3M CO
Form 10-Q
May 03, 2016
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE

SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2016

Commission file number: 1-3285

3M COMPANY

(Exact name of registrant as specified in its charter)

DELAWARE (State or other jurisdiction of incorporation or organization)	41-0417775 (I.R.S. Employer Identification No.)
3M Center, St. Paul, Minnesota (Address of principal executive offices)	55144 (Zip Code)

(651) 733-1110

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark 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	Accelerated filer
Non-accelerated filer	Smaller reporting company
(Do not check if a smaller reporting company)	

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at March 31, 2016
Common Stock, $0.01 par value per share	606,514,530 shares

This document (excluding exhibits) contains 74 pages.

The table of contents is set forth on page 2.

The exhibit index begins on page 71.

Table of Contents

3M COMPANY

Form 10-Q for the Quarterly Period Ended March 31, 2016

Table of Contents

3M COMPANY

FORM 10-Q

For the Quarterly Period Ended March 31, 2016

PART I. Financial Information

Item 1. Financial Statements.

3M Company and Subsidiaries

Consolidated Statement of Income

(Unaudited)

	Three months ended March 31,	
(Millions, except per share amounts)	2016	2015
Net sales	$ 7,409	$ 7,578
Operating expenses		
Cost of sales	3,678	3,821
Selling, general and administrative expenses	1,493	1,564
Research, development and related expenses	450	463
Total operating expenses	5,621	5,848
Operating income	1,788	1,730
Interest expense and income		
Interest expense	47	31
Interest income	(5)	(4)
Total interest expense — net	42	27
Income before income taxes	1,746	1,703
Provision for income taxes	468	502
Net income including noncontrolling interest	$ 1,278	$ 1,201
Less: Net income attributable to noncontrolling interest	3	2
Net income attributable to 3M	$ 1,275	$ 1,199
Weighted average 3M common shares outstanding — basic	607.4	636.2
Earnings per share attributable to 3M common shareholders — basic	$ 2.10	$ 1.88

Weighted average 3M common shares outstanding — diluted	621.3	649.2
Earnings per share attributable to 3M common shareholders — diluted	$ 2.05	$ 1.85
Cash dividends paid per 3M common share	$ 1.11	$ 1.025

The accompanying Notes to Consolidated Financial Statements are an integral part of this statement.

Table of Contents

3M Company and Subsidiaries

Consolidated Statement of Comprehensive Income

(Unaudited)

	Three months ended March 31,	
(Millions)	2016	2015
Net income including noncontrolling interest	$ 1,278	$ 1,201
Other comprehensive income (loss), net of tax:		
Cumulative translation adjustment	138	(193)
Defined benefit pension and postretirement plans adjustment	69	91
Debt and equity securities, unrealized gain (loss)	—	—
Cash flow hedging instruments, unrealized gain (loss)	(110)	70
Total other comprehensive income (loss), net of tax	97	(32)
Comprehensive income (loss) including noncontrolling interest	1,375	1,169
Comprehensive (income) loss attributable to noncontrolling interest	(2)	(2)
Comprehensive income (loss) attributable to 3M	$ 1,373	$ 1,167

The accompanying Notes to Consolidated Financial Statements are an integral part of this statement.

Table of Contents

3M Company and Subsidiaries

Consolidated Balance Sheet

(Unaudited)

(Dollars in millions, except per share amount)	March 31, 2016	December 31, 2015
Assets		
Current assets		
Cash and cash equivalents	$ 1,337	$ 1,798
Marketable securities — current	176	118
Accounts receivable — net	4,485	4,154
Inventories		
Finished goods	1,699	1,655
Work in process	1,157	1,008
Raw materials and supplies	771	855
Total inventories	3,627	3,518
Other current assets	1,249	1,398
Total current assets	10,874	10,986
Marketable securities — non-current	15	9
Investments	115	117
Property, plant and equipment	23,564	23,098
Less: Accumulated depreciation	(14,950)	(14,583)
Property, plant and equipment — net	8,614	8,515
Goodwill	9,375	9,249
Intangible assets — net	2,551	2,601
Prepaid pension benefits	226	188
Other assets	1,212	1,053
Total assets	$ 32,982	$ 32,718
Liabilities		
Current liabilities		
Short-term borrowings and current portion of long-term debt	$ 2,212	$ 2,044
Accounts payable	1,581	1,694
Accrued payroll	468	644
Accrued income taxes	590	332
Other current liabilities	2,327	2,404
Total current liabilities	7,178	7,118
Long-term debt	8,927	8,753
Pension and postretirement benefits	3,454	3,520
Other liabilities	1,649	1,580
Total liabilities	$ 21,208	$ 20,971
Commitments and contingencies (Note 12)		
Equity		
3M Company shareholders' equity:		

Common stock par value, $.01 par value, 944,033,056 shares issued	$ 9	$ 9
Additional paid-in capital	4,916	4,791
Retained earnings	36,785	36,575
Treasury stock, at cost: 337,518,526 shares at March 31, 2016; 334,702,932 shares at December 31, 2015	(23,716)	(23,308)
Accumulated other comprehensive income (loss)	(6,261)	(6,359)
Total 3M Company shareholders' equity	11,733	11,708
Noncontrolling interest	41	39
Total equity	$ 11,774	$ 11,747
Total liabilities and equity	$ 32,982	$ 32,718

The accompanying Notes to Consolidated Financial Statements are an integral part of this statement.

Table of Contents

3M Company and Subsidiaries

Consolidated Statement of Cash Flows

(Unaudited)

(Millions)	Three months ended March 31, 2016	2015
Cash Flows from Operating Activities		
Net income including noncontrolling interest	$ 1,278	$ 1,201
Adjustments to reconcile net income including noncontrolling interest to net cash provided by operating activities		
Depreciation and amortization	356	339
Company pension and postretirement contributions	(56)	(91)
Company pension and postretirement expense	59	134
Stock-based compensation expense	144	138
Deferred income taxes	(38)	44
Excess tax benefits from stock-based compensation	—	(101)
Changes in assets and liabilities		
Accounts receivable	(245)	(296)
Inventories	(37)	(131)
Accounts payable	(116)	56
Accrued income taxes (current and long-term)	334	100
Other — net	(419)	(313)
Net cash provided by operating activities	1,260	1,080
Cash Flows from Investing Activities		
Purchases of property, plant and equipment (PP&E)	(314)	(291)
Proceeds from sale of PP&E and other assets	18	4
Acquisitions, net of cash acquired	(4)	(150)
Purchases of marketable securities and investments	(225)	(191)
Proceeds from maturities and sale of marketable securities and investments	164	605
Proceeds from sale of businesses	56	19
Other investing	25	4
Net cash used in investing activities	(280)	—
Cash Flows from Financing Activities		
Change in short-term debt — net	138	(4)
Repayment of debt (maturities greater than 90 days)	—	—
Proceeds from debt (maturities greater than 90 days)	—	—
Purchases of treasury stock	(1,227)	(886)
Proceeds from issuance of treasury stock pursuant to stock option and benefit plans	357	309
Dividends paid to shareholders	(672)	(652)
Excess tax benefits from stock-based compensation	—	101
Other — net	(22)	(22)

Net cash used in financing activities	(1,426)	(1,154)
Effect of exchange rate changes on cash and cash equivalents	(15)	(32)
Net increase (decrease) in cash and cash equivalents	(461)	(106)
Cash and cash equivalents at beginning of year	1,798	1,897
Cash and cash equivalents at end of period	$ 1,337	$ 1,791

The accompanying Notes to Consolidated Financial Statements are an integral part of this statement.

Table of Contents

3M Company and Subsidiaries

Notes to Consolidated Financial Statements

(Unaudited)

NOTE 1. Significant Accounting Policies

Basis of Presentation

The interim consolidated financial statements are unaudited but, in the opinion of management, reflect all adjustments necessary for a fair statement of the Company's consolidated financial position, results of operations and cash flows for the periods presented. These adjustments consist of normal, recurring items. The results of operations for any interim period are not necessarily indicative of results for the full year. The interim consolidated financial statements and notes are presented as permitted by the requirements for Quarterly Reports on Form 10-Q.

This Quarterly Report on Form 10-Q should be read in conjunction with the Company's consolidated financial statements and notes included in its 2015 Annual Report on Form 10-K. As described in Note 14, effective in the first quarter of 2016, the Company made a product line reporting change involving two of its business segments. The Company has begun to report comparative results under this new structure with the filing of this Quarterly Report on Form 10-Q. In the second quarter of 2016, the Company plans to update its business segment disclosures in its 2015 Annual Report on Form 10-K via a Current Report on Form 8-K to reflect these changes.

Foreign Currency Translation

Local currencies generally are considered the functional currencies outside the United States. Assets and liabilities for operations in local-currency environments are translated at month-end exchange rates of the period reported. Income and expense items are translated at month-end exchange rates of each applicable month. Cumulative translation adjustments are recorded as a component of accumulated other comprehensive income (loss) in shareholders' equity.

Although local currencies are typically considered as the functional currencies outside the United States, under Accounting Standards Codification (ASC) 830, Foreign Currency Matters, the reporting currency of a foreign entity's parent is assumed to be that entity's functional currency when the economic environment of a foreign entity is highly inflationary—generally when its cumulative inflation is approximately 100 percent or more for the three years that precede the beginning of a reporting period. 3M has a subsidiary in Venezuela with operating income representing less than 1.0 percent of 3M's consolidated operating income for 2015. Since January 1, 2010, the financial statements of the Venezuelan subsidiary have been remeasured as if its functional currency were that of its parent.

The Venezuelan government sets official rates of exchange and conditions precedent to purchase foreign currency at these rates with local currency. Such rates and conditions have been and continue to be subject to change. In January 2014, the Venezuelan government announced that the National Center for Foreign Commerce (CENCOEX), had assumed the role with respect to the continuation of the existing official exchange rate, significantly expanded the use of a second currency auction exchange mechanism called the Complementary System for Foreign Currency Acquirement (or SICAD1), and issued exchange regulations indicating the SICAD1 rate of exchange would be used for payments related to international investments. In late March 2014, the Venezuelan government launched a third foreign exchange mechanism, SICAD2, which it later replaced with another foreign currency exchange platform in February 2015 called the Marginal System of Foreign Currency (SIMADI). The SIMADI rate was described as being derived from daily private bidders and buyers exchanging offers through authorized agents. This rate is approved and published by the Venezuelan Central Bank. In March 2016, the Venezuelan government effected a replacement of its preferential CENCOEX rate with Tipo de Cambio Protegido (DIPRO), described as available largely for essential imports; eliminated its SICAD exchange mechanism; and replaced its SIMADI rate with Tipo de Cambio Complementario (DICOM), published by the Venezuelan Central Bank and described as fluctuating in rate based on supply and demand.

The financial statements of 3M's Venezuelan subsidiary were remeasured utilizing the official CENCOEX (or its predecessor) rate into March 2014, the SICAD1 rate beginning in late March 2014, the SICAD2 rate beginning in June 2014, and the DICOM rate (or its SIMADI predecessor) beginning in February 2015. 3M's uses of these rates were

Table of Contents

based upon evaluation of a number of factors including, but not limited to, the exchange rate the Company's Venezuelan subsidiary may legally use to convert currency, settle transactions or pay dividends; the probability of accessing and obtaining currency by use of a particular rate or mechanism; and the Company's intent and ability to use a particular exchange mechanism. Other factors notwithstanding, remeasurement impacts of the changes in use of these exchange rates did not have material impacts on 3M's consolidated results of operations or financial condition.

The Company continues to monitor circumstances relative to its Venezuelan subsidiary. Changes in applicable exchange rates or exchange mechanisms may continue in the future. These changes could impact the rate of exchange applicable to remeasure the Company's net monetary assets (liabilities) denominated in Venezuelan Bolivars (VEF). As of March 31, 2016, the Company had a balance of net monetary assets denominated in VEF of less than 500 million VEF and the DIPRO and DICOM exchange rates were approximately 10 VEF and 260 VEF per U.S. dollar, respectively.

A need to deconsolidate the Company's Venezuelan subsidiary's operations may result from a lack of exchangeability of VEF-denominated cash coupled with an acute degradation in the ability to make key operational decisions due to government regulations in Venezuela. 3M monitors factors such as its ability to access various exchange mechanisms; the impact of government regulations on the Company's ability to manage its Venezuelan subsidiary's capital structure, purchasing, product pricing, and labor relations; and the current political and economic situation within Venezuela. Based upon such factors as of March 31, 2016, the Company continues to consolidate its Venezuelan subsidiary. As of March 31, 2016, the balance of intercompany receivables due from this subsidiary and its equity balance were not significant.

Earnings Per Share

The difference in the weighted average 3M shares outstanding for calculating basic and diluted earnings per share attributable to 3M common shareholders is a result of the dilution associated with the Company's stock-based compensation plans. Certain options outstanding under these stock-based compensation plans were not included in the computation of diluted earnings per share attributable to 3M common shareholders because they would not have had a dilutive effect (9.0 million average options for the three months ended March 31, 2016 and 3.5 million average options for the three months ended March 31, 2015). The computations for basic and diluted earnings per share follow:

Earnings Per Share Computations

	Three months ended March 31,

(Amounts in millions, except per share amounts)	2016	2015
Numerator:		
Net income attributable to 3M	$ 1,275	$ 1,199
Denominator:		
Denominator for weighted average 3M common shares outstanding — basic	607.4	636.2
Dilution associated with the Company's stock-based compensation plans	13.9	13.0
Denominator for weighted average 3M common shares outstanding — diluted	621.3	649.2
Earnings per share attributable to 3M common shareholders — basic	$ 2.10	$ 1.88
Earnings per share attributable to 3M common shareholders — diluted	$ 2.05	$ 1.85

New Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued ASU No. 2014-09, Revenue from Contracts with Customers, and in August 2015 issued ASU No. 2015-14, which amended ASU No. 2014-09 as to effective date. The ASU, as amended, provides a single comprehensive model to be used in the accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The standard's stated core principle is that an entity should recognize revenue to depict the transfer of

Table of Contents

promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve this core principle the ASU includes provisions within a five step model that includes identifying the contract with a customer, identifying the performance obligations in the contract, determining the transaction price, allocating the transaction price to the performance obligations, and recognizing revenue when (or as) an entity satisfies a performance obligation. The standard also specifies the accounting for some costs to obtain or fulfill a contract with a customer and requires expanded disclosures about revenue recognition. The standard provides for either full retrospective adoption or a modified retrospective adoption by which it is applied only to the most current period presented. For 3M, the ASU, as amended, is effective January 1, 2018. The Company is currently assessing this standard's impact on 3M's consolidated results of operations and financial condition.

In February 2015, the FASB issued ASU No. 2015-02, Amendments to the Consolidation Analysis, which changes guidance related to both the variable interest entity (VIE) and voting interest entity (VOE) consolidation models. With respect to the VIE model, the standard changes, among other things, the identification of variable interests associated with fees paid to a decision maker or service provider, the VIE characteristics for a limited partner or similar entity, and the primary beneficiary determination. With respect to the VOE model, the ASU eliminates the presumption that a general partner controls a limited partnership or similar entity unless the presumption can otherwise be overcome. Under the new guidance, a general partner would largely not consolidate a partnership or similar entity under the VOE model. The Company adopted this ASU effective January 1, 2016. Because 3M did not have significant involvement with entities subject to consolidation considerations impacted by the VIE model changes or with limited partnerships potentially impacted by the VOE model changes, the adoption did not have a material impact on the Company's consolidated results of operations and financial condition.

In April 2015, the FASB issued ASU No. 2015-05, Customer's Accounting for Fees Paid in a Cloud Arrangement, which requires a customer to determine whether a cloud computing arrangement contains a software license. If the arrangement contains a software license, the customer would account for fees related to the software license element in a manner consistent with accounting for the acquisition of other acquired software licenses. If the arrangement does not contain a software license, the customer would account for the arrangement as a service contract. An arrangement would contain a software license element if both (1) the customer has the contractual right to take possession of the software at any time during the hosting period without significant penalty and (2) it is feasible for the customer to either run the software on its own hardware or contract with another party unrelated to the vendor to host the software. 3M adopted this ASU prospectively to arrangements entered into, or materially modified beginning January 1, 2016. The adoption did not have a material impact on 3M's consolidated results of operations and financial condition.

In July 2015, the FASB issued ASU No. 2015-11, Simplifying the Measurement of Inventory, which modifies existing requirements regarding measuring inventory at the lower of cost or market. Under existing standards, the market amount requires consideration of replacement cost, net realizable value (NRV), and NRV less an approximately normal profit margin. The new ASU replaces market with NRV, defined as estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. This eliminates the need to determine and consider replacement cost or NRV less an approximately normal profit margin when measuring inventory. For 3M, this standard is effective prospectively beginning January 1, 2017, with early adoption permitted. The Company is currently assessing this ASU's impact on 3M's consolidated results of operations and financial condition.

In January 2016, the FASB issued ASU No. 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities, which revises the accounting related to (1) the classification and measurement of investments in equity securities and (2) the presentation of certain fair value changes for financial liabilities measured at fair value. The ASU also amends certain disclosure requirements associated with the fair value of financial instruments. The new guidance requires the fair value measurement of investments in equity securities and other ownership interests in an entity, including investments in partnerships, unincorporated joint ventures and limited liability companies (collectively, equity securities) that do not result in consolidation and are not accounted for under the equity method. Entities will need to measure these investments and recognize changes in fair value in net income. Entities will no longer be able to recognize unrealized holding gains and losses on equity securities they classify under current guidance as available for sale in other comprehensive income (OCI). They also will no longer be able to use the cost method of accounting for equity securities that do not have readily determinable fair values. Instead, for these types of equity investments that do not otherwise qualify for the net asset value practical expedient, entities will be permitted to elect a practicability exception and measure the investment at cost less impairment plus or minus observable price changes (in orderly transactions). The ASU also establishes an incremental recognition and disclosure requirement related to the presentation of fair value changes of financial liabilities for which the fair value option (FVO) has been elected. Under this guidance, an entity would be required to separately present in OCI the portion of the total fair value change attributable to instrument-specific credit risk as opposed to reflecting the entire amount in earnings. For derivative liabilities for which the FVO has been elected, however, any changes in fair value attributable to instrument-specific credit risk would continue to be presented in net income, which is consistent with current guidance. For 3M, this standard is effective beginning January 1, 2018 via a cumulative-effect adjustment to beginning retained earnings, except for guidance relative to equity securities without readily determinable fair values which is applied prospectively. The Company is currently assessing this ASU’s impact on 3M’s consolidated results of operations and financial condition.

In February 2016, the FASB issued ASU No. 2016-02, Leases, replacing existing lease accounting guidance. The new standard introduces a lessee model that would require entities to recognize assets and liabilities for most leases, but recognize expenses on their income statements in a manner similar to current accounting. The ASU does not make fundamental changes to existing lessor accounting. However, it modifies what qualifies as a sales-type and direct financing lease and related accounting and aligns a number of the underlying principles with those of the new revenue standard, ASU No. 2014-09, such as evaluating how collectability should be considered and determining when profit can be recognized. The guidance eliminates existing real estate-specific provisions and requires expanded qualitative and quantitative disclosures. The standard requires modified retrospective transition by which it is applied at the beginning of the earliest comparative period presented in the year of adoption. For 3M, the ASU is effective January 1, 2019. The Company is currently assessing this standard’s impact on 3M’s consolidated results of operations and financial condition.

In March 2016, the FASB issued ASU No. 2016-06, Contingent Put and Call Options in Debt Instruments. This ASU clarifies guidance used to determine if debt instruments that contain contingent put or call options would require separation of the embedded put or call feature from the debt instrument and trigger accounting for the feature as a derivative with changes in fair value recorded through income. Under the new guidance, fewer put or call options embedded in debt instruments would require derivative accounting. For 3M, this ASU is effective January 1, 2017. The Company’s outstanding debt with embedded put provisions does not require separate derivative accounting under existing guidance. As a result, 3M does not expect this ASU to have a material impact on the Company’s consolidated results of operations and financial condition.

In March 2016, the FASB issued ASU No. 2016-07, Simplifying the Transition to the Equity Method of Accounting, which eliminates the existing requirement to apply the equity method of accounting retrospectively (revising prior periods as if the equity method had always been applied) when an entity obtains significant influence over a previously held investment. The new guidance would require the investor to apply the equity method prospectively from the date the investment qualifies for the equity method. The investor would add the carrying value of the existing investment to the cost of any additional investment to determine the initial cost basis of the equity method investment. For 3M, this ASU is effective January 1, 2017 on a prospective basis, with early adoption permitted. 3M would apply this guidance to investments that transition to the equity method after the adoption date.

In March 2016, the FASB issued ASU No. 2016-08, Principal versus Agent Considerations (Reporting Revenue Gross versus Net), which amends ASU No. 2014-09, Revenue from Contracts with Customers, to clarify principal versus agent guidance in situations in which a revenue transaction involves a third party in providing goods or services to a customer. In such circumstances, an entity must determine whether the nature of its promise to the customer is to provide the underlying goods or services (i.e., the entity is the principal in the transaction) or to arrange for the third party to provide the underlying goods or services (i.e., the entity is the agent in the transaction). To determine the nature of its promise to the customer, the entity must first identify each specified good or service to be provided to the customer and then (before transferring it) assess whether it controls each specified good or service. The new ASU clarifies how an entity should identify the unit of accounting (the specified good or service) for the principal versus agent evaluation, and how it should apply the control principle to certain types of arrangements, such as service transactions, by explaining what a principal controls before the specified good or service is transferred to the customer. This ASU has the same effective date and transition requirements as ASU No. 2014-09, as amended by ASU No. 2015-14, which for 3M is effective January 1,

Table of Contents

2018. The Company is currently assessing this standard's impact on 3M's consolidated results of operations and financial condition.

In March 2016, the FASB issued ASU No. 2016-09, Improvements to Employee Share-Based Payment Accounting, which modifies certain accounting aspects for share-based payments to employees including, among other elements, the accounting for income taxes and forfeitures, as well as classifications in the statement of cash flows. With respect to income taxes, under current guidance, when a share-based payment award such as a stock option or restricted stock unit (RSU) is granted to an employee, the fair value of the award is generally recognized over the vesting period. However, the related deduction from taxes payable is based on the award's intrinsic value at the time of exercise (for an option) or on the fair value upon vesting of the award (for RSUs), which can be either greater (creating an excess tax benefit) or less (creating a tax deficiency) than the compensation cost recognized in the financial statements. Excess tax benefits are recognized in additional paid-in capital (APIC) within equity, and tax deficiencies are similarly recognized in APIC to the extent there is a sufficient APIC amount (APIC pool) related to previously recognized excess tax benefits. Under the new guidance, all excess tax benefits/deficiencies would be recognized as income tax benefit/expense in the statement of income. The new ASU's income tax aspects also impact the calculation of diluted earnings per share by excluding excess tax benefits/deficiencies from the calculation of assumed proceeds available to repurchase shares under the treasury stock method. Relative to forfeitures, the new standard allows an entity-wide accounting policy election either to continue to estimate the number of awards that will be forfeited or to account for forfeitures as they occur. The new guidance also impacts classifications within the statement of cash flows by no longer requiring inclusion of excess tax benefits as both a hypothetical cash outflow within cash flows from operating activities and hypothetical cash inflow within cash flows from financing activities. Instead, excess tax benefits would be classified in operating activities in the same manner as other cash flows related to income taxes. Additionally, the new ASU requires cash payments to tax authorities when an employer uses a net-settlement feature to withhold shares to meet statutory tax withholding provisions to be presented as financing activity (eliminating previous diversity in practice). For 3M, this standard is required effective January 1, 2017, with early adoption permitted. The Company early adopted ASU No. 2016-09 as of January 1, 2016. Prospectively beginning January 1, 2016, excess tax benefits/deficiencies have been reflected as income tax benefit/expense in the statement of income resulting in a $81 million tax benefit in the quarter ended March 31, 2016 (3M typically experiences the largest volume of stock option exercises and RSU vestings in the first quarter of its fiscal year). The extent of excess tax benefits/deficiencies is subject to variation in 3M stock price and timing/extent of RSU vestings and employee stock option exercises. 3M's adoption of this ASU also resulted in associated excess tax benefits being classified as operating activity in the same manner as other cash flows related to income taxes in the statement of cash flows prospectively beginning January 1, 2016. Based on the adoption methodology applied, the statement of cash flows classification of prior periods has not been adjusted. In addition, 3M did not change its accounting principles relative to elements of this standard and continued its existing practice of estimating the number of awards that will be forfeited.

In April 2016, the FASB issued ASU No. 2016-10, Identifying Performance Obligations and Licensing, which amends ASU No. 2014-09, Revenue from Contracts with Customers. In terms of identifying performance obligations in a revenue arrangement, the amendments clarify how entities would determine whether promised goods or services are separately identifiable from other promises in a contract and, therefore, would be accounted for separately. The guidance would also allow entities to disregard goods or services that are immaterial in the context of a contract and provides an accounting policy election to account for shipping and handling activities as fulfillment costs rather than as additional promised services. With regard to the licensing, the amendments clarify how an entity would evaluate the nature of its promise in granting a license of intellectual property, which determines whether the entity recognizes revenue over time or at a point in time. The standard also clarifies certain other aspects relative to licensing. This ASU has the same effective date and transition requirements as ASU No. 2014-09, as amended by ASU No. 2015-14, which for 3M is effective January 1, 2018. The Company is currently assessing this standard’s impact on 3M’s consolidated results of operations and financial condition.

Table of Contents

NOTE 2. Acquisitions and Divestitures

Acquisitions:

3M makes acquisitions of certain businesses from time to time that are aligned with its strategic intent with respect to, among other factors, growth markets and adjacent product lines or technologies.

There were no material business combinations that closed during the three months ended March 31, 2016. Adjustments in the first quarter of 2016 to the preliminary purchase price allocations of other acquisitions within the allocation period were not material. The allocation of purchase price related to the acquisition of Capital Safety Group S.A.R.L. in August 2015 is considered preliminary, primarily with respect to certain tax-related assets and liabilities. 3M expects to finalize the allocation of purchase price within the one year measurement-period following this acquisition.

Divestitures:

3M may divest certain businesses from time to time based upon review of the Company's portfolio considering, among other items, factors relative to the extent of strategic and technological alignment and optimization of capital deployment, in addition to considering if selling the businesses results in the greatest value creation for the Company and for shareholders.

In the first quarter of 2016, 3M (Safety and Graphics Business) completed the sale of the remainder of the assets of 3M's library systems business to One Equity Partners Capital Advisors L.P. (OEP). 3M had previously sold the North American business and the majority of the business outside of North America to OEP in the fourth quarter of 2015. The library systems business delivers circulation management solutions to library customers with on-premise hardware and software, maintenance and service, and an emerging cloud-based digital lending platform.

In the first quarter of 2016, 3M (Industrial Business) sold to Innovative Chemical Products Group, a portfolio company of Audax Private Equity, the assets of 3M's pressurized polyurethane foam adhesives business (formerly known as Polyfoam). This business is a provider of pressurized polyurethane foam adhesive formulations and systems into the residential roofing, commercial roofing and insulation and industrial foam segments in the United States with annual sales of approximately $20 million.

The Company recorded a pre-tax gain of $40 million in the first quarter of 2016 as a result of the sales of these businesses (recorded in selling, general and administrative expenses). The aggregate operating income of these businesses included in the Company’s operating results for the periods presented and the amounts of major assets and liabilities of any associated disposal groups classified as held-for-sale as of the respective balance sheet dates presented were not material.

Refer to Note 2 in 3M’s 2015 Annual Report on Form 10-K for more information on 3M’s acquisitions and divestitures.

Table of Contents

NOTE 3. Goodwill and Intangible Assets

There were no material acquisitions that closed during the first three months of 2016. The amounts in the "Translation and other" column in the following table primarily relate to changes in foreign currency exchange rates. The goodwill balances by business segment as of December 31, 2015 and March 31, 2016, follow:

Goodwill

(Millions)	December 31, 2015 Balance	Acquisition activity	Translation and other	March 31, 2016 Balance
Industrial	$ 2,573	$ —	$ 51	$ 2,624
Safety and Graphics	3,342	3	32	3,377
Health Care	1,624	—	20	1,644
Electronics and Energy	1,510	—	14	1,524
Consumer	200	—	6	206
Total Company	$ 9,249	$ 3	$ 123	$ 9,375

Accounting standards require that goodwill be tested for impairment annually and between annual tests in certain circumstances such as a change in reporting units or the testing of recoverability of a significant asset group within a reporting unit. At 3M, reporting units generally correspond to a division.

As described in Note 14, effective in the first quarter of 2016, the Company changed its business segment reporting in its continuing effort to improve the alignment of its businesses around markets and customers. For any product changes that resulted in reporting unit changes, the Company applied the relative fair value method to determine the impact on goodwill of the associated reporting units. During the first quarter of 2016, the Company completed its assessment of any potential goodwill impairment for reporting units impacted by this new structure and determined that no impairment existed.

Acquired Intangible Assets

The carrying amount and accumulated amortization of acquired finite-lived intangible assets, in addition to the balance of non-amortizable intangible assets, as of March 31, 2016, and December 31, 2015, follow:

(Millions)	March 31, 2016	December 31, 2015
Customer related intangible assets	$ 1,985	$ 1,973
Patents	610	616
Other technology-based intangible assets	526	525
Definite-lived tradenames	423	421
Other amortizable intangible assets	218	216
Total gross carrying amount	$ 3,762	$ 3,751
Accumulated amortization — customer related	(706)	(668)
Accumulated amortization — patents	(484)	(481)
Accumulated amortization — other technology based	(267)	(252)
Accumulated amortization — definite-lived tradenames	(222)	(215)
Accumulated amortization — other	(172)	(169)
Total accumulated amortization	$ (1,851)	$ (1,785)
Total finite-lived intangible assets — net	$ 1,911	$ 1,966
Non-amortizable intangible assets (primarily tradenames)	640	635
Total intangible assets — net	$ 2,551	$ 2,601

Table of Contents

Certain tradenames acquired by 3M are not amortized because they have been in existence for over 55 years, have a history of leading-market share positions, have been and are intended to be continuously renewed, and the associated products of which are expected to generate cash flows for 3M for an indefinite period of time.

Amortization expense for acquired intangible assets for the three-month periods ended March 31, 2016 and 2015 follows:

	Three months ended March 31,	
(Millions)	2016	2015
Amortization expense	$ 66	$ 53

Expected amortization expense for acquired amortizable intangible assets recorded as of March 31, 2016:

(Millions)	Remainder of 2016	2017	2018	2019	2020	2021	After 2021
Amortization expense	$ 188	$ 227	$ 205	$ 193	$ 183	$ 167	$ 748

The preceding expected amortization expense is an estimate. Actual amounts of amortization expense may differ from estimated amounts due to additional intangible asset acquisitions, changes in foreign currency exchange rates, impairment of intangible assets, accelerated amortization of intangible assets and other events. 3M expenses the costs incurred to renew or extend the term of intangible assets.

NOTE 4. Restructuring Actions

During the fourth quarter of 2015, management approved and committed to undertake certain restructuring actions primarily focused on structural overhead, largely in the U.S. and slower-growing markets, with particular emphasis on Europe, Middle East, and Africa (EMEA) and Latin America. This impacted approximately 1,700 positions worldwide and resulted in a fourth-quarter 2015 pre-tax charge of $114 million.

Components of these restructuring actions, including cash and non-cash impacts, follow:

(Millions)	Employee-Related	Asset-Related	Total
Expense incurred	$ 98	$ 16	$ 114
Non-cash changes	(8)	(16)	(24)
Cash payments	(27)	—	(27)
Accrued restructuring action balances as of December 31, 2015	$ 63	$ —	$ 63
Cash payments	(25)	—	(25)
Accrued restructuring action balances as of March 31, 2016	$ 38	$ —	$ 38

Non-cash changes include certain pension settlements and special termination benefits recorded in accrued pension and postretirement benefits and accelerated depreciation resulting from the cessation of use of certain long-lived assets. Remaining activities related to the restructuring are expected to be completed in 2016.

Table of Contents

NOTE 5. Supplemental Equity and Comprehensive Income Information

Consolidated Statement of Changes in Equity

Three months ended March 31, 2016

		3M Company Shareholders				
(Millions)	Total	Common Stock and Additional Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Non-controlling Interest
Balance at December 31, 2015	$ 11,747	$ 4,800	$ 36,575	$ (23,308)	$ (6,359)	$ 39
Net income	1,278		1,275			3
Other comprehensive income (loss), net of tax:						
Cumulative translation adjustment	138				139	(1)
Defined benefit pension and post-retirement plans adjustment	69				69	—
Debt and equity securities - unrealized gain (loss)	—				—	—
Cash flow hedging instruments - unrealized gain (loss)	(110)				(110)	—
Total other comprehensive income (loss), net of tax	97					
Dividends declared	(672)		(672)			
Stock-based compensation	125	125				
Reacquired stock	(1,163)			(1,163)		
Issuances pursuant to stock option and benefit plans	362		(393)	755		
Balance at March 31, 2016	$ 11,774	$ 4,925	$ 36,785	$ (23,716)	$ (6,261)	$ 41

Three months ended March 31, 2015

3M Company Shareholders

(Millions)	Total	Common Stock and Additional Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Non-controlling Interest
Balance at December 31, 2014	$ 13,142	$ 4,388	$ 34,317	$ (19,307)	$ (6,289)	$ 33
Net income	1,201		1,199			2
Other comprehensive income (loss), net of tax:						
Cumulative translation adjustment	(193)				(193)	—
Defined benefit pension and post-retirement plans adjustment	91				91	—
Debt and equity securities - unrealized gain (loss)	—				—	—
Cash flow hedging instruments - unrealized gain (loss)	70				70	—
Total other comprehensive income (loss), net of tax	(32)					
Dividends declared	(3)		(3)			
Stock-based compensation, net of tax impacts	228	228				
Reacquired stock	(896)			(896)		
Issuances pursuant to stock option and benefit plans	312		(433)	745		
Balance at March 31, 2015	$ 13,952	$ 4,616	$ 35,080	$ (19,458)	$ (6,321)	$ 35

In December 2014, 3M's Board of Directors declared a first-quarter 2015 dividend of $1.025 per share (paid in March 2015). This reduced 3M's stockholder equity and increased other current liabilities as of December 31, 2014, by approximately $0.6 billion.

Table of Contents

Changes in Accumulated Other Comprehensive Income (Loss) Attributable to 3M by Component

Three months ended March 31, 2016

(Millions)	Cumulative Translation Adjustment	Defined Benefit Pension and Postretirement Plans Adjustment	Debt and Equity Securities, Unrealized Gain (Loss)	Cash Flow Hedging Instruments, Unrealized Gain (Loss)	Total Accumulated Other Comprehensive Income (Loss)
Balance at December 31, 2015, net of tax:	$ (1,679)	$ (4,804)	$ —	$ 124	$ (6,359)
Other comprehensive income (loss), before tax:					
Amounts before reclassifications	60	—	—	(121)	(61)
Amounts reclassified out	—	103	—	(52)	51
Total other comprehensive income (loss), before tax	60	103	—	(173)	(10)
Tax effect	79	(34)	—	63	108
Total other comprehensive income (loss), net of tax	139	69	—	(110)	98
Balance at March 31, 2016, net of tax:	$ (1,540)	$ (4,735)	$ —	$ 14	$ (6,261)

Three months ended March 31, 2015

(Millions)	Cumulative Translation Adjustment	Defined Benefit Pension and Postretirement Plans Adjustment	Debt and Equity Securities, Unrealized Gain (Loss)	Cash Flow Hedging Instruments, Unrealized Gain (Loss)	Total Accumulated Other Comprehensive Income (Loss)
Balance at December 31, 2014, net of tax:	$ (1,095)	$ (5,293)	$ —	$ 99	$ (6,289)
Other comprehensive income (loss), before tax:					
Amounts before reclassifications	(44)	24	—	136	116
Amounts reclassified out	—	124	—	(27)	97
	(44)	148	—	109	213

Total other comprehensive income (loss), before tax										
Tax effect		(149)		(57)		—		(39)		(245)
Total other comprehensive income (loss), net of tax		(193)		91		—		70		(32)
Balance at March 31, 2015, net of tax:	$	(1,288)	$	(5,202)	$	—	$	169	$	(6,321)

Income taxes are not provided for foreign translation relating to permanent investments in international subsidiaries, but tax effects within cumulative translation does include impacts from items such as net investment hedge transactions. Reclassification adjustments are made to avoid double counting in comprehensive income items that are also recorded as part of net income.

Table of Contents

Reclassifications out of Accumulated Other Comprehensive Income Attributable to 3M

Details about Accumulated Other Comprehensive Income Components (Millions)	Amount Reclassified from Accumulated Other Comprehensive Income Three months ended March 31, 2016	2015	Location on Income Statement
Gains (losses) associated with, defined benefit pension and postretirement plans amortization			
Transition asset	$ —	$ —	See Note 9
Prior service benefit	23	18	See Note 9
Net actuarial loss	(126)	(159)	See Note 9
Curtailments/Settlements	—	17	See Note 9
Total before tax	(103)	(124)	
Tax effect	34	46	Provision for income taxes
Net of tax	$ (69)	$ (78)	
Debt and equity security gains (losses)			
Sales or impairments of securities	$ —	$ —	Selling, general and administrative expenses
Total before tax	—	—	
Tax effect	—	—	Provision for income taxes
Net of tax	$ —	$ —	
Cash flow hedging instruments gains (losses)			
Foreign currency forward/option contracts	$ 53	$ 30	Cost of sales
Commodity price swap contracts	—	(2)	Cost of sales
Interest rate swap contracts	(1)	(1)	Interest expense
Total before tax	52	27	
Tax effect	(18)	(10)	Provision for income taxes
Net of tax	$ 34	$ 17	
Total reclassifications for the period, net of tax	$ (35)	$ (61)	

Table of Contents

NOTE 6. Income Taxes

The Company files income tax returns in the U.S. federal jurisdiction, and various states and foreign jurisdictions. With few exceptions, the Company is no longer subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities for years before 2005.

The IRS has completed its field examination of the Company's U.S. federal income tax returns for the years 2005 through 2014. The Company protested certain IRS positions within these tax years and entered into the administrative appeals process with the IRS. In December 2012, the Company received a statutory notice of deficiency for the 2006 year. The Company filed a petition in Tax Court in the first quarter of 2013 relating to the 2006 tax year.

Currently, the Company is under examination by the IRS for its U.S. federal income tax returns for the years 2015 and 2016. It is anticipated that the IRS will complete its examination of the Company for 2015 by the end of the first quarter of 2017 and for 2016 by the end of the first quarter of 2018. As of March 31, 2016, the IRS has not proposed any significant adjustments to the Company's tax positions for which the Company is not adequately reserved.

Payments relating to other proposed assessments arising from the 2005 through 2016 examinations may not be made until a final agreement is reached between the Company and the IRS on such assessments or upon a final resolution resulting from the administrative appeals process or judicial action. In addition to the U.S. federal examination, there is also audit activity in several U.S. state and foreign jurisdictions.

3M anticipates changes to the Company's uncertain tax positions due to the closing and resolution of audit issues for various audit years mentioned above and closure of statutes. The Company is not currently able to reasonably estimate the amount by which the liability for unrecognized tax benefits will increase or decrease during the next 12 months as a result of the ongoing income tax authority examinations. The total amounts of unrecognized tax benefits that, if recognized, would affect the effective tax rate as of March 31, 2016 and December 31, 2015 are $375 million and $369 million, respectively.

The Company recognizes interest and penalties accrued related to unrecognized tax benefits in tax expense. The Company recognized in the consolidated statement of income on a gross basis approximately $4 million of benefit and $2 million of expense for the three months ended March 31, 2016 and March 31, 2015, respectively. At March 31, 2016 and December 31, 2015, accrued interest and penalties in the consolidated balance sheet on a gross basis were $39 million and $45 million, respectively. Included in these interest and penalty amounts are interest and penalties related to tax positions for which the ultimate deductibility is highly certain but for which there is uncertainty about the timing of such deductibility. Because of the impact of deferred tax accounting, other than interest and penalties, the disallowance of the shorter deductibility period would not affect the annual effective tax rate but would accelerate the payment of cash to the taxing authority to an earlier period.

The effective tax rate for the first quarter of 2016 was 26.8 percent, compared to 29.5 percent in the first quarter of 2015, a decrease of 2.7 percentage points. Primary factors that decreased the Company’s effective tax rate on a combined basis by 5.3 percentage points for the first three months of 2016 when compared to the same period for 2015 included the recognition of excess tax benefits beginning in 2016 related to employee share-based payments (resulting from the adoption of ASU No. 2016-09, as discussed in Note 1), the reinstatement of the R&D tax credit, and other items. This decrease was partially offset by a 2.6 percentage point year-on-year increase, which included international taxes that were impacted by changes to both the geographic mix of income before taxes and additional tax expense related to global cash optimization actions, plus remeasurements of 3M’s uncertain tax positions.

The provision for income taxes is determined using the asset and liability approach. Under this approach, deferred income taxes represent the expected future tax consequences of temporary differences between the carrying amounts and tax basis of assets and liabilities. The Company records a valuation allowance to reduce its deferred tax assets when uncertainty regarding their realizability exits. As of March 31, 2016 and December 31, 2015, the Company had valuation allowances of $32 million and $31 million on its deferred tax assets, respectively.

Table of Contents

NOTE 7. Marketable Securities

The Company invests in asset-backed securities, certificates of deposit/time deposits, commercial paper, and other securities. The following is a summary of amounts recorded on the Consolidated Balance Sheet for marketable securities (current and non-current).

(Millions)	March 31, 2016	December 31, 2015
Foreign government agency securities	$ 10	$ 10
Corporate debt securities	10	10
Commercial paper	36	12
Certificates of deposit/time deposits	46	26
U.S. municipal securities	3	3
Asset-backed securities:		
Automobile loan related	44	26
Credit card related	19	10
Equipment lease related	1	2
Other	7	19
Asset-backed securities total	71	57
Current marketable securities	$ 176	$ 118
U.S. municipal securities	$ 15	$ 9
Non-current marketable securities	$ 15	$ 9
Total marketable securities	$ 191	$ 127

Classification of marketable securities as current or non-current is based on the nature of the securities and availability for use in current operations. At March 31, 2016 and December 31, 2015, gross unrealized gains and/or losses (pre-tax) were not material. Refer to Note 5 for a table that provides the net realized gains (losses) related to sales or impairments of debt and equity securities, which includes marketable securities. The gross amounts of the realized gains or losses were not material. Cost of securities sold use the first in, first out (FIFO) method. Since these marketable securities are classified as available-for-sale securities, changes in fair value will flow through other comprehensive income, with amounts reclassified out of other comprehensive income into earnings upon sale or “other-than-temporary” impairment.

3M reviews impairments associated with its marketable securities in accordance with the measurement guidance provided by ASC 320, Investments-Debt and Equity Securities, when determining the classification of the impairment as “temporary” or “other-than-temporary”. A temporary impairment charge results in an unrealized loss being recorded in the other comprehensive income component of shareholders' equity. Such an unrealized loss does not reduce net income attributable to 3M for the applicable accounting period because the loss is not viewed as other-than-temporary. The factors evaluated to differentiate between temporary and other-than-temporary include the projected future cash flows, credit ratings actions, and assessment of the credit quality of the underlying collateral, as well as other factors.

Table of Contents

The balances at March 31, 2016 for marketable securities by contractual maturity are shown below. Actual maturities may differ from contractual maturities because the issuers of the securities may have the right to prepay obligations without prepayment penalties.

(Millions)	March 31, 2016
Due in one year or less	$ 95
Due after one year through five years	95
Due after five years through ten years	1
Due after ten years	—
Total marketable securities	$ 191

3M has a diversified marketable securities portfolio of $191 million as of March 31, 2016. Within this portfolio, asset-backed securities primarily include interests in automobile loans, credit cards and equipment leases. 3M's investment policy allows investments in asset-backed securities with minimum credit ratings of Aa2 by Moody's Investors Service or AA by Standard & Poor's or Fitch Ratings or DBRS. Asset-backed securities must be rated by at least two of the aforementioned rating agencies, one of which must be Moody's Investors Service or Standard & Poor's. At March 31, 2016, all asset-backed security investments were in compliance with this policy. Approximately 81.1 percent of all asset-backed security investments were rated AAA or A-1+ by Standard & Poor's and/or Aaa or P-1 by Moody's Investors Service and/or AAA or F1+ by Fitch Ratings. Interest rate risk and credit risk related to the underlying collateral may impact the value of investments in asset-backed securities, while factors such as general conditions in the overall credit market and the nature of the underlying collateral may affect the liquidity of investments in asset-backed securities. 3M does not currently expect risk related to its holding in asset-backed securities to materially impact its financial condition or liquidity.

NOTE 8. Long-Term Debt and Short-Term Borrowings

In March 2016, 3M amended and restated its existing $2.25 billion five-year revolving credit facility expiring in August 2019 to a $3.75 billion five-year revolving credit facility expiring in March 2021. This credit agreement includes a provision under which 3M may request an increase of up to $1.25 billion (at lender's discretion), bringing the total facility up to $5.0 billion. This revolving credit facility is undrawn at March 31, 2016. Under the $3.75 billion credit agreement, the Company is required to maintain its EBITDA to Interest Ratio as of the end of each fiscal quarter at not less than 3.0 to 1. This is calculated (as defined in the agreement) as the ratio of consolidated total EBITDA for the four consecutive quarters then ended to a total interest expense on all funded debt for the same period. At March 31, 2016, this ratio was approximately 51 to 1. Debt covenants do not restrict the payment of dividends.

Table of Contents

NOTE 9. Pension and Postretirement Benefit Plans

Net periodic benefit cost is recorded in cost of sales, selling, general and administrative expenses, and research, development and related expenses. Components of net periodic benefit cost and other supplemental information for the three months ended March 31, 2016 and 2015 follow:

Benefit Plan Information

	Three months ended March 31, Qualified and Non-qualified Pension Benefits				Postretirement Benefits	
	United States		International			
(Millions)	2016	2015	2016	2015	2016	2015
Net periodic benefit cost (benefit)						
Service cost	$ 65	$ 73	$ 33	$ 42	$ 13	$ 21
Interest cost	143	164	43	55	20	25
Expected return on plan assets	(260)	(267)	(78)	(81)	(23)	(22)
Amortization of transition (asset) obligation	—	—	—	—	—	—
Amortization of prior service cost (benefit)	(6)	(6)	(3)	(4)	(14)	(8)
Amortization of net actuarial (gain) loss	88	102	22	38	16	19
Net periodic benefit cost (benefit)	$ 30	$ 66	$ 17	$ 50	$ 12	$ 35
Settlements, curtailments, special termination benefits and other	—	—	—	(17)	—	—
Net periodic benefit cost (benefit) after settlements, curtailments, special termination benefits and other	$ 30	$ 66	$ 17	$ 33	$ 12	$ 35

For the three months ended March 31, 2016, contributions totaling $55 million were made to the Company's U.S. and international pension plans and $1 million to its postretirement plans. For total year 2016, the Company expects to contribute between approximately $200 million to $400 million of cash to its global defined benefit pension and postretirement plans. The Company does not have a required minimum cash pension contribution obligation for its U.S. plans in 2016. Future contributions will depend on market conditions, interest rates and other factors. 3M's annual measurement date for pension and postretirement assets and liabilities is December 31 each year, which is also the date used for the related annual measurement assumptions.

Beginning in 2016, 3M changed the method used to estimate the service and interest cost components of the net periodic pension and other postretirement benefit costs. The new method measures service cost and interest cost separately using the spot yield curve approach applied to each corresponding obligation. Service costs are determined based on duration-specific spot rates applied to the service cost cash flows. The interest cost calculation is determined by applying duration-specific spot rates to the year-by-year projected benefit payments. The spot yield curve approach does not affect the measurement of the total benefit obligations as the change in service and interest costs offset in the actuarial gains and losses recorded in other comprehensive income. The Company changed to the new method to provide a more precise measure of service and interest costs by improving the correlation between the projected benefit cash flows and the discrete spot yield curve rates. The Company accounted for this change as a change in estimate prospectively beginning in the first quarter of 2016. As a result of the change to the spot yield curve approach, 2016 annual defined benefit pension and postretirement net periodic benefit cost has decreased approximately $180 million.

Using this methodology, the Company determined discount rates for its plans as follows:

	U.S. Qualified Pension		International Pension (weighted average)		U.S. Postretirement Medical	
December 31, 2015 Liability:						
Benefit obligation	4.47	%	3.12	%	4.32	%
2016 Net Periodic Benefit Cost Components:						
Service cost	4.72	%	2.84	%	4.60	%
Interest cost	3.77	%	2.72	%	3.44	%

Table of Contents

The Company also sponsors employee savings plans under Section 401(k) of the Internal Revenue Code, as discussed in Note 11 in 3M's 2015 Annual Report on Form 10-K. Beginning on January 1, 2016, for U.S. employees, the Company reduced its match on employee 401(k) contributions. For eligible employees hired prior to January 1, 2009, employee 401(k) contributions of up to 5% of eligible compensation are matched in cash at rates of 45% or 60%, depending on the plan in which the employee participates. Employees hired on or after January 1, 2009, receive a cash match of 100% for employee 401(k) contributions of up to 5% of eligible compensation and also continue to receive an employer retirement income account cash contribution of 3% of the participant's total eligible compensation.

In August 2015, 3M modified the 3M Retiree Welfare Benefit Plan postretirement medical benefit reducing the future benefit for participants not retired as of January 1, 2016. Current retirees and employees who retired on or before January 1, 2016, were not impacted by these changes. The Retiree Medical Savings Account (RMSA) is no longer credited with interest, and the indexation on both the RMSA and the Medicare Health Reimbursement Arrangement was reduced from 3 percent to 1.5 percent per year (for those employees who are eligible for these accounts). Also effective January 1, 2016, 3M no longer offered 3M Retiree Health Care Accounts to new hires. Due to these changes the plan was re-measured in the third quarter of 2015, resulting in a decrease to the projected benefit obligation liability of approximately $233 million, and a related increase to shareholders' equity, specifically accumulated other comprehensive income.

In March 2015, 3M Japan modified the Japan Limited Defined Benefit Corporate Pension Plan (DBCPP). Beginning July 1, 2015, eligible employees receive a company provided contribution match of 6.12% of their eligible salary to their defined contribution plan. Employees no longer earn additional service towards their defined benefit pension plans after July 1, 2015, except for eligible salaries above the statutory defined contribution limits. As a result of this plan modification, the Company re-measured the DBCPP, which resulted in a $17 million pre-tax curtailment gain for the three months ended March 31, 2015.

3M was informed during the first quarter of 2009, that the general partners of WG Trading Company, in which 3M's benefit plans hold limited partnership interests, are the subject of a criminal investigation as well as civil proceedings by the SEC and CFTC (Commodity Futures Trading Commission). In March 2011, over the objections of 3M and six other limited partners of WG Trading Company, the district court judge ruled in favor of the court appointed receiver's proposed distribution plan (and in April 2013, the United States Court of Appeals for the Second Circuit affirmed the district court's ruling). The benefit plan trustee holdings of WG Trading Company interests were adjusted to reflect the decreased estimated fair market value, inclusive of estimated insurance proceeds, as of the annual measurement dates. The Company has insurance that it believes, based on what is currently known, will result in the probable recovery of a portion of the decrease in original asset value. In the first quarter of 2014, 3M and certain 3M benefit plans filed a lawsuit in the U.S. District Court for the District of Minnesota against five insurers seeking insurance coverage for the WG Trading Company claim. In September 2015, the court ruled in favor of the defendant insurance companies on a motion for summary judgment and dismissed the lawsuit. In October 2015, 3M and the 3M benefit plans filed a notice of appeal to the United States Court of Appeals for the Eighth Circuit. As of the 2015 measurement date, these holdings represented less than one half of one percent of 3M's fair value of total plan assets. 3M currently believes that the resolution of these events will not have a material adverse effect on the consolidated financial position of the Company.

Table of Contents

NOTE 10. Derivatives

The Company uses interest rate swaps, currency swaps, commodity price swaps, and forward and option contracts to manage risks generally associated with foreign exchange rate, interest rate and commodity price fluctuations. The information that follows explains the various types of derivatives and financial instruments used by 3M, how and why 3M uses such instruments, how such instruments are accounted for, and how such instruments impact 3M's financial position and performance.

Additional information with respect to the impacts on other comprehensive income of nonderivative hedging and derivative instruments is included in Note 5. Additional information with respect to the fair value of derivative instruments is included in Note 11. References to information regarding derivatives and/or hedging instruments associated with the Company's long-term debt are also made in Note 10 in 3M's 2015 Annual Report on Form 10-K.

Types of Derivatives/Hedging Instruments and Inclusion in Income/Other Comprehensive Income

Cash Flow Hedges:

For derivative instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss on the derivative is reported as a component of other comprehensive income and reclassified into earnings in the same period during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings.

Cash Flow Hedging - Foreign Currency Forward and Option Contracts: The Company enters into foreign exchange forward and option contracts to hedge against the effect of exchange rate fluctuations on cash flows denominated in foreign currencies. These transactions are designated as cash flow hedges. The settlement or extension of these derivatives will result in reclassifications (from accumulated other comprehensive income) to earnings in the period during which the hedged transactions affect earnings. 3M may dedesignate these cash flow hedge relationships in advance of the occurrence of the forecasted transaction. The portion of gains or losses on the derivative instrument previously accumulated in other comprehensive income for dedesignated hedges remains in accumulated other comprehensive income until the forecasted transaction occurs. Changes in the value of derivative instruments after dedesignation are recorded in earnings and are included in the Derivatives Not Designated as Hedging Instruments section below. Beginning in the second quarter of 2014, 3M began extending the maximum length of time over which it hedges its exposure to the variability in future cash flows of the forecasted transactions from a previous term of 12 months to a longer term of 24 months, with certain currencies being extended further to 36 months starting in the first quarter of 2015.

Cash Flow Hedging - Commodity Price Management: The Company manages commodity price risks through negotiated supply contracts, price protection agreements and forward contracts. 3M discontinued the use of commodity price swaps as cash flow hedges of forecasted commodity transactions in the first quarter of 2015. The Company used commodity price swaps as cash flow hedges of forecasted commodity transactions to manage price volatility. The related mark-to-market gain or loss on qualifying hedges was included in other comprehensive income to the extent effective, and reclassified into cost of sales in the period during which the hedged transaction affected earnings.

Cash Flow Hedging — Interest Rate Contracts: The Company may use forward starting interest rate contracts to hedge exposure to variability in cash flows from forecasted debt issuances. The amortization of gains and losses on forward starting interest rate swaps is included in the tables below as part of the gain/(loss) recognized in income on the effective portion of derivatives as a result of reclassification from accumulated other comprehensive income. Additional information regarding previously issued and terminated interest rate contracts can be found in Note 12 in 3M's 2015 Annual Report on Form 10-K.

In February 2016, the Company entered into a forward starting interest rate swap expiring in December 2016 with a notional amount of $100 million as a hedge against interest rate volatility associated with a forecasted issuance of fixed rate debt.

Table of Contents

As of March 31, 2016, the Company had a balance of $14 million associated with the after-tax net unrealized gain associated with cash flow hedging instruments recorded in accumulated other comprehensive income. This includes a remaining balance of $5 million (after tax loss) related to the forward starting interest rate swaps, which will be amortized over the respective lives of the debt. Based on exchange rates as of March 31, 2016, 3M expects to reclassify approximately $38 million of the after-tax net unrealized foreign exchange cash flow hedging gains to earnings over the remainder of 2016, approximately $9 million of the after-tax net unrealized foreign exchange cash flow hedging losses to earnings in 2017, and approximately $15 million of the after-tax net unrealized foreign exchange cash flow hedging losses to earnings after 2017 (with the impact offset by earnings/losses from underlying hedged items). 3M expects to reclassify approximately $36 million of the after-tax net unrealized foreign exchange cash flow hedging gains to earnings over the next 12 months.

The location in the consolidated statements of income and comprehensive income and amounts of gains and losses related to derivative instruments designated as cash flow hedges are provided in the following table.

Three months ended March 31, 2016

Derivatives in Cash Flow Hedging Relationships (Millions)	Pretax Gain (Loss) Recognized in Other Comprehensive Income on Effective Portion of Derivative	Pretax Gain (Loss) Recognized in Income on Effective Portion of Derivative as a Result of Reclassification from Accumulated Other Comprehensive Income		Ineffective Portion of Gain (Loss) on Derivative and Amount Excluded from Effectiveness Testing Recognized in Income	
	Amount	Location	Amount	Location	Amount
Foreign currency forward/option contracts	$ (120)	Cost of sales	$ 53	Cost of sales	$ —
Interest rate swap contracts	(1)	Interest expense	(1)	Interest expense	—
Total	$ (121)		$ 52		$ —

Three months ended March 31, 2015

Derivatives in Cash Flow Hedging Relationships (Millions)	Pretax Gain (Loss) Recognized in Other Comprehensive Income on Effective Portion of Derivative	Pretax Gain (Loss) Recognized in Income on Effective Portion of Derivative as a Result of Reclassification from Accumulated Other Comprehensive Income		Ineffective Portion of Gain (Loss) on Derivative and Amount Excluded from Effectiveness Testing Recognized in Income	
	Amount	Location	Amount	Location	Amount

Foreign currency forward/option contracts	$	136	Cost of sales	$	30	Cost of sales	$	—
Commodity price swap contracts		—	Cost of sales		(2)	Cost of sales		—
Interest rate swap contracts		—	Interest expense		(1)	Interest expense		—
Total	$	136		$	27		$	—

Fair Value Hedges:

For derivative instruments that are designated and qualify as fair value hedges, the gain or loss on the derivatives as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in current earnings.

Fair Value Hedging - Interest Rate Swaps: The Company manages interest expense using a mix of fixed and floating rate debt. To help manage borrowing costs, the Company may enter into interest rate swaps. Under these arrangements, the Company agrees to exchange, at specified intervals, the difference between fixed and floating interest amounts calculated by reference to an agreed-upon notional principal amount. The mark-to-market of these fair value hedges is recorded as gains or losses in interest expense and is offset by the gain or loss of the underlying debt instrument, which also is recorded in interest expense. These fair value hedges are highly effective and, thus, there is no impact on earnings due to hedge ineffectiveness. Additional information regarding designated interest rate swaps can be found in Note 12 in 3M's 2015 Annual Report on Form 10-K.

The location in the consolidated statements of income and amounts of gains and losses related to derivative instruments designated as fair value hedges and similar information relative to the hedged items are as follows:

Table of Contents

Three months ended March 31, 2016

Derivatives in Fair Value Hedging Relationships (Millions)	Gain (Loss) on Derivative Recognized in Income		Gain (Loss) on Hedged Item Recognized in Income	
	Location	Amount	Location	Amount
Interest rate swap contracts	Interest expense	$ 29	Interest expense	$ (29)
Total		$ 29		$ (29)

Three months ended March 31, 2015

Derivatives in Fair Value Hedging Relationships (Millions)	Gain (Loss) on Derivative Recognized in Income		Gain (Loss) on Hedged Item Recognized in Income	
	Location	Amount	Location	Amount
Interest rate swap contracts	Interest expense	$ 6	Interest expense	$ (6)
Total		$ 6		$ (6)

Net Investment Hedges:

The Company may use non-derivative (foreign currency denominated debt) and derivative (foreign exchange forward contracts) instruments to hedge portions of the Company’s investment in foreign subsidiaries and manage foreign exchange risk. For instruments that are designated and qualify as hedges of net investments in foreign operations and that meet the effectiveness requirements, the net gains or losses attributable to changes in spot exchange rates are recorded in cumulative translation within other comprehensive income. The remainder of the change in value of such instruments is recorded in earnings. Recognition in earnings of amounts previously recorded in cumulative translation is limited to circumstances such as complete or substantially complete liquidation of the net investment in the hedged foreign operation. To the extent foreign currency denominated debt is not designated in or is dedesignated from a net investment hedge relationship, changes in value of that portion of foreign currency denominated debt due to exchange rate changes are recorded in earnings through their maturity date.

3M’s use of foreign exchange forward contracts designated in hedges of the Company’s net investment in foreign subsidiaries can vary by time period depending on when foreign currency denominated debt balances designated in such relationships are dedesignated, matured, or are newly issued and designated. Additionally, variation can occur in connection with the extent of the Company’s desired foreign exchange risk coverage.

At March 31, 2016, the total notional amount of foreign exchange forward contracts designated in net investment hedges was approximately 974 million Euros and approximately 248 billion South Korean Won, along with a principal amount of long-term debt instruments designated in net investment hedges totaling 3.6 billion Euros. The maturity dates of these derivative and nonderivative instruments designated in net investment hedges range from 2016 to 2030.

The location in the consolidated statements of income and comprehensive income and amounts of gains and losses related to derivative and nonderivative instruments designated as net investment hedges are as follows. There were no reclassifications of the effective portion of net investment hedges out of accumulated other comprehensive income into income for the periods presented in the table below.

Table of Contents

Three months ended March 31, 2016

Derivative and Nonderivative Instruments in Net Investment Hedging Relationships (Millions)	Pretax Gain (Loss) Recognized as Cumulative Translation within Other Comprehensive Income on Effective Portion of Instrument	Ineffective Portion of Gain (Loss) on Instrument and Amount Excluded from Effectiveness Testing Recognized in Income	
	Amount	Location	Amount
Foreign currency denominated debt	$ (144)	N/A	$ —
Foreign currency forward contracts	(43)	Cost of sales	(2)
Total	$ (187)		$ (2)

Three months ended March 31, 2015

Derivative and Nonderivative Instruments in Net Investment Hedging Relationships (Millions)	Pretax Gain (Loss) Recognized as Cumulative Translation within Other Comprehensive Income on Effective Portion of Instrument	Ineffective Portion of Gain (Loss) on Instrument and Amount Excluded from Effectiveness Testing Recognized in Income	
	Amount	Location	Amount
Foreign currency denominated debt	$ 240	N/A	$ —
Foreign currency forward contracts	157	Cost of sales	—
Total	$ 397		$ —

Derivatives Not Designated as Hedging Instruments:

3M enters into foreign exchange forward contracts that are not designated in hedge relationships to offset, in part, the impacts of certain intercompany transactions and to further mitigate short-term currency impacts. In addition, the Company enters into commodity price swaps to offset, in part, fluctuations in costs associated with the use of certain precious metals. These derivative instruments are not designated in hedging relationships; therefore, fair value gains and losses on these contracts are recorded in earnings. The Company does not hold or issue derivative financial instruments for trading purposes.

The location in the consolidated statements of income and amounts of gains and losses related to derivative instruments not designated as hedging instruments are as follows:

Derivatives Not Designated as Hedging Instruments (Millions)	Three months ended March 31, 2016 Gain (Loss) on Derivative Recognized in Income Location	Amount
Foreign currency forward/option contracts	Cost of sales	$ (5)
Foreign currency forward contracts	Interest expense	(7)
Total		$ (12)

Derivatives Not Designated as Hedging Instruments (Millions)	Three months ended March 31, 2015 Gain (Loss) on Derivative Recognized in Income Location	Amount
Foreign currency forward/option contracts	Cost of sales	$ 4
Foreign currency forward contracts	Interest expense	89
Commodity price swap contracts	Cost of sales	(4)
Total		$ 89

Table of Contents

Location and Fair Value Amount of Derivative Instruments

The following tables summarize the fair value of 3M's derivative instruments, excluding nonderivative instruments used as hedging instruments, and their location in the consolidated balance sheet. Notional amounts below are presented at period end foreign exchange rates, except interest rate swaps, which are presented using the contract inception date's foreign exchange rate. Additional information with respect to the fair value of derivative instruments is included in Note 11.

March 31, 2016 (Millions)	Gross Notional Amount	Assets Location	Fair Value Amount	Liabilities Location	Fair Value Amount
Derivatives designated as hedging instruments					
Foreign currency forward/option contracts	$ 3,159	Other current assets	$ 72	Other current liabilities	$ 83
Foreign currency forward/option contracts	1,192	Other assets	26	Other liabilities	26
Interest rate swap contracts	1,853	Other assets	53	Other current liabilities	1
Total derivatives designated as hedging instruments			$ 151		$ 110
Derivatives not designated as hedging instruments					
Foreign currency forward/option contracts	$ 4,775	Other current assets	$ 19	Other current liabilities	$ 46
Total derivatives not designated as hedging instruments			$ 19		$ 46
Total derivative instruments			$ 170		$ 156

December 31, 2015 (Millions)	Gross Notional Amount	Assets Location	Fair Value Amount	Liabilities Location	Fair Value Amount
Derivatives designated as hedging instruments					
Foreign currency forward/option contracts	$ 2,815	Other current assets	$ 148	Other current liabilities	$ 14
Foreign currency forward/option contracts	1,240	Other assets	61	Other liabilities	3

Interest rate swap contracts	1,753	Other assets	24	Other liabilities	1
Total derivatives designated as hedging instruments			$ 233		$ 18