UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

(Mark one)

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

For the quarter ended September 30, 2023

☐ **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: 001-35475

ZURN ELKAY WATER SOLUTIONS CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**20-5197013**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification No.)**
511 W. Freshwater Way	**53204**
Milwaukee, Wisconsin	**(Zip Code)**
(Address of Principal Executive Offices)	

Registrant's telephone number, including area code: (855) 480-5050

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

Title of Each Class	Trading Symbol(s)	Name of Each Exchange on Which Registered
Common Stock, $.01 par value	**ZWS**	**The New York Stock Exchange**

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 checkmark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§229.405 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 whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	☒	Accelerated filer	☐
Non-accelerated filer	☐	Smaller reporting company	☐
		Emerging growth 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 accounting 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 Exchange Act Rule 12b-2). 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 October 27, 2023
Zurn Elkay Water Solutions Corporation Common Stock, $0.01 par value per share	172,810,551 shares

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Private Securities Litigation Reform Act Safe Harbor Statement

Our disclosure and analysis in this report concerning our operations, cash flows and financial position, including, in particular, the likelihood of our success in developing and expanding our business and the realization of sales from our backlog, include forward-looking statements. Statements that are predictive in nature, that depend upon or refer to future events or conditions, or that include words such as “expects,” “anticipates,” “intends,” “plans,” “believes,” “estimates” and similar expressions are forward-looking statements. Although these statements are based upon reasonable assumptions, including projections of orders, sales, operating margins, earnings, cash flows, research and development costs, working capital and capital expenditures, they are subject to risks and uncertainties that are described more fully herein and in our Annual Report on Form 10-K for the year ended December 31, 2022, in Part I, Item 1A, “Risk Factors” and in Part I under the heading "Cautionary Notice Regarding Forward-Looking Statements", as well as in our other filings with the Securities and Exchange Commission. Accordingly, we can give no assurance that we will achieve the results anticipated or implied by our forward-looking statements. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise, except as required by law.

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Zurn Elkay Water Solutions Corporation and Subsidiaries
Condensed Consolidated Balance Sheets
(in Millions, except share amounts)

	(Unaudited) September 30, 2023	December 31, 2022
Assets		
Current assets:		
Cash and cash equivalents	$ 173.1	$ 124.8
Receivables, net	233.9	219.7
Inventories	284.3	366.7
Income taxes receivable	4.0	18.3
Other current assets	26.0	28.0
Total current assets	721.3	757.5
Property, plant and equipment, net	189.1	183.8
Intangible assets, net	966.0	1,009.7
Goodwill	795.3	777.0
Insurance for asbestos claims	72.1	72.1
Other assets	69.1	63.9
Total assets	$ 2,812.9	$ 2,864.0
Liabilities and stockholders' equity		
Current liabilities:		
Current maturities of debt	$ 6.3	$ 5.7
Trade payables	60.7	116.9
Compensation and benefits	25.1	19.2
Current portion of pension and postretirement benefit obligations	1.6	1.6
Other current liabilities	136.1	145.9
Total current liabilities	229.8	289.3
Long-term debt	547.9	530.2
Pension and postretirement benefit obligations	53.2	50.5
Deferred income taxes	205.5	221.4
Operating lease liability	39.6	34.2
Reserve for asbestos claims	78.9	79.0
Other liabilities	46.4	44.4
Total liabilities	1,201.3	1,249.0
Stockholders' equity:		
Common stock, $0.01 par value; 200,000,000 shares authorized; shares issued and outstanding: 172,623,478 at September 30, 2023 and 176,876,406 at December 31, 2022	1.7	1.8
Additional paid-in capital	2,850.4	2,853.1
Retained deficit	(1,166.9)	(1,164.9)
Accumulated other comprehensive loss	(73.6)	(75.0)
Total stockholders' equity	1,611.6	1,615.0
Total liabilities and stockholders' equity	$ 2,812.9	$ 2,864.0

See notes to the condensed consolidated financial statements.

Zurn Elkay Water Solutions Corporation and Subsidiaries
Condensed Consolidated Statements of Operations
(in Millions, except share and per share amounts)
(Unaudited)

	Three Months Ended		Nine Months Ended	
	September 30, 2023	September 30, 2022	September 30, 2023	September 30, 2022
Net sales	$ 398.4	$ 417.7	$ 1,173.7	$ 941.5
Cost of sales	228.5	277.3	681.5	585.4
Gross profit	169.9	140.4	492.2	356.1
Selling, general and administrative expenses	92.9	124.3	277.7	236.6
Restructuring and other similar charges	2.2	11.7	11.9	13.1
Amortization of intangible assets	14.7	14.5	44.0	19.1
Income (loss) from operations	60.1	(10.1)	158.6	87.3
Non-operating expense:				
Interest expense, net	(9.9)	(8.0)	(29.8)	(18.0)
Other income (expense), net	(2.5)	0.6	(3.3)	0.3
Income (loss) before income taxes	47.7	(17.5)	125.5	69.6
Provision for income taxes	(12.5)	(1.6)	(34.8)	(22.9)
Net income (loss) from continuing operations	35.2	(19.1)	90.7	46.7
Income from discontinued operations, net of tax	6.2	—	8.1	0.8
Net income (loss)	$ 41.4	$ (19.1)	$ 98.8	$ 47.5
Basic net income (loss) per share:				
Continuing operations	$ 0.20	$ (0.11)	$ 0.52	$ 0.33
Discontinued operations	$ 0.04	$ —	$ 0.05	$ 0.01
Net income (loss)	$ 0.24	$ (0.11)	$ 0.57	$ 0.33
Diluted net income (loss) per share:				
Continuing operations	$ 0.20	$ (0.11)	$ 0.51	$ 0.32
Discontinued operations	$ 0.04	$ —	$ 0.05	$ 0.01
Net income (loss)	$ 0.24	$ (0.11)	$ 0.56	$ 0.33
Weighted-average number of shares outstanding (in thousands):				
Basic	173,276	174,867	174,632	142,699
Effect of dilutive equity awards	2,866	—	2,803	2,004
Diluted	176,142	174,867	177,435	144,703

See notes to the condensed consolidated financial statements.

Zurn Elkay Water Solutions Corporation and Subsidiaries
Condensed Consolidated Statements of Comprehensive Income
(in Millions)
(Unaudited)

	Three Months Ended		Nine Months Ended	
	September 30, 2023	September 30, 2022	September 30, 2023	September 30, 2022
Net income (loss)	$ 41.4	$ (19.1)	$ 98.8	$ 47.5
Other comprehensive income (loss):				
Foreign currency translation adjustments	(2.1)	(4.1)	1.4	(4.1)
Other comprehensive income (loss), net of tax	(2.1)	(4.1)	1.4	(4.1)
Total comprehensive income (loss)	$ 39.3	$ (23.2)	$ 100.2	$ 43.4

See notes to the condensed consolidated financial statements.

Zurn Elkay Water Solutions Corporation and Subsidiaries
Condensed Consolidated Statements of Cash Flows
(in Millions)
(Unaudited)

	Nine Months Ended	
	September 30, 2023	**September 30, 2022**
Operating activities		
Net income	$ 98.8	$ 47.5
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation	22.3	11.8
Amortization of intangible assets	44.0	19.1
Non-cash asset impairment	2.5	—
Loss on dispositions of long-lived assets	—	0.3
Deferred income taxes	(7.1)	4.1
Other non-cash expenses	1.8	5.3
Stock-based compensation expense	30.5	15.5
Changes in operating assets and liabilities:		
Receivables, net	(14.0)	(34.4)
Inventories	57.7	(50.9)
Other assets	17.1	34.8
Accounts payable	(56.4)	9.7
Accruals and other	(1.5)	(50.2)
Cash provided by operating activities	195.7	12.6
Investing activities		
Expenditures for property, plant and equipment	(15.9)	(4.3)
Acquisitions, net of cash acquired	—	(44.8)
Proceeds from dispositions of long-lived assets	0.3	1.3
Proceeds from insurance claims	9.0	—
Proceeds associated with divestiture of discontinued operations	—	35.0
Cash used for investing activities	(6.6)	(12.8)
Financing activities		
Proceeds from borrowings of debt	13.0	85.0
Repayments of debt	(17.7)	(89.4)
Proceeds from exercise of stock options	1.9	1.9
Taxes withheld and paid on employees' share-based payment awards	(1.9)	(0.5)
Repurchase of common stock	(100.2)	—
Payment of common stock dividends	(36.6)	(20.1)
Cash used for financing activities	(141.5)	(23.1)
Effect of exchange rate changes on cash, cash equivalents and restricted cash	0.7	(1.4)
Increase (decrease) in cash, cash equivalents and restricted cash	48.3	(24.7)
Cash, cash equivalents and restricted cash at beginning of period	124.8	96.6
Cash, cash equivalents and restricted cash at end of period	$ 173.1	$ 71.9

See notes to the condensed consolidated financial statements.

Zurn Elkay Water Solutions Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements
September 30, 2023
(Unaudited)

1. Basis of Presentation and Significant Accounting Policies

The unaudited condensed consolidated financial statements included herein have been prepared by Zurn Elkay Water Solutions Corporation (“Zurn Elkay” or the “Company”) in accordance with accounting principles generally accepted in the United States ("GAAP") pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the disclosures are adequate to make the information presented not misleading.

In the opinion of management, the condensed consolidated financial statements include all adjustments necessary for a fair presentation of the results of operations for the interim periods. Results for the interim periods are not necessarily indicative of results that may be expected for the year ending December 31, 2023. These condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2022.

The Company

On July 1, 2022, Zurn Water Solutions Corporation ("Zurn") completed its combination with Elkay Manufacturing Company (“Elkay”) through the Merger of Elkay with and into a newly created subsidiary of the Company, with Elkay surviving as a wholly owned subsidiary of Zurn Elkay (the “Merger” or "Elkay Transaction"). The Company's results of operations include the acquired operations subsequent to July 1, 2022. See Note 2, Acquisition, for additional information on the Elkay Transaction.

Zurn Elkay Water Solutions Corporation is a growth-oriented, pure-play water management business that designs, procures, manufactures, and markets what the Company believes to be the broadest sustainable product portfolio of specification-driven water management solutions to improve health, human safety and the environment. The Company's product portfolio includes professional grade water safety and control products, flow system products, hygienic and environmental products, and drinking water products for public and private spaces that deliver superior value to building owners, positively impact the environment and human hygiene and reduce product installation time. The Company's heritage of innovation and specification has allowed it to provide highly-engineered, mission-critical solutions to customers for decades and affords it the privilege of having long-term, valued relationships with market leaders. The Company operates in a disciplined way and the Zurn Elkay Business System (“ZEBS”) is its operating philosophy. Grounded in the spirit of continuous improvement, ZEBS creates a scalable, process-based framework that focuses on driving superior customer satisfaction and financial results by targeting world-class operating performance throughout all aspects of its business.

Reclassifications

Certain prior year amounts have been reclassified to conform to the presentation used for the nine months ended September 30, 2023.

2. Acquisition

Elkay Merger

On July 1, 2022, the Company completed the Elkay Merger for a purchase price of $ 1,457.8 million. Elkay, a market leader of drinking water solutions and commercial sinks, complements the Company's existing product portfolio. The purchase price includes $1,411.9 million of Zurn's common stock based on Zurn's closing stock price of $27.48 on July 1, 2022, and $45.9 million of net cash payments for the repayment of Elkay's term loan and Elkay's transaction related costs outstanding that were in excess of Elkay's cash and cash equivalents at the time of closing. Pursuant to the terms of the merger agreement, the Company issued 51,564,524 shares of its common stock, which represented approximately 29% of outstanding shares immediately following the Merger. During the six months ended June 30, 2023, we completed the final price adjustments and the adjusted purchase price is reflected in the purchase price amounts above, following the return of 186,020 of the shares issued at closing to the Company as a result of lower working capital and cash balances at closing compared to targets stipulated in the merger agreement. The shares returned to the Company were canceled upon receipt.

In accordance with the merger agreement, at closing the Company increased the size of its Board of Directors to eleven members and appointed two directors designated by Elkay. As of September 30, 2023, the Board of Directors consisted of ten members, including one director designated by Elkay. Zurn senior management immediately prior to the consummation of the Elkay Merger remained as the executive officers of the Company immediately after the Elkay Merger. The Company's management determined that the Company is the accounting acquirer in the Elkay Merger based on the facts and circumstances noted within this section and other relevant factors. As such, the Company applied the acquisition method of accounting to the identifiable assets and liabilities of the Elkay business, which have been measured at estimated fair value as of the date of the business combination. The excess of the purchase price over the fair value assigned to the assets acquired and liabilities assumed was recorded as goodwill, which is not expected to be deductible for tax purposes.

Elkay’s assets and liabilities were measured at estimated fair values at July 1, 2022, primarily using Level 3 inputs. Estimates of fair value represent management’s best estimate of assumptions about future events and uncertainties, including significant judgments related to future cash flows, discount rates, competitive trends, margin and revenue growth assumptions including royalty rates and customer attrition rates and others. Inputs used were generally obtained from historical data supplemented by current and anticipated market conditions and growth rates expected as of the Merger date.

As of June 30, 2023, the valuation process to determine the fair values of the net assets acquired during the measurement period was complete. The final fair value of the assets acquired and liabilities assumed were as follows (in millions):

		As Reported June 30, 2023
Assets acquired:		
Receivables, net	$	92.0
Inventories		139.5
Other current assets		8.5
Property, plant and equipment, net		127.1
Intangible assets, net		865.5
Goodwill		546.2
Other assets		56.9
Total assets acquired		1,835.7
Liabilities assumed:		
Trade payables		30.5
Compensation and benefits		39.3
Current portion of pension and postretirement benefit obligations		17.3
Other current liabilities		45.8
Operating lease liability		24.2
Pension and postretirement benefit obligations		3.6
Deferred income taxes		206.7
Other liabilities		10.5
Total liabilities assumed		377.9
Total purchase price	$	1,457.8

Unaudited Pro Forma Information

The following unaudited supplemental pro forma financial information presents the financial results from continuing operations for the nine months ended September 30, 2022 as if the Elkay Merger had occurred on January 1, 2022. The pro forma financial information includes, where applicable, adjustments for: (i) additional amortization expense that would have been recognized related to the acquired intangible assets, (ii) additional depreciation expense that would have been recognized related to the acquired property, plant, and equipment, (iii) removing Elkay Merger-Related costs recognized by Elkay during the nine months ended September 30, 2022 as these costs will not affect the combined operations, and (iv) the estimated income tax effect on the pro forma adjustments. The pro forma financial information excludes adjustments for estimated cost synergies or other effects of the integration of the Elkay Merger.

The pro forma financial information is presented for illustrative purposes only and is not necessarily indicative of the operating results that would have been achieved had the Elkay Merger been completed as of the date indicated or the results that may be obtained in the future.

		Nine Months Ended September 30, 2022
Net sales	$	1,240.2
Net income from continuing operations	$	71.4
Earnings per share from continuing operations		
Basic	$	0.50
Assuming dilution	$	0.49

3. Restructuring and Other Similar Charges

During the three and nine months ended September 30, 2023, the Company continued to execute various restructuring actions. These initiatives were implemented to drive efficiencies and reduce operating costs while also modifying the Company's footprint to reflect changes in the markets it serves, the impact of acquisitions, including Elkay, on the Company's overall manufacturing capacity and the refinement of its overall product portfolio. These restructuring actions primarily resulted in workforce reductions, lease termination costs and other facility rationalization costs. Management expects to continue executing similar initiatives to optimize its operating margin and manufacturing footprint. As such, the Company expects further expenses related to workforce reductions, potential impairment or accelerated depreciation of assets, lease termination costs and other facility rationalization costs. The Company's restructuring plans are preliminary and the full extent of related expenses are not yet estimable.

The following table summarizes the Company's restructuring and other similar charges during the three and nine months ended September 30, 2023 and September 30, 2022, (in millions):

	Three Months Ended		Nine Months Ended	
	September 30, 2023	September 30, 2022	September 30, 2023	September 30, 2022
Employee termination benefits	$ 0.5	$ 10.5	$ 3.4	$ 11.8
Contract termination and other associated costs	1.7	1.2	8.5	1.3
Total restructuring and other similar costs	$ 2.2	$ 11.7	$ 11.9	$ 13.1

The following table summarizes the activity in the Company's restructuring accrual for the nine months ended September 30, 2023 (in millions):

	Employee termination benefits	Contract termination and other associated costs	Total
Accrued Restructuring Costs, December 31, 2022 (1)	$ 7.8	$ 1.2	$ 9.0
Charges	3.4	8.5	11.9
Cash payments	(9.2)	(7.0)	(16.2)
Non-cash charges (2)	—	(2.5)	(2.5)
Accrued Restructuring Costs, September 30, 2023 (1)	$ 2.0	$ 0.2	$ 2.2

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(1) As of September 30, 2023, the restructuring accrual is included in other current liabilities in the condensed consolidated balance sheets. As of December 31, 2022, $8.4 million of the restructuring accrual is included in other current liabilities and $0.6 million is included in other liabilities in the condensed consolidated balance sheets.

(2) Non-cash charges consist of asset impairments based on Level 3 inputs.

4. Discontinued Operations

On October 4, 2021, the Company completed a Reverse Morris Trust tax-free spin-off transaction (the “Spin-Off Transaction”) in which (i) substantially all the assets and liabilities of the Company's Process & Motion Control ("PMC") business were transferred to a newly created subsidiary, Land Newco, Inc. (“Land”), (ii) the shares of Land were distributed to the Company's stockholders pro rata, and (iii) Land was merged with a subsidiary of Regal Rexnord Corporation (formerly known as Regal Beloit Corporation), in which the stock of Land was converted into a specified number of shares of Regal Rexnord Corporation in accordance with the exchange ratio. The operating results of PMC are reported as discontinued operations in the condensed consolidated statements of operations for all periods presented, as the Spin-Off Transaction of PMC represented a strategic shift that had a major impact on operations and financial results. The condensed consolidated statements of cash flows for the nine months ended September 30, 2023 and September 30, 2022 have not been adjusted to separately disclose cash flows related to the discontinued operations. During 2022, the Company received $35.0 million from Regal Rexnord Corporation as a result of the final working capital and cash balances at closing exceeding the targets stipulated in the Spin-Off Transaction agreement.

The major components of the Income from discontinued operations, net of tax presented in the condensed consolidated statements of operations for the three and nine months ended September 30, 2023 and September 30, 2022, are as follows (in millions):

	Three Months Ended		Nine Months Ended	
	September 30, 2023	September 30, 2022	September 30, 2023	September 30, 2022
Selling, general and administrative expenses (1)	$ 6.6	$ —	$ 8.4	$ —
Income from discontinued operations before income tax	6.6	—	8.4	—
Income tax (expense) benefit	(0.4)	—	(0.3)	0.8
Income from discontinued operations, net of tax	$ 6.2	$ —	$ 8.1	$ 0.8

(1) Selling, general and administrative expenses include the reversal of certain accruals as a result of costs the Company will no longer incur related to the Spin-Off Transaction.

The condensed consolidated statements of cash flows for the nine months ended September 30, 2023 and September 30, 2022 have not been adjusted to separately disclose cash flows related to discontinued operations. However, the significant investing and financing cash flows and other significant non-cash operating items associated with the discontinued operations were as follows (in millions):

	Nine Months Ended	
	September 30, 2023	September 30, 2022
Proceeds associated with divestiture of discontinued operations	$ —	$ 35.0

5. Revenue Recognition

A performance obligation is a promise in a contract to transfer a distinct good or service to the customer, and is the unit of account in Accounting Standards Codification ("ASC") 606, *Revenue from Contracts with Customers*. A contract's transaction price is allocated to each distinct performance obligation and revenue is recognized when obligations under the terms of a contract with the customer are satisfied. For the majority of the Company's product sales, revenue is recognized at a point-in-time when control of the product is transferred to the customer, which generally occurs when the product is shipped from the Company's manufacturing facility to the customer. When contracts include multiple products to be delivered to the customer, generally each product is separately priced and is determined to be distinct within the context of the contract. Other than a standard assurance-type warranty that the product will conform to agreed-upon specifications, there are generally no other significant post-shipment obligations. The expected costs associated with standard warranties continue to be recognized as an expense when the products are sold.

When the contract provides the customer the right to return eligible products or when the customer is part of a sales rebate program, the Company reduces revenue at the point of sale using current facts and historical experience by using an estimate for expected product returns and rebates associated with the transaction. The Company adjusts these estimates at the earlier of when the most likely amount of consideration that is expected to be received changes or when the consideration becomes fixed. Accordingly, an increase or decrease to revenue is recognized at that time.

Sales and other taxes collected concurrent with revenue-producing activities are excluded from revenue. The Company has elected to recognize the cost for freight and shipping when control of products has transferred to the customer as a component of cost of sales in the consolidated statements of operations. The Company classifies shipping and handling fees billed to customers as net sales and the corresponding costs are classified as cost of sales in the condensed consolidated statements of operations.

Revenue by Category

The Company designs, procures, manufactures, and markets a comprehensive portfolio of water management solutions. The Company disaggregates its sales by customer type and geographic location, which the Company believes best depicts how the nature, amount, timing and uncertainty of its revenue and cash flows may be impacted differently by certain economic factors. The following tables present revenue disaggregated by customer type and the geographic region of the end customer (in millions):

	Three Months Ended		Nine Months Ended	
Customer Type	**September 30, 2023**	**September 30, 2022**	**September 30, 2023**	**September 30, 2022**
Institutional	$ 179.8	$ 169.8	$ 531.6	$ 366.2
Commercial	115.2	127.9	339.1	287.8
All other	103.4	120.0	303.0	287.5
Total	$ 398.4	$ 417.7	$ 1,173.7	$ 941.5

	Three Months Ended		Nine Months Ended	
Geography	**September 30, 2023**	**September 30, 2022**	**September 30, 2023**	**September 30, 2022**
United States	$ 366.6	$ 383.6	$ 1,082.6	$ 860.7
Canada	21.5	21.8	59.6	57.4
Rest of world	10.3	12.3	31.5	23.4
Total	$ 398.4	$ 417.7	$ 1,173.7	$ 941.5

Contract Balances

For substantially all of the Company's product sales, the customer is billed 100% of the contract value when the product ships and payment is generally due 30 days from shipment. Certain contracts include longer payment periods; however, the Company has elected to utilize the practical expedient in which the Company will only recognize a financing component to the sale if payment is due more than one year from the date of shipment.

Billings are recorded as accounts receivable when an unconditional right to the contractual consideration exists. Contract assets arise when the Company performs by transferring goods or services to a customer before the customer pays consideration, or before the customer's payment is due. A contract liability exists when the Company has received consideration or the amount is due from the customer in advance of revenue recognition. Contract liabilities and contract assets as of September 30, 2023 and December 31, 2022 were not material.

Backlog

The Company had backlog of $ 45.8 million as of September 30, 2023, which represents the most likely amount of consideration expected to be received in satisfying the remaining backlog under open contracts. The Company has elected to use the optional exemption provided by ASC 606-10-50-14A for variable consideration, and has not included estimated rebates in the amount of unsatisfied performance obligations. The Company expects to recognize approximately 95% of the backlog in the remaining three months of the year ending December 31, 2023, and the remaining approximately 5% in 2024 and beyond.

Timing of Performance Obligations Satisfied at a Point in Time

The Company determined that the customer is able to control the product when it is delivered to them; thus, depending on the shipping terms, control will transfer at different points between the Company's manufacturing facility or warehouse and the customer's location. The Company considers control to have transferred upon shipment or delivery because the Company has a present right to payment at that time, the customer has legal title to the asset, the Company has transferred physical possession of the asset and the customer has significant risks and rewards of ownership of the asset.

Variable Consideration

The Company provides volume-based rebates and the right to return product to certain customers, which are accrued for based on current facts and historical experience. Rebates are paid either on an annual or quarterly basis. There are no other significant variable consideration elements included in the Company's contracts with customers.

Contract Costs

The Company has elected to expense contract costs as incurred if the amortization period is expected to be one year or less. If the amortization period of these costs is expected to be greater than one year, the costs would be subject to capitalization. As of September 30, 2023 and December 31, 2022, the contract assets capitalized, as well as amortization recognized in the three and nine months ended September 30, 2023 and September 30, 2022, are not significant and no impairment losses were recognized.

Allowance for Credit Losses

The Company assesses the collectability of customer receivables based on the credit worthiness of a customer as determined by credit checks and analysis, as well as the customer's payment history. In determining the allowance for credit losses, the Company also considers various factors, including the aging of customer accounts and historical write-offs. In addition, the Company monitors other risk factors, including forward-looking information when establishing allowances for credit losses, which reflects the current estimate of credit losses expected to be incurred over the life of the receivables.

6. Income Taxes

The provision for income taxes for all periods presented is based on an estimated effective income tax rate for the respective fiscal years. The estimated annual effective income tax rate is determined excluding the effect of significant discrete items or items that are reported net of their related tax effects. The tax effect of significant discrete items is reflected in the period in which they occur. The Company's income tax expense is impacted by a number of factors, including the amount of taxable earnings derived in foreign jurisdictions with tax rates that are generally higher than the U.S. federal statutory rate, state tax rates in the jurisdictions where the Company does business and the Company's ability to utilize various tax credits, capital loss and net operating loss ("NOL") carryforwards.

The Company regularly reviews its deferred tax assets for recoverability and valuation allowances are established based on historical losses, projected future taxable income and the expected timing of the reversals of existing temporary differences, as deemed appropriate. In addition, all other available positive and negative evidence is taken into consideration for purposes of determining the proper balances of such valuation allowances. As a result of this review, the Company continues to maintain a full valuation allowance against U.S. federal and state capital loss carryforwards and a partial valuation allowance against certain foreign NOL carryforwards and other related foreign deferred tax assets, as well as certain U.S. state NOL carryforwards. Future changes to the balances of these valuation allowances, as a result of this continued review and analysis by the Company, could impact the financial statements for such period of change.

The income tax provision was $12.5 million for the three months ended September 30, 2023, compared to $ 1.6 million for the three months ended September 30, 2022. The effective income tax rate for the three months ended September 30, 2023 was 26.2% versus (9.1)% for the three months ended September 30, 2022. The effective income tax rate for the three months ended September 30, 2023 was above the U.S. federal statutory rate of 21% primarily due to the accrual of additional income taxes associated with compensation deduction limitations under Section 162(m) of the Internal Revenue Code, the accrual of various state income taxes and the accrual of foreign income taxes, which are generally above the U.S. federal statutory rate, partially offset by the recognition of income tax benefits associated with share-based payments. The income tax provision recognized on the loss from operations for the three months ended September 30, 2022 was primarily due to non-deductible transactions costs associated with the Merger, the accrual of additional income taxes associated with compensation deduction limitations under Section 162(m) of the Internal Revenue Code, the accrual of various state income taxes and the accrual of foreign income taxes, which are generally above the U.S. federal statutory rate, partially offset by the reduction in the valuation allowance associated with certain state NOL carryforwards.

The income tax provision was $34.8 million for the nine months ended September 30, 2023, compared to $ 22.9 million for the nine months ended September 30, 2022. The effective income tax rate for the nine months ended September 30, 2023 was 27.7% versus 32.9% for the nine months ended September 30, 2022. The effective income tax rate for the nine months ended September 30, 2023 was above the U.S. federal statutory rate of 21% primarily due to the accrual of additional income taxes associated with compensation deduction limitations under Section 162(m) of the Internal Revenue Code, the accrual of various state income taxes and the accrual of foreign income taxes, which are generally above the U.S. federal statutory rate, partially offset by the recognition of income tax benefits associated with share-based payments. The effective income tax rate for the nine months ended September 30, 2022 was above the U.S. federal statutory rate of 21% primarily due to non-deductible transactions costs associated with the Merger, the accrual of additional income taxes associated with compensation deduction limitations under Section 162(m) of the Internal Revenue Code, the accrual of various state income taxes and the accrual of foreign income taxes, which are generally above the U.S. federal statutory rate, partially offset by the recognition of income tax benefits associated with share-based payments and the reduction in the valuation allowance associated with certain state NOL carryforwards.

The Company's total liability for net unrecognized tax benefits as of September 30, 2023 and December 31, 2022 was $ 5.5 million. The Company recognizes accrued interest and penalties related to unrecognized income tax benefits in income tax expense. As of September 30, 2023 and December 31, 2022, the total amount of unrecognized tax benefits includes gross accrued interest and penalties of $1.0 million and $0.7 million, respectively. The Company recognized $0.3 million and $0.0 million of net interest and penalties as income tax expense during the nine months ended September 30, 2023 and September 30, 2022, respectively.

The Company conducts business in multiple locations within and outside the U.S. Consequently, the Company is subject to periodic income tax examinations by domestic and foreign income tax authorities. In accordance with the terms of the sale agreement relating to a group of certain previously owned legal entities (the parent of which was VAG Holding GbmH, "VAG"), the Company is required to indemnify the purchaser for any future income tax liabilities associated with all open tax years ending prior to, and including, the short period ended on the date of the Company's sale of VAG. VAG was notified by the German tax authorities of its intention to conduct an income tax examination of the VAG German entities' corporate income and trade tax returns for the tax years ended March 31, 2014 through 2020. Similarly, in accordance with the Spin-Off Transaction, the Company is required to indemnify Regal Rexnord Corporation for any future income tax liabilities associated with PMC entities relating to all open tax years ending prior to, and including, the short period ended on the date of the Spin-Off. There are currently a number of ongoing tax examinations being conducted by the applicable tax authorities in Germany with respect to certain PMC entities. It appears reasonably possible that the amounts of unrecognized income tax benefits and indemnification liabilities could change in the next twelve months upon conclusion of the current ongoing examinations; however, any potential payments of income tax, interest and penalties are not expected to be significant to the Company's consolidated financial statements. With certain exceptions, the Company is no longer subject to U.S. federal income tax examinations for tax years ending prior to March 31, 2020, state and local income tax examinations for years ending prior to March 31, 2019 or significant foreign income tax examinations for years ending prior to March 31, 2018.

7. Earnings per Share

Basic net income per share from continuing and discontinued operations is computed by dividing net income from continuing operations and income from discontinued operations, respectively, by the corresponding weighted average number of common shares outstanding for the period. Diluted net income per share from continuing and discontinued operations is computed based on the weighted average number of common shares outstanding, increased by the number of incremental shares that would have been outstanding if the potential dilutive shares were issued through the exercise of outstanding stock options to purchase common shares, except when the effect would be anti-dilutive.

The computation for diluted net income per share for the three and nine months ended September 30, 2023 excludes 0.3 million shares due to their anti-dilutive effects. The computation for diluted net income per share for the three and nine months ended September 30, 2022 excludes 2.3 million and 0.8 million shares due to their anti-dilutive effects, respectively.

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8. Stockholders' Equity

Stockholders' equity consists of the following (in millions):

	Common stock (1)	Additional paid-in capital	Retained deficit	Accumulated other comprehensive loss	Total stockholders' equity
Balance at December 31, 2021	$ 1.3	$ 1,436.9	$ (1,236.9)	$ (74.9)	$ 126.4
Total comprehensive income	—	—	30.2	2.0	32.2
Stock-based compensation expense	—	3.9	—	—	3.9
Proceeds from exercise of stock options	—	0.5	—	—	0.5
Taxes withheld and paid on employees' share-based payment awards	—	(0.5)	—	—	(0.5)
Proceeds associated with divestiture of discontinued operations	—	—	35.0	—	35.0
Common stock dividends ($0.03 per share)	—	(3.8)	—	—	(3.8)
Balance at March 31, 2022	$ 1.3	$ 1,437.0	$ (1,171.7)	$ (72.9)	$ 193.7
Total comprehensive income (loss)	—	—	36.4	(2.0)	34.4
Stock-based compensation expense	—	3.8	—	—	3.8
Proceeds from exercise of stock options	—	1.3	—	—	1.3
Common stock dividends ($0.03 per share)	—	(3.8)	—	—	(3.8)
Balance at June 30, 2022	$ 1.3	$ 1,438.3	$ (1,135.3)	$ (74.9)	$ 229.4
Total comprehensive loss	—	—	(19.1)	(4.1)	(23.2)
Stock-based compensation expense	—	7.8	—	—	7.8
Proceeds from exercise of stock options	—	0.1	—	—	0.1
Elkay Merger (2)	0.5	1,416.5	—	—	1,417.0
Common stock dividends ($0.07 per share)	—	(12.5)	—	—	(12.5)
Balance at September 30, 2022	$ 1.8	$ 2,850.2	$ (1,154.4)	$ (79.0)	$ 1,618.6

	Common stock (1)	Additional paid-in capital	Retained deficit	Accumulated other comprehensive loss	Total stockholders' equity
Balance at December 31, 2022	$ 1.8	$ 2,853.1	$ (1,164.9)	$ (75.0)	$ 1,615.0
Total comprehensive income (loss)	—	—	22.8	(0.1)	22.7
Stock-based compensation expense	—	11.2	—	—	11.2
Proceeds from exercise of stock options	—	0.6	—	—	0.6
Elkay Merger (2)	—	(5.1)	—	—	(5.1)
Common stock issued to fund defined contribution plans	—	0.8	—	—	0.8
Repurchase of common stock	—	—	(37.0)	—	(37.0)
Common stock dividends ($0.07 per share)	—	(8.7)	—	—	(8.7)
Balance at March 31, 2023	$ 1.8	$ 2,851.9	$ (1,179.1)	$ (75.1)	$ 1,599.5
Total comprehensive income	—	—	34.6	3.6	38.2
Stock-based compensation expense	—	10.2	—	—	10.2
Proceeds from exercise of stock options	—	0.6	—	—	0.6
Repurchase of common stock	(0.1)	—	(50.8)	—	(50.9)
Common stock dividends ($0.07 per share)	—	(9.0)	—	—	(9.0)
Balance at June 30, 2023	$ 1.7	$ 2,853.7	$ (1,195.3)	$ (71.5)	$ 1,588.6
Total comprehensive income (loss)	—	—	41.4	(2.1)	39.3
Stock-based compensation expense	—	10.0	—	—	10.0
Proceeds from exercise of stock options	—	0.7	—	—	0.7
Taxes withheld and paid on employees' share-based payment awards	—	(1.9)	—	—	(1.9)
Repurchase of common stock	—	—	(13.0)	—	(13.0)
Common stock dividends ($0.07 per share)	—	(12.1)	—	—	(12.1)
Balance at September 30, 2023	$ 1.7	$ 2,850.4	$ (1,166.9)	$ (73.6)	$ 1,611.6

(1) During the three and nine months ended September 30, 2023, the Company issued135,502 and 462,738 shares of common stock, respectively, upon the exercise of stock options, vesting of restricted stock units, and for other common stock issuances. During the three and nine months ended September 30, 2022, the Company issued 51,577,307 and 52,039,485 shares of common stock, respectively, upon the exercise of stock options, vesting of restricted stock units, the Elkay Merger, and for other common stock issuances.

(2) During the nine months ended September 30, 2023, 186,020 of the shares issued at closing of the Elkay Merger were returned to the Company as a result of lower working capital and cash balances at closing compared to targets stipulated in the Merger Agreement. The shares returned to the Company were canceled upon receipt. Refer to Note 2, Acquisition for additional information.

Share Repurchase Program

During fiscal 2015, the Company's Board of Directors approved a common stock repurchase program (the "Repurchase Program") authorizing the repurchase of up to $200.0 million of the Company's common stock from time to time on the open market or in privately negotiated transactions. On January 27, 2020, the Company's Board of Directors approved increasing the remaining share repurchase authority under the Repurchase Program to $300.0 million. On February 8, 2023, the Company's Board of Directors approved increasing the remaining share repurchase authority under the Repurchase Program to $500.0 million. The Repurchase Program does not require the Company to acquire any particular amount of common stock and does not specify the timing of purchases or the prices to be paid; however, the program will continue until the maximum amount of dollars authorized have been expended or until it is modified or terminated by the Board of Directors. During the three months ended September 30, 2023, the Company repurchased 444,606 shares of common stock at a total cost of $ 13.0 million at a weighted average price of $ 29.24 per share. During the nine months ended September 30, 2023, the Company repurchased 4,434,475 shares of common stock at a total cost of $ 100.1 million at a weighted average price of $22.55 per share. The repurchased shares were canceled by the Company upon receipt. During the three and nine months ended September 30, 2022, the Company did not repurchase any shares of common stock. Approximately $ 415.5 million of the existing authority remained under the Repurchase Program at September 30, 2023.

9. Accumulated Other Comprehensive Loss

The changes in accumulated other comprehensive loss, net of tax, for the nine months ended September 30, 2023, are as follows (in millions):

	Foreign Currency Translation and Other	Pension and Postretirement Plans	Total
Balance at December 31, 2022	$ (75.1)	$ 0.1	$ (75.0)
Other comprehensive income before reclassifications	1.4	—	1.4
Net current period other comprehensive income	1.4	—	1.4
Balance at September 30, 2023	$ (73.7)	$ 0.1	$ (73.6)

There were no amounts reclassified from accumulated other comprehensive loss to net income during the three and nine months ended September 30, 2023 and 2022.

10. Inventories

The major classes of inventories are summarized as follows (in millions):

	September 30, 2023	December 31, 2022
Finished goods	$ 221.4	$ 285.9
Work in progress	14.0	19.1
Raw materials	51.0	75.7
Inventories at First-in, First-Out ("FIFO") cost	286.4	380.7
Adjustment to state inventories at Last-in, First-Out ("LIFO") cost	(2.1)	(14.0)
	$ 284.3	$ 366.7

11. Goodwill and Intangible Assets

The changes in the net carrying value of goodwill for the nine months ended September 30, 2023, are presented below (in millions):

Net carrying amount as of December 31, 2022	$	777.0
Currency translation adjustments		(0.7)
Purchase accounting adjustments (1)		19.0
Net carrying amount as of September 30, 2023	$	795.3

(1) Refer to Note 2, Acquisition for additional information regarding the acquisition.

The gross carrying amount and accumulated amortization for each major class of identifiable intangible assets as of September 30, 2023 and December 31, 2022 are as follows (in millions):

		September 30, 2023		
	Weighted Average Useful Life	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Intangible assets subject to amortization:				
Patents	9 years	$ 25.9	$ (22.7)	$ 3.2
Customer relationships (including distribution network)	16 years	1,069.6	(336.0)	733.6
Tradenames	19 years	156.8	(14.6)	142.2
Intangible assets not subject to amortization - trademarks and tradenames		87.0	—	87.0
Total intangible assets, net	16 years	$ 1,339.3	$ (373.3)	$ 966.0

		December 31, 2022		
	Weighted Average Useful Life	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Intangible assets subject to amortization:				
Patents	9 years	$ 25.5	$ (22.5)	$ 3.0
Customer relationships (including distribution network)	16 years	1,069.5	(298.2)	771.3
Tradenames	19 years	156.8	(8.5)	148.3
Intangible assets not subject to amortization - trademarks and tradenames		87.1	—	87.1
Total intangible assets, net	16 years	$ 1,338.9	$ (329.2)	$ 1,009.7

Intangible asset amortization expense totaled $14.7 million and $14.5 million for the three months ended September 30, 2023 and September 30, 2022, respectively. Intangible asset amortization expense totaled $44.0 million and $19.1 million for the nine months ended September 30, 2023 and September 30, 2022, respectively.

The Company expects to recognize amortization expense on the intangible assets subject to amortization of $ 58.7 million in the year ending December 31, 2023 (inclusive of the $44.0 million of amortization expense recognized in the nine months ended September 30, 2023), $ 58.7 million in 2024, $58.7 million in 2025, $58.5 million in 2026, $58.5 million in 2027 and $ 58.5 million in 2028.

12. Other Current Liabilities

Other current liabilities are summarized as follows (in millions):

	September 30, 2023	December 31, 2022
Commissions	$ 11.3	$ 9.0
Current portion of operating lease liability	10.4	9.4
Income taxes payable	3.2	2.3
Legal and environmental	0.9	2.3
Product warranty (1)	4.6	4.2
Restructuring and other similar charges (2)	2.2	8.4
Risk management (3)	16.0	16.3
Sales rebates	64.5	56.0
Tax indemnities	13.4	19.0
Taxes, other than income taxes	3.6	2.5
Other	6.0	16.5
	$ 136.1	$ 145.9

(1) See more information related to the product warranty obligations within Note 15, Commitments and Contingencies.

(2) See more information related to the restructuring obligations within Note 3, Restructuring and Other Similar Charges.

(3) Includes projected liabilities related to losses arising from automobile, general and product liability claims.

13. Long-Term Debt

Long-term debt is summarized as follows (in millions):

	September 30, 2023	December 31, 2022
Term loan (1)	$ 532.4	$ 535.3
Finance leases	21.8	0.6
Total	554.2	535.9
Less current maturities	6.3	5.7
Long-term debt	$ 547.9	$ 530.2

(1) Includes unamortized debt issuance costs of $8.0 million and $9.2 million at September 30, 2023 and December 31, 2022, respectively.

Senior Secured Credit Facility

On October 4, 2021, ZBS Global, Inc. (“Holdings”), Zurn Holdings, Inc., Zurn LLC (together, the “Original Borrowers”), the lenders from time to time party thereto, and Credit Suisse AG, Cayman Islands Branch, as administrative agent for the lenders (in such capacity, the “Administrative Agent”) entered into a Fourth Amended and Restated First Lien Credit Agreement, which was amended by that certain Amendment No. 1 to Fourth Amended and Restated First Lien Credit Agreement dated as of July 1, 2022 (the "2022 Amendment") (as so amended, the “Credit Agreement”). Pursuant to the 2022 Amendment, Elkay joined the Credit Agreement as a borrower (Elkay and the Original Borrowers, collectively, the "Borrowers"). The Credit Agreement is funded by a syndicate of banks and other financial institutions and provides for (i) a $550.0 million term loan facility (the “Term Loan”) and (ii) a $200.0 million revolving credit facility (the “Revolving Credit Facility”).

The obligations under the Credit Agreement and related documents are secured by liens on substantially all of the assets of Holdings, the Borrowers, and certain subsidiaries of the Borrowers pursuant to a Third Amended and Restated Guarantee and Collateral Agreement, dated as of October 4, 2021, among Holdings, the Borrowers, the subsidiaries of the Borrowers party thereto, and the Administrative Agent, as supplemented pursuant to that certain Supplement No. 1 dated as of July 1, 2022, executed by Elkay and its domestic subsidiaries, and certain other collateral documents.

The Credit Agreement contains representations, warranties, covenants and events of default, including, without limitation, a financial covenant under which the Borrowers are, if certain conditions are met, obligated to maintain on a consolidated basis, as of the end of each fiscal quarter, a certain maximum Net First Lien Leverage Ratio (as defined in the

Credit Agreement). As of September 30, 2023, the Borrowers were in compliance with all applicable covenants under the Credit Agreement.

Term Debt

The Credit Agreement provides for the issuance of a term loan facility in an aggregate principal amount of $ 550.0 million. The proceeds of the Term Loan were, together with the dividend received by the Company in connection with the Spin-Off Transaction and cash on hand, used to (i) repay in full a $625 million term loan, together with accrued interest thereon, (ii) redeem the $ 500 million of outstanding principal amount of the 4.875% notes, and (iii) pay related fees and expenses.

The Term Loan has a maturity date of October 4, 2028. The Borrowers are required to make quarterly payments of principal in an amount equal to $1.4 million each quarter until the maturity date.

For purposes of the Term Loan, effective July 1, 2023, the secured overnight financing rate ("SOFR") replaced LIBOR, and accordingly, beginning July 1, 2023 the Term Loan bears interest at the Borrowers' option, by reference to a base rate or a rate based on Term SOFR, plus a Term SOFR adjustment of 0.115%, 0.262%, or 0.428% for interest periods of one month, three months, and six months, respectively, plus an applicable margin based on the Borrowers' Net First Lien Leverage Ratio as of the last day of each fiscal quarter. If the Net First Lien Leverage Ratio is greater than 1.80 to 1.00, the applicable margin shall equal 1.25% in the case of base rate borrowings and 2.25% in the case of SOFR borrowings. In the event the Borrowers' Net First Lien Leverage Ratio is less than or equal to 1.80 to 1.00, the applicable margin on both base rate and SOFR borrowings would decrease by 0.25%. The Borrowers' Net First Lien Leverage Ratio was 1.26 to 1.00 as of September 30, 2023, and therefore the applicable margin is 2.00%.

Prior to July 1, 2023, the Term Loan bore interest at the Borrowers' option, by reference to a base rate or a rate based on LIBOR, in either case plus an applicable margin determined quarterly based on the Borrowers' Net First Lien Leverage Ratio as of the last day of each fiscal quarter as illustrated above.

At September 30, 2023 and for the nine months then ended, the borrowings under the Term Loan had weighted-average effective interest rates of 7.43% and 6.97%, respectively.

On October 11, 2023 the Company made a voluntary principal repayment of the Term Loan in the amount of $ 60.0 million.

Revolving Credit Facility

The Credit Agreement includes a $ 200.0 million revolving credit facility that has a maturity date of October 2, 2026. Similar to the Term Loan, effective July 1, 2023, the SOFR replaced LIBOR, and accordingly, beginning July 1, 2023 the Revolving Credit Facility bears interest by reference to a base rate or a rate based on Term SOFR, plus a Term SOFR adjustment of 0.115%, 0.262%, or 0.428% for interest periods of one month, three months, and six months, respectively, plus an applicable margin based on the Borrowers' Net First Lien Leverage Ratio as of the last day of each fiscal quarter. If the Net First Lien Leverage Ratio is greater than 2.00 to 1.00, the applicable margin shall equal 1.00% in the case of base rate borrowings and 2.00% in the case of SOFR borrowings. In the event the Borrowers' Net First Lien Leverage Ratio is less than or equal to 2.00 to 1.00, the applicable margin on both base rate and SOFR borrowings would decrease by 0.25%. The Borrowers' Net First Lien Leverage Ratio was 1.26 to 1.00 as of September 30, 2023. The Borrowers are also required to pay a quarterly commitment fee on the average daily unused portion of the Revolving Credit Facility for each fiscal quarter and fees in connection with the issuance of letters of credit. If the Net First Lien Leverage Ratio is greater than 2.00 to 1.00, the commitment fee shall equal 0.50%, and if the Company's Net First Lien Leverage Ratio is less than or equal to 2.00 to 1.00, the commitment fee shall equal 0.375%.

Prior to July 1, 2023, borrowings under the Revolving Credit Facility bore interest at the Borrowers' option, by reference to a base rate or a rate based on LIBOR, in either case, plus an applicable margin determined quarterly based on the Borrowers' Net First Lien Leverage Ratio as of the last day of each fiscal quarter as illustrated above.

At September 30, 2023 and December 31, 2022, there were no amounts borrowed under the Revolving Credit Facility. As of September 30, 2023 and December 31, 2022, $5.8 million and $7.5 million of the Revolving Credit Facility was considered utilized in connection with outstanding letters of credit, respectively.

Finance Leases

At September 30, 2023 and December 31, 2022, the Company had finance lease obligations of $ 21.8 million and $0.6 million, respectively.

14. Fair Value Measurements

ASC 820 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants. ASC 820 also specifies a fair value hierarchy based upon the observability of inputs used in valuation techniques. Observable inputs (highest level) reflect market data obtained from independent sources, while unobservable inputs (lowest level) reflect internally developed assumptions about the assumptions a market participant would use.

In accordance with ASC 820, fair value measurements are classified under the following hierarchy:

- Level 1 - Quoted prices for identical instruments in active markets.
- Level 2 - Quoted prices for similar instruments; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs or significant value-drivers are observable.
- Level 3 - Model-derived valuations in which one or more inputs or value-drivers are both significant to the fair value measurement and unobservable.

If applicable, the Company uses quoted market prices in active markets to determine fair value, and therefore classifies such measurements within Level 1. In some cases where market prices are not available, the Company makes use of observable market-based inputs to calculate fair value, in which case the measurements are classified within Level 2. If quoted or observable market prices are not available, fair value is based upon internally developed models that use, where possible, current market-based parameters. These measurements are classified within Level 3 if they use significant unobservable inputs.

Fair Value of Financial Instruments

The Company has a nonqualified deferred compensation plan where assets are invested in mutual funds and corporate-owned life insurance contracts held in a Rabbi Trust, which is restricted for payments to participants of the plan. The Company has elected to use the fair value option for the mutual funds, which are measured using quoted prices of identical instruments in active markets categorized as Level 1. Corporate-owned life insurance contracts are recorded at cash surrender value, which is provided by a third party and reflects the net asset value of the underlying publicly traded mutual funds categorized as Level 2. The deferred compensation plan assets are classified within other assets on the condensed consolidated balance sheets. Deferred compensation plan liabilities are measured at fair value based on quoted prices of identical instruments to the investment vehicles selected by the participants categorized as Level 1. Deferred compensation plan liabilities are classified within other liabilities on the condensed consolidated balance sheets.

The following table provides a summary of the Company's assets and liabilities that were recognized at fair value on a recurring basis as of September 30, 2023 and December 31, 2022 (in millions):

	Fair Value as of September 30, 2023			
	Level 1	Level 2	Level 3	Total
Deferred compensation plan assets	$ 0.1	$ 12.1	$ —	$ 12.2
Deferred compensation plan liabilities	13.3	—	—	13.3
	Fair Value as of December 31, 2022			
	Level 1	Level 2	Level 3	Total
Deferred compensation plan assets	$ 0.2	$ 11.3	$ —	$ 11.5
Deferred compensation plan liabilities	12.1	—	—	12.1

There were no transfers of assets between levels at September 30, 2023 and December 31, 2022, respectively.

Fair Value of Non-Derivative Financial Instruments

The carrying amounts of cash, receivables, payables and accrued liabilities approximated fair value at September 30, 2023 and December 31, 2022, due to the short-term nature of those instruments. The fair value of long-term debt as of September 30, 2023 and December 31, 2022, was approximately $562.2 million and $543.1 million, respectively. The fair value is based on quoted market prices for the same instruments.

15. Commitments and Contingencies

Warranties:

The Company offers warranties on the sales of certain of its products and records an accrual for estimated future claims. Such accruals are based upon historical experience and management's estimate of the level of future claims. The following table presents changes in the Company's product warranty liability (in millions):

	Nine Months Ended	
	September 30, 2023	September 30, 2022
Balance at beginning of period	$ 4.2	$ 1.3
Acquired obligations	—	3.4
Charged to operations	2.0	2.8
Claims settled	(1.6)	(2.0)
Balance at end of period	$ 4.6	$ 5.5

Contingencies:

The Company's subsidiaries are involved in various unresolved legal actions, administrative proceedings and claims in the ordinary course of business involving, among other things, product liability, commercial, employment, workers' compensation, intellectual property claims and environmental matters. The Company establishes accruals in a manner that is consistent with accounting principles generally accepted in the United States for costs associated with such matters when liability is probable and those costs are capable of being reasonably estimated. Although it is not possible to predict with certainty the outcome of these unresolved legal actions or the range of possible loss or recovery, based upon current information, management believes the eventual outcome of these unresolved legal actions, either individually or in the aggregate, will not have a material adverse effect on the financial position, results of operations or cash flows of the Company.

Certain Company subsidiaries are subject to asbestos litigation. As of September 30, 2023, Zurn and numerous other unrelated companies were defendants in approximately 6,000 asbestos related lawsuits representing approximately 7,500 claims. Plaintiffs' claims allege personal injuries caused by exposure to asbestos used primarily in industrial boilers formerly manufactured by a segment of Zurn. Zurn did not manufacture asbestos or asbestos components. Instead, Zurn purchased them from suppliers. These claims are being handled pursuant to a defense strategy funded by insurers.

As of September 30, 2023, the Company estimates the potential liability for the asbestos-related claims described above, as well as the claims expected to be filed in the next ten years, to be approximately $79.0 million, of which Zurn expects approximately $ 58.0 million to be paid in the next ten years on such claims, with the balance of the estimated liability being paid in subsequent years. The $ 79.0 million was developed based on actuarial studies and represents the projected indemnity payout for current and future claims. There are inherent uncertainties involved in estimating the number of future asbestos claims, future settlement costs, and the effectiveness of defense strategies and settlement initiatives. As a result, actual liability could differ from the estimate described herein and could be substantial. The liability for the asbestos-related claims is recorded in reserve for asbestos claims within the condensed consolidated balance sheets.

Management estimates that the available insurance to cover this ten year estimated potential asbestos liability as of September 30, 2023 is $72.1 million.

The Company recorded a receivable from its insurance carriers, which corresponds to the amount of this potential asbestos liability that is covered by available insurance and is currently determined to be probable of recovery. However, there is no assurance the Company's current insurance coverage will ultimately be available or that this asbestos liability will not ultimately exceed the Company's coverage limits. Factors that could cause a decrease in the amount of available coverage or create gaps in coverage include: changes in law governing the policies, potential disputes and settlements with the carriers regarding the scope of coverage, and insolvencies of one or more of the Company's carriers. The receivable for probable asbestos-related recoveries is recorded in insurance for asbestos claims within the condensed consolidated balance sheets.

16. Retirement Benefits

The components of net periodic (benefit) cost are as follows (in millions):

	Three Months Ended		Nine Months Ended	
	September 30, 2023	September 30, 2022	September 30, 2023	September 30, 2022
Pension Benefits:				
Interest cost	$ 3.0	$ 2.1	$ 9.0	$ 6.4
Expected return on plan assets	(1.9)	(2.4)	(5.6)	(7.2)
Net periodic cost (benefit)	$ 1.1	$ (0.3)	$ 3.4	$ (0.8)
Other Postretirement Benefits:				
Interest cost	$ 0.2	$ 0.1	$ 0.5	$ 0.2
Net periodic cost	$ 0.2	$ 0.1	$ 0.5	$ 0.2

The service cost component of net periodic benefits is presented within Cost of sales and Selling, general and administrative expenses in the condensed consolidated statements of operations, while the other components of net periodic cost (benefit) are presented within Other income (expense), net. The Company recognizes the net actuarial gains or losses in excess of the corridor in operating results during the final quarter of each fiscal year (or upon any required re-measurement event).

During the nine months ended September 30, 2023 and September 30, 2022, the Company made contributions of $ 0.2 million and $1.0 million, respectively, to its U.S. qualified pension plan trusts.

See Note 16, Retirement Benefits, to the audited consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2022 for further information regarding retirement benefits.

17. Stock-Based Compensation

The Zurn Elkay Water Solutions Corporation Performance Incentive Plan (the "Plan") is utilized to provide performance incentives to the Company's officers, employees, directors and certain others by permitting grants of equity awards (for common stock), as well as performance-based cash awards, to such persons to encourage them to maximize the Company's performance and create value for the Company's stockholders. For the three months ended September 30, 2023 and September 30, 2022, the Company recognized $10.0 million and $7.8 million of stock-based compensation expense, respectively. For the nine months ended September 30, 2023 and September 30, 2022, the Company recognized $30.5 million and $15.5 million of stock-based compensation expense, respectively.

During the nine months ended September 30, 2023, the Company granted the following stock options, restricted stock units, performance stock units and common stock to directors, executive officers, and certain other employees:

Award Type	Number of Awards	Weighted Average Grant-Date Fair Value
Stock options	125,283	$ 8.25
Restricted stock units	306,081	$ 23.30
Performance stock units	425,246	$ 23.25
Common stock	171,089	$ 24.25

See Note 15, Stock-Based Compensation, to the audited consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2022, for further information regarding stock-based compensation.

18. Subsequent Events

On October 19, 2023, the Company's Board of Directors declared a quarterly cash dividend on the Company's common stock of $ 0.08 per-share to be paid on December 7, 2023, to stockholders of record as of November 20, 2023.

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

General

On July 1, 2022, we completed our combination with Elkay Manufacturing Company (“Elkay”) through the Merger of Elkay with and into a newly created subsidiary of Zurn, with Elkay surviving as a wholly owned subsidiary of Zurn Elkay (the “Merger” or "Elkay Transaction"). In conjunction with the Merger, we changed our name from Zurn Water Solutions Corporation to Zurn Elkay Water Solutions Corporation. Our results of operations include the acquired operations subsequent to July 1, 2022. See Item 1, Note 2, Acquisition, for additional information on the Elkay Merger.

Zurn Elkay Water Solutions Corporation is a growth-oriented, pure-play water management business that designs, procures, manufactures, and markets what we believe to be the broadest sustainable product portfolio of specification-driven water management solutions to improve health, human safety and the environment. Our product portfolio includes professional grade water safety and control products, flow system products, hygienic and environmental products, and drinking water products for public and private spaces that deliver superior value to building owners, positively impact the environment and human hygiene and reduce product installation time. Our heritage of innovation and specification has allowed us to provide highly-engineered, mission-critical solutions to customers for decades and affords us the privilege of having long-term, valued relationships with market leaders. We operate in a disciplined way and the Zurn Elkay Business System (“ZEBS”) is our operating philosophy. Grounded in the spirit of continuous improvement, ZEBS creates a scalable, process-based framework that focuses on driving superior customer satisfaction and financial results by targeting world-class operating performance throughout all aspects of our business.

The following information should be read in conjunction with the audited consolidated financial statements and notes thereto, along with Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations (“MD&A”), in our Annual Report on Form 10-K for the year ended December 31, 2022.

Critical Accounting Policies and Estimates

The condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP"), which require us to make estimates and assumptions that affect the reported amounts of assets and liabilities on the date of the financial statements and revenues and expenses during the periods reported. Actual results could differ from those estimates. Refer to Item 7, MD&A, of our Annual Report on Form 10-K for the year ended December 31, 2022 for information with respect to our critical accounting policies which we believe could have the most significant effect on our reported results and require subjective or complex judgments by management. Except for the items reported below, management believes that as of September 30, 2023, and during the period from January 1, 2023 through September 30, 2023, there has been no material change to this information.

Recent Accounting Pronouncements

See Item 1, Note 1, Basis of Presentation and Significant Accounting Policies regarding recent accounting pronouncements.

Acquisitions

On July 1, 2022, we completed the Elkay Merger for a purchase price of $1,457.8 million. Elkay, a market leader of drinking water solutions and commercial sinks, complements our existing product portfolio. The purchase price includes $1,411.9 million of Zurn's common stock based on Zurn's closing stock price of $27.48 on July 1, 2022, and $45.9 million of net cash payments for the repayment of Elkay's term loan and Elkay's transaction related costs outstanding that were in excess of Elkay's cash and cash equivalents at the time of closing. Pursuant to the terms of the merger agreement, we issued 51,564,524 shares of common stock, which represented approximately 29% of outstanding shares immediately following the Merger. During the six months ended June 30, 2023, we completed the final price adjustments and the adjusted purchase price is reflected in the purchase price amounts above, following the return of 186,020 of the shares we issued at closing as a result of lower working capital and cash balances at closing compared to targets stipulated in the merger agreement. The shares returned were canceled upon receipt. As of June 30, 2023, the measurement period was complete. Our results of operations include Elkay subsequent to the Merger date. See Item 1, Note 2, Acquisition for additional information on the Elkay Merger.

Spin-Off of Process & Motion Control Segment

On October 4, 2021, we completed a Reverse Morris Trust tax-free spin-off transaction (the “Spin-off Transaction”) in which (i) substantially all the assets and liabilities of our Process & Motion Control ("PMC") business were transferred to a newly created subsidiary, Land Newco, Inc. (“Land”), (ii) the shares of Land were distributed to our stockholders pro rata, and (iii) Land was merged with a subsidiary of Regal Rexnord Corporation (formerly known as Regal Beloit Corporation), in which the stock of Land was converted into a specified number of shares of Regal Rexnord Corporation. During 2022, we received $35.0 million from Regal Rexnord Corporation as a result of the final working capital and cash balances at closing exceeding the targets stipulated in the Spin-Off Transaction agreement.

The operating results of PMC are reported as discontinued operations in our condensed consolidated statements of operations for all periods presented. The condensed consolidated statements of cash flows for the period ended September 30, 2023 have not been adjusted to separately disclose cash flows related to the discontinued operations.

The major components of the Income from discontinued operations, net of tax presented in the condensed consolidated statements of operations for the three and nine months ended September 30, 2023 and September 30, 2022, are as follows (in millions):

	Three Months Ended		Nine Months Ended	
	September 30, 2023	**September 30, 2022**	**September 30, 2023**	**September 30, 2022**
Selling, general and administrative expenses (1)	$ 6.6	$ —	$ 8.4	$ —
Income from discontinued operations before income tax	6.6	—	8.4	—
Income tax (expense) benefit	(0.4)	—	(0.3)	0.8
Income from discontinued operations, net of tax	$ 6.2	$ —	$ 8.1	$ 0.8

(1) Selling, general and administrative expenses include the reversal of certain accruals as a result of costs the Company will no longer incur related to the Spin-Off Transaction.

See Item 1, Note 4, Discontinued Operations for additional information.

Restructuring and Other Similar Costs

During the three and nine months ended September 30, 2023, the Company continued to execute various restructuring actions. These initiatives were implemented to drive efficiencies and reduce operating costs while also modifying the Company's footprint to reflect changes in the markets it serves, the impact of acquisitions, including Elkay, on the Company's overall manufacturing capacity and the refinement of its overall product portfolio. These restructuring actions primarily resulted in workforce reductions, lease termination costs and other facility rationalization costs. Management expects to continue executing similar initiatives to optimize its operating margin and manufacturing footprint. As such, the Company expects further expenses related to workforce reductions, potential impairment or accelerated depreciation of assets, lease termination costs and other facility rationalization costs. For the three and nine months ended September 30, 2023, restructuring charges totaled $2.2 million and $11.9 million, respectively. For the three and nine months ended September 30, 2022, restructuring charges totaled $11.7 million and $13.1 million, respectively. Refer to Item 1, Note 3, Restructuring and Other Similar Charges for further information.

Results of Operations

Three Months Ended September 30, 2023 compared with the Three Months Ended September 30, 2022:

Net sales

(Dollars in Millions)

	Three Months Ended			
	September 30, 2023	September 30, 2022	Change	% Change
Net Sales	$ 398.4	$ 417.7	$ (19.3)	(4.6) %

Net sales were $398.4 million and $417.7 million during the three months ended September 30, 2023 and September 30, 2022, respectively, a decrease of 5% year-over-year. Core sales decreased 5% year over year as a result of lower year-over-year demand associated with products sold into our residential end markets, the planned exit of certain residential sink products as well as timing of shipments in the prior year as we continued working down an elevated backlog during the three months ended September 30, 2022.

Income (loss) from operations

(Dollars in Millions)

	Three Months Ended			
	September 30, 2023	September 30, 2022	Change	% Change
Income (loss) from operations	$ 60.1	$ (10.1)	$ 70.2	(695.0)%
% of net sales	*15.1 %*	*(2.4) %*	*17.5 %*	

During the three months ended September 30, 2023, income from operations was $60.1 million compared to a loss of $10.1 million during the three months ended September 30, 2022. Income from operations as a percentage of net sales increased by 1750 basis points year over year due to the benefits resulting from productivity synergies and restructuring actions related to the Elkay Merger, lower material and transportation costs, and lower restructuring charges. Additionally, income from operations for the three months ended September 30, 2022 included merger costs of $33.7 million and a purchase accounting fair value adjustment of $14.6 million related to the Elkay Merger.

Interest expense, net

Interest expense, net was $9.9 million for the three months ended September 30, 2023, compared to $8.0 million for the three months ended September 30, 2022. The increase in interest expense as compared to the prior year period is primarily a result of higher year-over-year interest rates. See Item 1, Note 13 Long-Term Debt for more information.

Other income (expense), net

Other expense, net for the three months ended September 30, 2023, was $2.5 million compared to other income of $0.6 million for the three months ended September 30, 2022. Other income (expense), net consists primarily of foreign currency transaction gains and losses, the non-service cost components associated with our defined benefit plans and other non-operational gains and losses. The year-over-year change is primarily driven by higher interest cost within the non-service cost components of our defined benefit plans.

Provision for income taxes

The income tax provision was $12.5 million for the three months ended September 30, 2023, compared to $1.6 million for the three months ended September 30, 2022. The effective income tax rate for the three months ended September 30, 2023 was 26.2% versus (9.1)% for the three months ended September 30, 2022. The effective income tax rate for the three months ended September 30, 2023 was above the U.S. federal statutory rate of 21% primarily due to the accrual of additional income taxes associated with compensation deduction limitations under Section 162(m) of the Internal Revenue Code, the accrual of various state income taxes and the accrual of foreign income taxes, which are generally above the U.S. federal statutory rate, partially offset by the recognition of income tax benefits associated with share-based payments. The income tax provision recognized on the loss from operations for the three months ended September 30, 2022 was primarily due to non-deductible transactions costs associated with the Merger, the accrual of additional income taxes associated with compensation deduction limitations under Section 162(m) of the Internal Revenue Code, the accrual of various state income taxes and the accrual of foreign income taxes, which are generally above the U.S. federal statutory rate, partially offset by the reduction in the valuation allowance associated with certain state NOL carryforwards.

On a quarterly basis, we review and analyze our valuation allowances associated with deferred tax assets relating to certain foreign and state net operating loss carryforwards as well as U.S. federal and state capital loss carryforwards. In conjunction with this analysis, we weigh both positive and negative evidence for purposes of determining the proper balances of such valuation allowances. Future changes to the balances of these valuation allowances, as a result of our continued review and analysis, could impact the financial statements for such period of change.

Net income (loss)

Net income for the three months ended September 30, 2023, was $41.4 million compared to a net loss of $19.1 million for the three months ended September 30, 2022. Diluted net income (loss) per share for the three months ended September 30, 2023 and September 30, 2022, was $0.24 and $(0.11), respectively. The year-over-year change is the result of the factors described above. Net income from discontinued operations, net of tax, was $6.2 million for the three months ended September 30, 2023 compared to $0.0 million for the three months ended September 30, 2022. Diluted net income per share from discontinued operations for the three months ended September 30, 2023 and September 30, 2022, was $0.04 and $0.00, respectively.

Nine Months Ended September 30, 2023 compared with the Nine Months Ended September 30, 2022:

Net sales

(Dollars in Millions)

	Nine Months Ended			
	September 30, 2023	September 30, 2022	Change	% Change
Net Sales	$ 1,173.7	$ 941.5	$ 232.2	24.7 %

Net sales were $1,173.7 million during the nine months ended September 30, 2023, an increase of 25% year-over-year. Excluding a 28% increase in sales associated with our combination with Elkay, core sales decreased 3% year over year as a result of lower year-over-year demand associated with products sold into our residential end markets, the planned exit of certain residential sink products as well as timing of shipments in the prior year as we continued working down an elevated backlog during the second and third quarter of 2022.

Income from operations

(Dollars in Millions)

	Nine Months Ended			
	September 30, 2023	September 30, 2022	Change	% Change
Income from operations	158.6	87.3	71.3	81.7 %
% of net sales	*13.5 %*	*9.3 %*	*4.2 %*	

Income from operations during the nine months ended September 30, 2023 was $158.6 million compared to $87.3 million during the nine months ended September 30, 2022. Income from operations as a percentage of net sales increased by 420 basis points year over year due to the benefits of productivity synergies and restructuring actions, partially offset by higher non-cash stock-based compensation expense, and incremental depreciation and intangible asset amortization resulting from the Elkay Merger during the nine months ended September 30, 2023. Additionally, income from operations for the nine months ended September 30, 2022 included merger costs of $33.7 million and a purchase accounting fair value adjustment of $14.6 million related to the Elkay Merger.

Interest expense, net

Interest expense, net was $29.8 million during the nine months ended September 30, 2023, compared to $18.0 million during the nine months ended September 30, 2022. The increase in interest expense as compared to the prior year period is primarily a result of higher year-over-year interest rates. See Item 1, Note 13 Long-Term Debt for more information.

Other income (expense), net

Other expense, net during the nine months ended September 30, 2023 was $3.3 million compared to other income of $0.3 million during the nine months ended September 30, 2022. Other income (expense), net consists primarily of foreign currency transaction gains and losses, the non-service cost components associated with our defined benefit plans and other non-operational gains and losses. The year-over-year change is primarily driven by higher interest cost within the non-service cost components of our defined benefit plans and accruals for estimated environmental remediation costs, partially offset by income recognized in connection with an insurance settlement.

Provision for income taxes

The income tax provision was $34.8 million for the nine months ended September 30, 2023, compared to $22.9 million for the nine months ended September 30, 2022. The effective income tax rate for the nine months ended September 30, 2023 was 27.7% versus 32.9% for the nine months ended September 30, 2022. The effective income tax rate for the nine months ended September 30, 2023 was above the U.S. federal statutory rate of 21% primarily due to the accrual of additional income taxes associated with compensation deduction limitations under Section 162(m) of the Internal Revenue Code, the accrual of various state income taxes and the accrual of foreign income taxes, which are generally above the U.S. federal statutory rate, partially offset by the recognition of income tax benefits associated with share-based payments. The effective income tax rate for the nine months ended September 30, 2022 was above the U.S. federal statutory rate of 21% primarily due to non-deductible transactions costs associated with the Merger, the accrual of additional income taxes associated with compensation deduction limitations under Section 162(m) of the Internal Revenue Code, the accrual of various state income taxes and the accrual of foreign income taxes, which are generally above the U.S. federal statutory rate, partially offset by the recognition of income tax benefits associated with share-based payments and the reduction in the valuation allowance associated with certain state NOL carryforwards.

Net income

Net income for the nine months ended September 30, 2023, was $98.8 million compared to $47.5 million for the nine months ended September 30, 2022. Diluted net income per share for the nine months ended September 30, 2023 and September 30, 2022, was $0.56 and $0.33, respectively. Net income from discontinued operations, net of tax, was $8.1 million for the nine months ended September 30, 2023 compared to $0.8 million for the nine months ended September 30, 2022. Diluted net income per share from discontinued operations for the nine months ended September 30, 2023 and September 30, 2022, was $0.05 and $0.01, respectively.

Non-GAAP Financial Measures

Non-GAAP financial measures are intended to supplement and not replace financial measures prepared in accordance with GAAP. The following non-GAAP financial measures are utilized by management in comparing our operating performance on a consistent basis. We believe that these financial measures are appropriate to enhance an overall understanding of our underlying operating performance trends compared to historical and prospective periods and our peers. Management also believes that these measures are useful to investors in their analysis of our results of operations and provide improved comparability between fiscal periods as well as insight into the compliance with our debt covenants. Non-GAAP financial measures should not be considered in isolation from, or as a substitute for, financial information calculated in accordance with GAAP. Investors are encouraged to review the reconciliation of these non-GAAP measures to their most directly comparable GAAP financial measures.

Core sales

Core sales excludes the impact of acquisitions (such as the Elkay Merger), divestitures and foreign currency translation. Management believes that core sales facilitates easier and more meaningful comparisons of our net sales performance with prior and future periods and to our peers. We exclude the effect of acquisitions and divestitures because the nature, size and number can vary dramatically from period to period and between us and our peers and can also obscure underlying business trends and make comparisons of long-term performance difficult. We exclude the effect of foreign currency translation from this measure because the volatility of currency translation is not under management's control.

EBITDA

EBITDA represents earnings before interest and other debt related activities, taxes, depreciation and amortization. EBITDA is presented because it is an important supplemental measure of performance and it is frequently used by analysts, investors and other interested parties in the evaluation of companies in our industry. EBITDA is also presented and compared by analysts and investors in evaluating our ability to meet debt service obligations. Other companies in our industry may calculate EBITDA differently. EBITDA is not a measurement of financial performance under GAAP and should not be considered as an alternative to cash flow from operating activities or as a measure of liquidity or an alternative to net income as indicators of operating performance or any other measures of performance derived in accordance with GAAP. Because EBITDA is calculated before recurring cash charges, including interest expense and taxes, and is not adjusted for capital expenditures or other recurring cash requirements of the business, it should not be considered as a measure of discretionary cash available to invest in the growth of the business.

Adjusted EBITDA

Adjusted EBITDA is the term we use to describe EBITDA as defined and adjusted in our credit agreement, which is net income, adjusted for the items summarized in the table below. Adjusted EBITDA is an important measure because, under our credit agreement, our ability to incur certain types of acquisition debt and certain types of subordinated debt, make certain types of acquisitions or asset exchanges, operate our business and make dividends or other distributions, all of which will impact our financial performance, is impacted by our Adjusted EBITDA, as our lenders measure our performance with a net first lien leverage ratio by comparing our senior secured bank indebtedness to our Adjusted EBITDA. It also is intended to show our unleveraged, pre-tax operating results and therefore reflects our financial performance based on operational factors, excluding non-operational, non-cash or non-recurring losses or gains. It is also provided to aid investors in understanding our compliance with our debt covenants. Adjusted EBITDA is not a presentation made in accordance with GAAP, and our use of the term Adjusted EBITDA varies from others in our industry. This measure should not be considered as an alternative to net income, income from operations or any other performance measures derived in accordance with GAAP. Adjusted EBITDA has important limitations as an analytical tool, and should not be considered in isolation, or as a substitute for analysis of our results as reported under GAAP. For example, Adjusted EBITDA does not reflect: (a) our capital expenditures, future requirements for capital expenditures or contractual commitments; (b) changes in, or cash requirements for, our working capital needs; (c) the significant interest expenses, or the cash requirements necessary to service interest or principal payments, on our debt; (d) tax payments that represent a reduction in cash available to us; (e) any cash requirements for the assets being depreciated and amortized that may have to be replaced in the future; or (f) the impact of earnings or charges resulting from matters that we and the lenders under our credit agreement may not consider indicative of our ongoing operations. In particular, our definition of Adjusted EBITDA allows us to add back certain non-cash, non-operating or non-recurring charges that are deducted in calculating net income, even though these are expenses that may recur, vary greatly and are difficult to predict and can represent the effect of long-term strategies as opposed to short-term results.

In addition, certain of these excluded expenses added back in calculating Adjusted EBITDA can represent the reduction of cash that could be used for other corporate purposes. Further, although not included in the calculation of Adjusted EBITDA below, the measure may at times allow us to add estimated cost savings and operating synergies related to operational changes ranging from acquisitions or dispositions to restructuring, and/or exclude one-time transition expenditures that we anticipate we will need to incur to realize cost savings before such savings have occurred.

For the nine months ended September 30, 2023, we had net income of $98.8 million and Adjusted EBITDA for the same period of $255.4 million. The calculation of Adjusted EBITDA under our credit agreement as of September 30, 2023, is presented in the table below. However, the results of such calculation could differ in the future based on the different types of adjustments that may be included in such respective calculations at the time.

Covenant Compliance

Our credit agreement, which governs our senior secured credit facilities, contains, among other provisions, restrictive covenants regarding indebtedness, payments and distributions, mergers and acquisitions, asset sales, affiliate transactions, capital expenditures and the maintenance of certain financial ratios. Payment of borrowings under the credit agreement may be accelerated if there is an event of default. Events of default include the failure to pay principal and interest when due, a material breach of a representation or warranty, certain non-payments or defaults under other indebtedness, covenant defaults, events of bankruptcy and a change of control. Certain covenants contained in the credit agreement restrict our ability to take certain actions, such as incurring additional debt or making acquisitions, if we are unable to comply with a maximum total Net First Lien Leverage Ratio (consolidated indebtedness to Adjusted EBITDA) of 5.00 to 1.00 as of the end of each fiscal quarter. At September 30, 2023, our Net First Lien Leverage Ratio was 1.26 to 1.00. Failure to comply with these covenants could limit our long-term growth prospects by hindering our ability to borrow under the revolver, to obtain future debt and/or to make acquisitions.

Set forth below is a reconciliation of net income to Adjusted EBITDA for the periods indicated below.

(in millions)	Nine months ended September 30, 2022	Twelve months ended December 31, 2022	Nine months ended September 30, 2023	Twelve months ended September 30, 2023
Net income	$ 47.5	$ 61.7	$ 98.8	$ 113.0
Income from discontinued operations, net of tax (1)	(0.8)	(4.7)	(8.1)	(12.0)
Provision for income taxes	22.9	26.8	34.8	38.7
Actuarial gain on pension and postretirement benefit obligations	—	(1.9)	—	(1.9)
Other expense (income), net (2)	(0.3)	(1.7)	3.3	1.9
Interest expense	18.0	26.9	29.8	38.7
Depreciation and amortization	30.9	54.5	66.3	89.9
EBITDA	118.2	161.6	224.9	268.3
Adjustments to EBITDA				
Restructuring and other similar charges (3)	13.1	15.4	11.9	14.2
Stock-based compensation expense	15.5	25.0	30.5	40.0
Merger costs (4)	33.7	33.7	—	—
Last-in first-out ("LIFO") adjustments (5)	4.0	9.7	(11.9)	(6.2)
Acquisition-related fair value adjustment	15.2	18.9	—	3.7
Other, net (6)	0.3	0.3	—	—
Subtotal of adjustments to EBITDA	81.8	103.0	30.5	51.7
Adjusted EBITDA	**$ 200.0**	**$ 264.6**	**$ 255.4**	**$ 320.0**
Consolidated indebtedness (7)				$ 401.8
Total Net First Lien Leverage Ratio (8)				**1.26**

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(1) Income from discontinued operations, net of tax is not included in Adjusted EBITDA in accordance with the terms of our credit agreement.

(2) Other expense (income), net for the periods indicated, consists primarily of gains and losses from foreign currency transactions, the non-service cost components of net periodic benefit costs associated with our defined benefit plans and other non-operational gains and losses.

(3) Restructuring and other similar charges is comprised of costs associated with workforce reductions, asset impairments, lease termination costs, and other facility rationalization costs. See Item 1, Note 3, Restructuring and Other Similar Charges for more information.

(4) Merger costs is comprised of costs associated with legal and other professional services incurred in connection with completing the Elkay Merger, which are excluded in calculating Adjusted EBITDA as defined in our credit agreement.

(5) LIFO adjustments are excluded in calculating Adjusted EBITDA as defined in our credit agreement.

(6) Other, net consists of gains and losses on the disposition of long-lived assets.

(7) Our credit agreement defines our consolidated indebtedness as the sum of all indebtedness (other than letters of credit or bank guarantees, to the extent undrawn) consisting of indebtedness for borrowed money and capitalized lease obligations, less unrestricted cash, which was $152.4 million (as defined by the credit agreement) at September 30, 2023.

(8) Our credit agreement defines the total Net First Lien Leverage Ratio as the ratio of consolidated indebtedness (as described above) to Adjusted EBITDA for the trailing four fiscal quarters.

Liquidity and Capital Resources

Our primary sources of liquidity are available cash and cash equivalents, cash flow from operations, and borrowing availability of up to $200.0 million under our revolving credit facility.

As of September 30, 2023, we had $173.1 million of cash and cash equivalents and $194.2 million of additional borrowing capacity. As of September 30, 2023, the available borrowings under our credit facility were reduced by $5.8 million due to outstanding letters of credit. As of December 31, 2022, we had $124.8 million of cash and cash equivalents and approximately $192.5 million of additional borrowing capacity under our revolving credit facility.

Our revolving credit facility is available to fund our working capital requirements, capital expenditures and for other general corporate purposes. We believe this resource is adequate for our expected short-term and long-term needs.

Cash Flows

Cash provided by operating activities was $195.7 million and $12.6 million during the nine months ended September 30, 2023 and 2022, respectively. The change in year-over-year operating cash flows was primarily the result of a lower use of cash for trade working capital, an increase in net income, and the timing of accrued expenses during the nine months ended September 30, 2023.

Cash used for investing activities was $6.6 million during the nine months ended September 30, 2023 and $12.8 million during the nine months ended September 30, 2022. Investing activities during the nine months ended September 30, 2023, consisted of $15.9 million of capital expenditures, which were partially offset by the receipt of $9.0 million in connection with an insurance settlement and $0.3 million from the sale of certain long-lived assets. Investing activities during the nine months ended September 30, 2022, included $4.3 million of capital expenditures and net cash payments of $44.8 million in connection with acquisitions, which was offset by the receipt of $35.0 million from Regal Rexnord Corporation in connection with the final net assets transferred in the PMC Spin-Off Transaction and the receipt of $1.3 million in connection with the sale of certain long-lived assets.

Cash used for financing activities was $141.5 million during the nine months ended September 30, 2023, compared to $23.1 million during the nine months ended September 30, 2022. During the nine months ended September 30, 2023, we utilized a net $4.7 million of cash for payments on outstanding debt, $100.2 million to repurchase outstanding shares of our common stock and $36.6 million for the payment of common stock dividends. During the nine months ended September 30, 2022, we utilized a net $4.4 million of cash for payments on outstanding debt and $20.1 million for the payment of common stock dividends, which was partially offset by $1.4 million of proceeds from the exercise of stock options, net of taxes withheld and paid on employees' share-based awards.

Indebtedness

As of September 30, 2023, we had $554.2 million of total indebtedness outstanding as follows (in millions):

	Total Debt at September 30, 2023	Current Maturities of Debt	Long-term Portion
Term loan (1)	$ 532.4	$ 5.5	$ 526.9
Finance leases	21.8	0.8	21.0
Total	$ 554.2	$ 6.3	$ 547.9

____

(1) Includes unamortized debt issuance costs of $8.0 million at September 30, 2023.

See Item 1, Note 13, Long-Term Debt for a description of our outstanding indebtedness.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to market risk during the normal course of business from changes in foreign currency exchange rates and interest rates. The exposure to these risks is managed through a combination of normal operating and financing activities and at times derivative financial instruments in the form of foreign currency forward contracts to cover certain known foreign currency transactional risks. We also have historically entered into interest rate derivatives to manage interest rate fluctuations.

ITEM 4. CONTROLS AND PROCEDURES

We maintain a set of disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

We carried out an evaluation, under the supervision and with the participation of management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Rules 13a-15(f) and 15d-15(f) of the Exchange Act. Based on that evaluation as of September 30, 2023, the Chief Executive Officer and Chief Financial Officer concluded that, as of such date, the Company's disclosure controls and procedures are adequate and effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act and that such information is accumulated and communicated to the Company's management, including the Chief Executive Officer and Chief Financial Officer, in a manner allowing timely decisions regarding required disclosure. As such, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the period covered by this report.

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 the changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

There have been no changes in our internal control over financial reporting that occurred during our last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

See the information under the heading "Commitments and Contingencies" in Note 15 to the condensed consolidated financial statements contained in Part I, Item 1 of this report, which is incorporated in this Part II, Item 1 by reference.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

In fiscal 2015, the Company's Board of Directors approved a stock repurchase program (the "Repurchase Program") authorizing the repurchase of up to $200.0 million of the Company's common stock from time to time on the open market or in privately negotiated transactions. On January 27, 2020, the Company's Board of Directors increased the remaining share repurchase authority under the Repurchase Program to $300.0 million. On February 8, 2023, the Company's Board of Directors approved increasing the remaining share repurchase authority under the Repurchase Program to $500.0 million. The Repurchase Program does not require the Company to acquire any particular amount of common stock and does not specify the timing of purchases or the prices to be paid; however, the program will continue until the maximum amount of dollars authorized have been expended or until it is modified or terminated by the Board of Directors. During the three months ended September 30, 2023, the Company repurchased 444,606 shares of common stock at a total cost of $13.0 million at a weighted average price of $29.24 per share. The repurchased shares were canceled by the Company upon receipt. Approximately $415.5 million of the existing authority remained under the Repurchase Program at September 30, 2023.

ISSUER PURCHASES OF EQUITY SECURITIES

	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1)	Maximum Approximate Dollar Value that may yet be Purchased Under the Plans or Programs (1)
Period				
July 1 - July 31, 2023	—	$ —	—	$ 428,482,327
August 1 - August 31, 2023	318,857	$ 29.42	318,857	$ 419,752,079
September 1 - September 30, 2023	125,749	$ 28.77	125,749	$ 415,473,453
Total/Average	444,606	$ 29.24	444,606	

(1) See explanation of the Repurchase Program above.

ITEM 5. OTHER INFORMATION

During the three months ended September 30, 2023, no director or officer of the Company adopted or terminated a "Rule 10b5-1 trading arrangement" or "non-Rule 10b5-1 trading arrangement," as each term is defined in Item 408(a) of Regulation S-K.

ITEM 6. EXHIBITS

hibit No.	Description	Filed Herewith
1.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 and Rule 13a-14(a) under the Securities Exchange Act of 1934, as amended.	X
1.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 and Rule 13a-14(a) under the Securities Exchange Act of 1934, as amended.	X
2.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350	X
..INS	Inline XBRL Instance Document (The instance document does not appear in the interactive data file because its XBRL tags are embedded within the inline XBRL document.)	X
.SCH	Inline XBRL Taxonomy Extension Schema Document	X
.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document	X
.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document	X
.LAB	Inline XBRL Taxonomy Extension Label Linkbase Document	X
.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document	X
04	Cover Page Inline XBRL data (contained in Exhibit 101)	X

SIGNATURE

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

			ZURN ELKAY WATER SOLUTIONS CORPORATION
Date:	October 31, 2023	By:	/s/ MARK W. PETERSON
		Name:	**Mark W. Peterson**
		Title:	**Senior Vice President and Chief Financial Officer**

Exhibit 31.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER

I, Todd A. Adams, Chair of the Board, President and Chief Executive Officer of **Zurn Elkay Water Solutions Corporation**, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Zurn Elkay Water Solutions Corporation;
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 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 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 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 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.

Date: October 31, 2023

By:	/s/ TODD A. ADAMS
Name:	Todd A. Adams
Title:	Chairman of the Board, President and Chief Executive Officer

Exhibit 31.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER

I, Mark W. Peterson, Senior Vice President and Chief Financial Officer of **Zurn Elkay Water Solutions Corporation**, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Zurn Elkay Water Solutions Corporation;
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 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 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 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 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.

Date: October 31, 2023

By:	/s/ MARK W. PETERSON
Name:	Mark W. Peterson
Title:	Senior Vice President and Chief Financial Officer

EXHIBIT 32.1

CERTIFICATION

Pursuant to 18 United States Code § 1350

Each of the undersigned hereby certifies that the Quarterly Report on Form 10-Q for the quarter ended September 30, 2023 of Zurn Elkay Water Solutions Corporation (the "Company") filed with the Securities and Exchange Commission on or about the date hereof fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that the information contained in such report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: October 31, 2023

By:	/s/ TODD A. ADAMS
Name:	Todd A. Adams
Title:	Chairman of the Board, President and Chief Executive Officer

Date: October 31, 2023

By:	/s/ MARK W. PETERSON
Name:	Mark W. Peterson
Title:	Senior Vice President and Chief Financial Officer

This certification accompanies the Quarterly Report on Form 10-Q pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not be deemed filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended. A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.