporate Governance – Director Independence” in the Proxy Statement is incorporated herein by reference.

Item 14 Principal Accountant Fees and Services

In previous years our Independent Registered Public Accounting Firm was KPMG Audit Plc.. Due to an internal reorganization of KPMG’s U.K. operations, KPMG LLP replaced KPMG Audit Plc. as the Company’s Independent Registered Public Accounting Firm for the year ended December 31, 2018.

Information regarding fees and services related to the Company’s independent registered public accounting firm, KPMG LLP, is provided under the heading “Principal Accountant Fees and Services” in the Proxy Statement and is incorporated herein by reference. Information regarding the Audit Committee’s pre-approval policies and procedures is provided under the heading “Audit Committee Pre-approval Policies and Procedures” in the Proxy Statement and is incorporated herein by reference.

PART IV

Item 15 Exhibits and Financial Statement Schedules

(1) Financial Statements

The Consolidated Financial Statements (including notes) of Innospec Inc. and its subsidiaries, together with the report of KPMG LLP dated February 20, 2019, are set forth in Item 8.

(2) Financial Statement Schedules

Financial statement schedules have been omitted since they are either included in the financial statements, not applicable or not required.

(3) Exhibits

- 2.1 [Amended and Restated Share and Asset Purchase Agreement, dated as of December 22, 2016, by and between Huntsman Investments \(Netherlands\) B.V. and Innospec International Ltd \(Incorporated by reference to Exhibit 2.1 of the Company's Form 8-K on January 3, 2017\).](#)
- 3.1 [Amended and Restated Certificate of Incorporation of the Company \(Incorporated by reference to Exhibit 3.1 of the Company's Form 10-K on March 16, 2006\).](#)
- 3.2 [Amended and Restated By-laws of the Company \(Incorporated by reference to Exhibit 3.1 of the Company's Form 8-K on November 13, 2015\).](#)
- 10.1 [Executive Service Agreement of Mr. Philip J Boon dated June 1, 2009 \(Incorporated by reference to Exhibit 10.1 of the Company's Form 8-K on May 27, 2009\). *](#)
- 10.2 [Contract of Employment, Mr. Ian McRobbie \(Incorporated by reference to Exhibit 10.23 of the Company's Form 10-K on March 28, 2003\). *](#)
- 10.3 [Contract of Employment, Dr. Catherine Hessner \(Incorporated by reference to Exhibit 10.26 of the Company's Form 10-K on March 31, 2005\). *](#)
- 10.4 [Contract of Employment, Mr. Patrick Williams, dated October 11, 2005, \(Incorporated by reference to Exhibit 99.1 of the Company's Form 8-K on October 12, 2005\) and Executive Service Agreement dated April 2, 2009. \(Incorporated by reference to Exhibit 10.1 of the Company's Form 8-K on April 3, 2009\). *](#)

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- 10.5 [Contract of Employment, Mr. Ian Cleminson, dated June 30, 2006 \(Incorporated by reference to Exhibit 99.2 of the Company's Form 8-K on June 30, 2006\). *](#)
- 10.6 [Innospec Inc. Performance Related Stock Option Plan 2008 \(Incorporated by reference to Appendix A of the Company's Proxy Statement on April 1, 2011\). *](#)
- 10.7 [Innospec Inc. Company Share Option Plan 2008 \(Incorporated by reference to Appendix B of the Company's Proxy Statement on April 1, 2011\). *](#)
- 10.8 [Innospec Inc. Non-Employee Directors' Stock Option Plan 2008 \(Incorporated by reference to Appendix C of the Company's Proxy Statement on April 1, 2011\). *](#)
- 10.9 [Innospec Inc. Sharesave Plan 2008 \(Incorporated by reference to Appendix D of the Company's Proxy Statement on March 31, 2008\). *](#)
- 10.10 [Innospec Inc. Executive Co-Investment Stock Plan 2004, as amended by the First Amendment 2006 \(Incorporated by reference to Exhibit 10.10 of the Company's Form 10-K on February 17, 2012\). *](#)
- 10.11 [Contract of Employment, Mr. David E. Williams, dated September 17, 2009 \(Incorporated by reference to Exhibit 10.1 of the Company's Form 8-K on September 14, 2009\). *](#)
- 10.12 [Form of Indemnification Agreement for individual who is an officer \(Incorporated by reference to Exhibit 10.1 of the Company's Form 8-K filed on February 27, 2014\).](#)
- 10.13 [Form of Indemnification Agreement for individual who is a director \(Incorporated by reference to Exhibit 10.2 of the Company's Form 8-K filed on February 27, 2014\).](#)
- 10.14 [Form of Indemnification Agreement for individual who is an officer and director \(Incorporated by reference to Exhibit 10.3 of the Company's Form 8-K filed on February 27, 2014\).](#)
- 10.15 [Employment contract for Brian Watt \(Incorporated by Reference to Exhibit 10.4 of the Company's Form 10-Q filed on May 7, 2014\). *](#)
- 10.16 [Innospec Inc. 2014 Long-Term Incentive Plan \(Incorporated by Reference to Exhibit 10.5 of the Company's Form 10-Q filed on May 7, 2014\). *](#)

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- 10.17 [Increase Confirmation Letter, dated July 31, 2014, among the Company, certain subsidiaries of the Company, and U.S. Bank N.A. \(Incorporated by reference to Exhibit 10.1 of the Company's Form 8-K filed on July 31, 2014\).](#)
- 10.18 [Second Amendment and Restatement Agreement, dated November 6, 2015, relating to the Facility Agreement dated December 14, 2011 as previously amended and restated on August 28, 2013 \(Incorporated by reference to Exhibit 10.1 of the Company's Form 8-K on November 9, 2015\).](#)
- 10.19 [Executive Service Letter to Mr. Philip J Boon dated October 15, 2015 \(Incorporated by reference to Exhibit 10.24 of the Company's Form 10-K on February 17, 2016\). *](#)
- 10.20 [Third Amendment and Restatement Agreement with various lenders, dated December 14, 2016, which amends and restates the Company's credit facility agreement dated December 14, 2011, as amended and restated on August 28, 2013 and November 6, 2015 \(Incorporated by reference to Exhibit 10.1 of the Company's Form 8-K on December 16, 2016\).](#)
- 10.21 [Innospec Inc. 2018 Omnibus Long-Term Incentive Plan \(Incorporated by reference to Exhibit 10.1 to the Registrant's Form 8-K filed May 10, 2018\).](#)
- 10.22 [Innospec Inc. ShareSave Plan 2008 \(as amended and restated\) \(Incorporated by reference to Exhibit 10.2 to the Registrant's Form 8-K filed May 10, 2018\).](#)
- 12.1 [Computation of Financial Ratios \(filed herewith\).](#)
- 14 [The Innospec Inc. Code of Ethics \(as updated\) \(Incorporated by reference to Exhibit 14 of the Company's Form 10-K on February 17, 2012\).](#)
- 16 [Letter regarding change in certifying accountant dated June 17, 2011 \(Incorporated by reference to Exhibit 16.1 of the Company's Form 8-K on June 17, 2011\).](#)
- 21.1 [Principal Subsidiaries of the Registrant \(filed herewith\).](#)
- 23.1 [Consent of Independent Registered Public Accounting Firm, KPMG LLP \(filed herewith\).](#)
- 23.2 [Consent of Independent Registered Public Accounting Firm, KPMG Audit Plc \(filed herewith\).](#)

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31.1	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
31.2	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
32.1	Certification of the Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith).
32.2	Certification of the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith).
101	XBRL Instance Document and Related Items.

* Denotes a management contract or compensatory plan.

Item 16 Form 10-K Summary

Not Applicable.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

INNOSPEC INC.
(Registrant)
Date:
February 20, 2019

By: /s/ PATRICK S. WILLIAMS
Patrick S. Williams
President and Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated as of February 20, 2019:

<u>/s/ MILTON C. BLACKMORE</u> Milton C. Blackmore	Chairman and Director
<u>/s/ PATRICK S. WILLIAMS</u> Patrick S. Williams	President and Chief Executive Officer (Principal Executive Officer); Director
<u>/s/ IAN P. CLEMINSON</u> Ian P. Cleminson	Executive Vice President and Chief Financial Officer
<u>/s/ CHRISTOPHER J. PARSONS</u> Christopher J. Parsons	Head of Group Finance (Principal Accounting Officer)
<u>/s/ HUGH G. C. ALDOUS</u> Hugh G. C. Aldous	Director
<u>/s/ DAVID F. LANDLESS</u> David F. Landless	Director
<u>/s/ LAWRENCE J. PADFIELD</u> Lawrence J. Padfield	Director
<u>/s/ ROBERT I. PALLER</u> Robert I. Paller	Director
<u>/s/ JOACHIM ROESER</u> Joachim Roeser	Director

EXHIBIT 12.1 - STATEMENT REGARDING COMPUTATION OF FINANCIAL RATIOS

(in millions except financial ratios, share and per share data)

		2018	2017	2016	2015	2014
1. NET INCOME ATTRIBUTABLE TO INNOSPEC INC. AS A PERCENTAGE OF SALES						
A	Net income attributable to Innospec Inc.	\$ 85.0	\$ 61.8	\$ 81.3	\$ 119.5	\$ 84.1
B	Net sales	\$1476.9	\$1306.8	\$ 883.4	\$1012.3	\$ 960.9
	A % of B	5.8%	4.7%	9.2%	11.8%	8.8%
2. EFFECTIVE TAX RATE AS A PERCENTAGE						
C	Income taxes	\$ 46.6	\$ 66.3	\$ 21.8	\$ 32.8	\$ 26.8
D	Income before income taxes	\$ 131.6	\$ 128.1	\$ 103.1	\$ 152.3	\$ 110.9
	C % of D	35.4%	51.8%	21.1%	21.5%	24.2%
3. CURRENT RATIO						
E	Current assets	\$ 663.9	\$ 561.5	\$ 441.1	\$ 458.7	\$ 414.2
F	Current liabilities	\$ 296.6	\$ 261.5	\$ 183.1	\$ 206.1	\$ 222.9
	Ratio of E to F	2.2	2.1	2.4	2.2	1.9
4. EARNINGS PER SHARE ATTRIBUTABLE TO INNOSPEC INC.						
G	Net income attributable to Innospec Inc.	\$ 85.0	\$ 61.8	\$ 81.3	\$ 119.5	\$ 84.1
H	Basic shares outstanding	24,401	24,148	23,998	24,107	24,391
I	Diluted shares outstanding	24,603	24,486	24,442	24,612	24,878
G/H	Basic earnings per share attributable to Innospec Inc.	<u>\$ 3.48</u>	<u>\$ 2.56</u>	<u>\$ 3.39</u>	<u>\$ 4.96</u>	<u>\$ 3.45</u>
G/I	Diluted earnings per share attributable to Innospec Inc.	<u>\$ 3.45</u>	<u>\$ 2.52</u>	<u>\$ 3.33</u>	<u>\$ 4.86</u>	<u>\$ 3.38</u>

Shares in thousands, earnings per share attributable to Innospec Inc. in dollars.

EXHIBIT 21.1 PRINCIPAL SUBSIDIARIES OF THE REGISTRANT

Alcor Chemie Vertriebs GmbH (Switzerland)
Innospec Active Chemicals LLC (USA)
Innospec Deutschland GmbH (Germany)
Innospec Finance Limited (U.K.)
Innospec France SA (France)
Innospec Fuel Specialties LLC (USA)
Innospec Holdings Limited (U.K.)
Innospec International Limited (U.K.)
Innospec Leuna GmbH (Germany)
Innospec Limited (U.K.)
Innospec Oil Field Chemicals LLC (USA)
Innospec International Holdings LLC (USA)
Independence Oilfield Chemicals LLC (USA)
Innospec Performance Chemicals Europe Limited (U.K.)
Innospec Performance Chemicals Spain S.L. (Spain)
Innospec Performance Chemicals Italia s.r.l (Italy)
Innospec Saint-Mihiel SAS (France)
Innospec Canada Limited (Canada)
Bachman Services, Inc. (USA)
BioSuite LLC (USA)
Strata Control Services, Inc. (USA)
Chemsil Silicones, Inc. (USA)
Chemtec Chemical Co. (USA)
Innospec Russ OOO (Russia)
Innospec Chemicals Beijing Limited (China)
Innospec Do Brasil Limited (Brazil)

Consent of Independent Registered Public Accounting Firm

The Board of Directors
Innospec, Inc.:

We consent to the incorporation by reference in the registration statements (No. 333-225518, 333-131687, 333-124139, 333-174050 and 333-174439) on Form S-8 of Innospec, Inc. of our report dated February 20, 2019, with respect to the consolidated balance sheet of Innospec, Inc. as of December 31, 2018, the related consolidated statements of income, comprehensive income, accumulated other comprehensive loss, cash flows and equity for the year then ended, and the related notes (collectively, the consolidated financial statements), and the effectiveness of internal control over financial reporting as of December 31, 2018, which report appears in the December 31, 2018 annual report on Form 10-K of Innospec, Inc.

KPMG LLP

Manchester, United Kingdom
February 20, 2019

Consent of Independent Registered Public Accounting Firm

The Board of Directors
Innospec, Inc.:

We consent to the incorporation by reference in the registration statements (No. 333-225518, 333-131687, 333-124139, 333-174050 and 333-174439) on Form S-8 of Innospec, Inc. of our report dated February 15, 2018, with respect to the consolidated balance sheet of Innospec, Inc. as of December 31, 2017, the related consolidated statements of income, comprehensive income, accumulated other comprehensive loss, cash flows and equity for each of the years in the two-year period ended December 31, 2017, and the related notes (collectively, the consolidated financial statements), which report appears in the December 31, 2018 annual report on Form 10-K of Innospec, Inc.

KPMG Audit Plc

Manchester, United Kingdom
February 20, 2019

**CERTIFICATION OF PATRICK S. WILLIAMS PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Patrick S. Williams, certify that:

1. I have reviewed this annual report on Form 10-K of Innospec Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ PATRICK S. WILLIAMS

Patrick S. Williams
President and Chief Executive Officer
February 20, 2019

**CERTIFICATION OF IAN P. CLEMINSON PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Ian P. Cleminson, certify that:

1. I have reviewed this annual report on Form 10-K of Innospec Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ IAN P. CLEMINSON

Ian P. Cleminson

Executive Vice President and Chief Financial Officer

February 20, 2019

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report on Form 10-K of Innospec Inc. (the "Company") for the period ended December 31, 2018 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Patrick S. Williams, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- 1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- 2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ PATRICK S. WILLIAMS

Patrick S. Williams
President and Chief Executive Officer
February 20, 2019

The foregoing certification is being furnished solely pursuant to 18 U.S.C. §1350 and is not being filed as part of this Report or as a separate disclosure document.

A signed original of this written statement required by 18 U.S.C. §1350 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission upon request.

**CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report on Form 10-K of Innospec Inc. (the "Company") for the period ended December 31, 2018 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Ian P. Cleminson, Executive Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- 1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- 2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ IAN P. CLEMINSON

Ian P. Cleminson
Executive Vice President and Chief Financial Officer
February 20, 2019

The foregoing certification is being furnished solely pursuant to 18 U.S.C. §1350 and is not being filed as part of this Report or as a separate disclosure document.

A signed original of this written statement required by 18 U.S.C. §1350 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission upon request.