HERCULES INC
Form 10-Q/A
August 20, 2002

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q/A

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

For the quarterly period ended June 30, 2002
Commission file number 1-496

HERCULES INCORPORATED

A Delaware corporation
I.R.S. Employer Identification No. 51-0023450
Hercules Plaza
1313 North Market Street
Wilmington, Delaware 19894-0001
Telephone: 302-594-5000

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

Yes: X No:

As of July 31, 2002, 109,201,778 shares of registrant's common stock were outstanding.

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

HERCULES INCORPORATED
CONSOLIDATED STATEMENT OF OPERATIONS

(Dollars in millions, except per share)	(Unaudited) Three Months Ended June 30,

	2002	2001
Net sales	$ 437	$ 459
Cost of sales (Note 6)	267	294
Selling, general and administrative expenses	84	107
Research and development	11	14
Goodwill and intangible asset amortization (Note 4)	3	6
Other operating expense (income), net (Note 7)	19	(65)
Profit from operations	53	103
Interest and debt expense (Note 8)	25	53
Preferred security distributions of subsidiary trusts	14	14
Other (expense) income, net (Note 9)	(45)	4
(Loss) income before income taxes and equity loss	(31)	40
(Benefit) provision for income taxes	(9)	25
(Loss) income before equity income (loss)	(22)	15
Equity income (loss) of affiliated companies, net of tax	1	(1)
Net(loss) income from continuing operations before discontinued operations and cumulative effect of change in accounting principle	(21)	14
Discontinued operations (Note 3)		
Income (loss) from operations of discontinued business (including loss on disposal of $155 million in the six months ended June 30, 2002)	16	27
Provision for income taxes	6	18
Net income (loss) on discontinued operations	10	9
Net (loss) income before cumulative effect of change in accounting principle	(11)	23
Cumulative effect of change in accounting principle, net of tax, (Note 4)	--	--
Net (loss) income	$ (11)	$ 23
Basic and diluted (loss) earnings per share (Note 5)		
Continuing operations	$(0.19)	$ 0.13
Discontinued operations	$ 0.09	$ 0.08
Cumulative effect of change in accounting principle	$ --	$ --
Net (loss) income	$(0.10)	$ 0.21
Weighted average number of shares - basic (millions)	109.0	108.1
Weighted average number of shares - diluted (millions)	109.0	108.3

See accompanying notes to financial statements.

HERCULES INCORPORATED
CONSOLIDATED BALANCE SHEET

(Dollars in millions)	(Unaudited) June 30, 2002	Decemb 20
ASSETS		
Current assets		
Cash and cash equivalents	$ 72	$
Accounts and notes receivable, net	373	
Inventories		
Finished products	82	
Materials, supplies, and work in process	81	
Deferred income taxes	--	
Total current assets	608	
Property, plant, and equipment	1,927	2,
Accumulated depreciation and amortization	(1,257)	(1,
Net property, plant, and equipment	670	
Goodwill and other intangible assets, net (Note 4)	631	2,
Other assets	815	
Total assets	$ 2,724	$ 5,
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$ 148	$
Accrued expenses	388	
Short-term debt (Note 11)	141	
Total current liabilities	677	
Long-term debt (Note 11)	545	1,
Deferred income taxes	202	
Postretirement benefits and other liabilities	470	
Commitments and contingencies (Note 13)		
Company-obligated preferred securities of subsidiary trusts (Note 12)	624	
Stockholders' equity		
Series preferred stock	--	
Common stock (shares issued: 2002 - 159,984,444; 2001 - 159, 984,444)	83	
Additional paid-in capital	688	
Unearned compensation	(104)	(
Other comprehensive losses	(137)	(
Retained earnings	1,508	2,
	2,038	2,
Reacquired stock, at cost (shares: 2002 - 50,832,374; 2001 - 51,196,972)	(1,832)	(1,
Total stockholders' equity	206	

Total liabilities and stockholders' equity	$ 2,724	$ 5,

See accompanying notes to financial statements.

HERCULES INCORPORATED
CONSOLIDATED STATEMENT OF CASH FLOW

(Dollars in millions)	(Unau Six Months E
	2002
Net cash used in operating activities of continuing operations	(303)
CASH FLOW FROM INVESTING ACTIVITIES:	
Capital expenditures	(13)
Proceeds of investment and fixed asset disposals	1,811
Other, net	4
Net cash provided by investing activities of continuing operations	1,802
CASH FLOW FROM FINANCING ACTIVITIES:	
Long-term debt proceeds	250
Long-term debt repayments	(1,770)
Change in short-term debt	(8)
Common stock issued	4
Net cash (used in) financing activities of continuing operations	(1,524)
Net cash provided by discontinued operations	25
Effect of exchange rate changes on cash	(4)
Net decrease in cash and cash equivalents	(4)
Cash and cash equivalents - beginning of period	76
Cash and cash equivalents - end of period	$72
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:	
Cash paid during the period for:	
Interest (net of amount capitalized)	66
Preferred security distributions of subsidiary trusts	29
Income taxes	133
Non-cash investing and financing activities:	
Incentive and other employee benefit stock plan	--

See accompanying notes to financial statements.

HERCULES INCORPORATED
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

(Dollars in millions)	(Unaudited) Three Months Ended June 30,		(Unaudited) Six Months Ended Jun	
	2002	2001	2002	200
Net (loss) income	$ (11)	$ 23	$(591)	$ 1
Foreign currency translation	33	(21)	(22)	(6
Reclassification adjustment for loss included in net (loss) income	103	--	103	-
Comprehensive income (loss)	$ 125	$ 2	$(510)	$(5

See accompanying notes to financial statements.

HERCULES INCORPORATED
NOTES TO FINANCIAL STATEMENTS
(Unaudited)

1. These condensed consolidated financial statements of Hercules Incorporated ("Hercules" or the "Company") are unaudited, but in the opinion of management include all adjustments necessary to present fairly in all material respects Hercules' financial position and results of operations for the interim periods. These condensed consolidated financial statements should be read in conjunction with the accounting policies, financial statements and notes included in Hercules' Annual Report on Form 10-K for the year ended December 31, 2001. Certain prior period amounts have been reclassified to conform to the current period presentation.

Pursuant to Securities and Exchange Commission ("SEC") Regulation S-X, Rule 3-10, the Company is required to provide condensed consolidating financial information on the Company and its subsidiaries in a prescribed format in all periodic reports filed with the SEC. The information necessary to present all of the required disclosures was not available in time to be included in this Form 10-Q filing. The Company is in the process of preparing the required condensed consolidating financial information and intends to file a Form 10-Q/A, which will include this information, as soon as it is available.

Pursuant to SEC Regulation S-X, Rule 3-16, the Company was required to provide separate company stand-alone audited financial statements in its Annual Report on Form 10-K for the fiscal year ended December 31, 2001 for certain subsidiaries whose stock was pledged as collateral and constituted a substantial portion of the collateral for the Company's registered debt (the "Collateral Audits"). The information necessary to present all of the required Collateral Audits was not available in time to be included in the Form 10-K filing. The Company is in the process of preparing the required Collateral Audits and intends to file a Form 10-K/A, which will include this information, as soon as it is available. Until these Collateral Audits are filed, the

Company will not have any registration statements or post-effective amendments to registration statements declared effective, and can not make offerings under effective registration statements. The stock pledges were released on April 29, 2002 (see Note 11). As a result, based on the Company's current debt structure, separate company stand-alone audited financial statements will not be required in the Company's Annual Report on Form 10-K for the fiscal year ending December 31, 2002.

The Company believes that the condensed consolidating financial information required by Regulation S-X, Rule 3-10, is not necessary to make the statements in its Quarterly Reports on Forms 10-Q and 10-Q/A for the quarters ended March 31, 2002 and June 30, 2002, in light of the circumstances under which they were made, not misleading as of the end of the period covered by each such report. The Company also believes that the Collateral Audits required by Regulation S-S, Rule 3-16, are not necessary to make the statements in its Annual Report on Form 10-K for the year ended December 31, 2001, in light of the circumstances under which they were made, not misleading as of the end of the period covered by such report.

2. In June 2001, the Financial Accounting Standards Board ("FASB") approved the issuance of Statement of Financial Accounting Standards No. 143, "Accounting for Asset Retirement Obligations" ("SFAS 143"). SFAS 143 establishes accounting standards for the recognition and measurement of legal obligations associated with the retirement of tangible long-lived assets. SFAS 143 will become effective for the Company on January 1, 2003 and requires recognition of a liability for an asset retirement obligation in the period in which it is incurred. The Company is in the process of evaluating the impact of this standard, but it does not believe it will have a material effect on its financial statements.

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS 144"). SFAS 144 addresses financial accounting and reporting for the impairment or disposal of long-lived assets.

In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment to FASB Statement No. 13, and Technical Corrections." The Company has elected to early adopt the provisions of SFAS 145 related to the rescission of SFAS 4, "Reporting Gains and Losses from the Extinguishment of Debt" ("SFAS 4"). Accordingly, the prepayment penalties and the write-off of debt issuance costs relating to the April 2002 debt repayment (see Note 11) are reported in net (loss) income from continuing operations. Under SFAS 4, the majority of these costs would have been reported as an extraordinary loss in the Consolidated Statement of Operations.

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS 146"). SFAS 146 addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs in a Restructuring)". SFAS 146 defines the timing of the recognition of costs associated with exit or disposal activities, the types of costs that may be recognized and the methodology for calculating the fair value of such costs. The provisions of SFAS 146 are effective for exit or disposal activities that are initiated after December 31, 2002. The Company does not believe this statement will have a material effect on its financial statements.

3. Discontinued Operations

On April 29, 2002, the Company completed the sale of the BetzDearborn Water Treatment Business (the "Water Treatment Business") to GE Specialty Materials, a unit of General Electric Company. The sale price was $1.8 billion in cash, resulting in net after tax proceeds of approximately $1.7 billion. The Company used the net proceeds to prepay debt under its senior credit facility and ESOP credit facility (see Note 11). Pursuant to SFAS 144, the Water Treatment Business has been treated as a discontinued operation as of February 12, 2002, and accordingly, 2001 financial information has been restated.

The Paper Process Chemicals Business, representing approximately one-third of the business originally acquired with BetzDearborn Inc. in 1998, was fully integrated into and continues to be reported within the Pulp and Paper Division.

Summarized below are the results of operations for the three and six months ended June 30, 2002 and 2001. The loss from discontinued operations for the three and six months ended June 30, 2002 includes an after-tax loss on the disposal of the business of $0 and $230 million, respectively.

(Dollars in millions)	Three Months Ended June 30,		Six Months Ended June	
	2002(1)	2001	2002(1)	2001
Net Sales	$77	$211	$ 269	$415
Profit from operations	16	26	49	42
Income before income taxes	16	27	51	42
Tax provision	6	18	20	24
Income from operations	10	9	31	18
Loss from disposal of business, including taxes of $0 and $75 million	--	--	(230)	--
Income (loss) from discontinued operations	$10	$ 9	$(199)	$ 18

(1) Results of operations for the respective periods are through April 28, 2002.

4. Goodwill and Other Intangible Assets

Effective January 1, 2002 the Company adopted the provisions of Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"). Under SFAS 142, goodwill and intangible assets with indefinite useful lives are not amortized but instead are reviewed for impairment at least annually and written down only in periods in which it is determined that the fair value is less than the recorded value. SFAS 142 also requires the transitional impairment review for goodwill, as well as an annual impairment review, to be performed on a reporting unit basis. The Company has identified the following reporting units: BetzDearborn, Pulp and Paper, Aqualon, FiberVisions and Resins. In connection with the Company's transitional review, recorded goodwill was determined to be impaired in the BetzDearborn and FiberVisions reporting units. In the first quarter of 2002, the Company completed its transitional impairment review of identified reporting units and recognized after tax impairment losses of $262 million in the BetzDearborn

reporting unit and $87 million in the FiberVisions reporting unit as a cumulative effect of a change in accounting principle.

In addition, an after tax impairment loss of $19 million was recognized in the first quarter of 2002 relating to the Company's equity investment in CP Kelco, which will also have an impairment under SFAS 142. After recognition of this impairment, the carrying value for the Company's investment in CP Kelco is zero.

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The following table reflects the effect of the adoption of SFAS 142 on net (loss) income and net (loss) earnings per share as if SFAS 142 had been in effect for the periods presented.

(Dollars in millions, except per share)	Three Months Ended June 30, 2002	Three Months Ended June 30, 2001
Net (loss) income before cumulative effect of change in accounting principle:		
As reported	$ (11)	$ 23
Goodwill amortization	--	13
Adjusted net (loss) income before cumulative effect of change in accounting principle	$ (11)	$ 36
Basic net (loss) earnings per share before cumulative effect of change in accounting principle:		
As reported	$ (0.10)	$ 0.21
Goodwill amortization	--	0.12
Adjusted basic (loss) earnings per share before cumulative effect of change in accounting principle	$ (0.10)	$ 0.33
Diluted net (loss) earnings per share before cumulative effect of change in accounting principle:		
As reported	$ (0.10)	$ 0.21
Goodwill amortization	--	0.12
Adjusted diluted (loss) earnings per share before cumulative effect of change in accounting principle	$ (0.10)	$ 0.33
Net (loss) income:		
As reported	$ (11)	$ 23
Goodwill amortization	--	13
Adjusted net (loss) income	$ (11)	$ 36
Basic net (loss) earnings per share:		
As reported	$ (0.10)	$ 0.21
Goodwill amortization	--	0.12
Adjusted basic (loss) earnings per share	$ (0.10)	$ 0.33

Diluted net (loss) earnings per share:		
As reported	$ (0.10)	$ 0.21
Goodwill amortization	--	0.12
Adjusted diluted (loss) earnings per share	$ (0.10)	$ 0.33

Accumulated amortization for goodwill upon adoption of SFAS 142 was $185 million. The following table shows changes in the carrying amount of goodwill for the six months ended June 30, 2002, by operating segment.

(Dollars in millions)	Performance Products	Engineered Materials and Additives	Tota
Balance at January 1, 2002	$ 1,724	$ 172	$ 1,8
Discontinued operations			
BetzDearborn	(948)	--	(9
Total discontinued operations	(948)	--	(9
Impairment losses			
BetzDearborn, discontinued operations	(155)	--	(1
BetzDearborn, cumulative effect	(267)	--	(2
FiberVisions, cumulative effect	--	(87)	(
Total impairment losses	(422)	(87)	(5
Foreign currency translation	15	--	
Balance at June 30, 2002	$ 369	$ 85	$ 4

The following table provides information regarding the Company's other intangible assets with finite lives:

(Dollars in millions)	Customer Relationships	Trademarks & Tradenames	Other Intangibles
Gross Carrying Amount			
Balance, January 1, 2002	$ 330	$ 250	$ 140
Discontinued operations - BetzDearborn	(241)	(180)	(70)
Balance, June 30, 2002	89	70	70
Accumulated Amortization			
Balance, January 1, 2002	$ (28)	$ (20)	$ (57)

Current year amortization	(2)	(1)	(4)
Discontinued operations - BetzDearborn	21	16	23
Balance, June 30, 2002	(9)	(5)	(38)
Net Carrying Amount			
Balance, January 1, 2002	$ 302	$ 230	$ 83
Current year amortization	(2)	(1)	(4)
Discontinued operations - BetzDearborn	(220)	(164)	(47)
Balance, June 30, 2002	$ 80	$ 65	$ 32

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Total amortization expense for each of the three month periods ended June 30, 2002 and 2001 for other intangible assets was $3 million and $6 million respectively, of which $3 million and $2 million was included in income from continuing operations for the three months ended June 30, 2002 and 2001, respectively. Total amortization expense for each of the six month periods ended June 30, 2002 and 2001 for other intangible assets was $7 million and $13 million, respectively, of which $5 million and $5 million, was included in income from continuing operations for the six months ended June 30, 2002 and 2001, respectively. Total goodwill amortization expense for the three and six months ended June 30, 2001 was $13 million and $25 million, respectively, of which $4 million and $8 million respectively, was included in income from continuing operations. Estimated amortization expense for 2002 and the five succeeding fiscal years is as follows: 2002 through 2006 - $9 million per year, 2007 - $8 million.

5. The following table shows the amounts used in computing (loss) earnings per share and the effect on income and the weighted-average number of shares of dilutive potential common stock:

(In millions, except per share)	Three Months Ended June 30, 2002		2001		Six 2002	
	(Loss) income	(Loss) earnings per share	(Loss) income	(Loss) earnings per share	(Loss) income	ea
BASIC:						
Continuing operations	$ (21)	$ (0.19)	$ 14	$ 0.13	$ (24)	$
Discontinued operations	10	0.09	9	0.08	(199)	
Cumulative effect of change in accounting principle	--	--	--	--	(368)	
Net (loss) income	(11)	(0.10)	23	0.21	(591)	
Weighted average number of basic shares (millions)	109.0		108.1		109.0	
DILUTED:						
Continuing operations	$ (21)	$ (0.19)	$ 14	$ 0.13	$ (24)	$
Discontinued operations	10	0.09	9	0.08	(199)	
Cumulative effect of change in accounting principle	--	--	--	--	(368)	

Net (loss) income	(11)	(0.10)	23	0.21	(591)
Weighted average number of diluted shares (millions)	109.0		108.3		109.0

6. Cost and expenses include depreciation related to continuing operations of $17 million and $20 million for the three months ended June 30, 2002 and 2001,respectively, and $35 million and $40 million for the six months ended June 30, 2002 and 2001, respectively.

7. Other operating expense (income), net, for the three and six months ended June 30, 2002 include environmental charges of approximately $4 million and $5 million, respectively, additional non-recurring restructuring charges of $6 million and $10 million associated with the comprehensive cost reduction and work process redesign program announced in September 2001 (see Note 10), respectively, and $6 million for an asset impairment charge in the Performance Products segment and miscellaneous expenses of $3 million in both periods.

Other operating expense (income), net, for the three and six months ended June 30, 2001 includes $74 million of net gains relating to the sale of the hydrocarbon resins and select portions of the rosin resins business, the peroxy

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chemicals business and the 50% interest in Hercules-Sanyo, Inc. These gains are partially offset by $5 million of executive severance charges for the three and six months ended June 30, 2001. The three and six months ended June 30, 2001 also include environmental charges of $1 million and $4 million, respectively, and non-recurring fees associated with the proxy contest and other matters of $2 million and $3 million, respectively. In addition, the three and six months ended June 30, 2001 include $1 million of costs relating to the abandonment of a capital project.

8. Interest and debt costs are summarized as follows:

(Dollars in millions)	Three Months Ended June 30,		Six Months Ended June 30,	
	2002	2001	2002	2001
Costs incurred	$25	$55	$61	$112
Amount capitalized	--	2	--	4
Interest expense	$25	$53	$61	$108

9. Other (expense) income, net, for the three and six months ended June 30, 2002 primarily includes a $43 million charge for debt prepayment penalties and the write-off of debt issuance costs associated with the repayment of debt with the proceeds from the sale of the Water Treatment Business (see Notes 3 and 11) and approximately $2 million and $6 million, respectively, for litigation costs of a former operating unit.

Other (expense) income, net, for the three and six months ended June 30, 2001 primarily includes foreign currency gains of approximately $6 million

and $5 million, respectively, offset by miscellaneous other expenses, net, of $2 million and $3 million, respectively.

10. The consolidated balance sheet reflects liabilities for employee severance benefits and other exit costs of $30 million and $43 million, respectively, at June 30, 2002 and December 31, 2001. During 2001, management authorized and committed to a plan to reduce the workforce as part of the comprehensive cost reduction and work process redesign program. Under this plan, approximately 1,129 employees have left or will leave the Company, of which approximately 912 employees were terminated through June 30, 2002. The Company incurred restructuring charges of $61 million relating to this plan, which includes charges of $55 million for employee termination benefits and $6 million for exit costs related to facility closures. For the three and six months ended June 30, 2002, as a result of additional employee terminations, the estimate for severance benefits pertaining to the 2001 plan increased by $5 million and $9 million, respectively. The estimate for exit costs related to facility closures was increased by an additional $1 million in the quarter ended June 30, 2002. The plan includes reductions throughout the Company with the majority of them from support functions as well as the BetzDearborn and Pulp and Paper Divisions.

The restructuring liabilities also include amounts relating to the 1998 plan initiated upon the acquisition of BetzDearborn and additional plans that the Company committed to in 2000 relating to the restructuring of the BetzDearborn and Pulp and Paper Divisions and corporate realignment due to the divestiture of non-core businesses. The total number of employee terminations relating to the 1998 plan is 889. The total number of employee terminations relating to the 2000 plan is 212. Actions under the 1998 and 2000 plans are complete.

Cash payments during the three and six months ended June 30, 2002 were $9 million and $20 million, respectively, for severance benefits and other exit costs. Severance benefits paid during the year include the continuing benefit streams of previously terminated employees under all three plans as well as those terminated in the current year. Severance benefits were paid in accordance with the Company's standard severance pay plans, or in accordance with local practices outside the United States.

A reconciliation of activity with respect to the liabilities established for these plans is as follows:

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	(Dollars in millions) June 30, 2002	December 31, 2001
Balance at beginning of year	$ 43	$ 34
Additional termination benefits and other exit costs	10	51
Cash payments	(20)	(25)
Reversals against goodwill	(3)	(10)
Reversals against earnings	--	(7)
Balance at end of period	$ 30	$ 43

The balance at the end of the period represents severance benefits and other exit costs of which $26 million pertains to the 2001 restructuring plan,

$2 million pertains to the 1998 BetzDearborn plan and $2 million relates to other restructuring plans initiated in 2000.

11. A summary of short-term and long-term debt follows:

	(Dollars in millions) June 30, 2002	December 31, 2001
SHORT-TERM:		
Banks	$ 1	$ 9
Current maturities of long-term debt	140	242
	$141	$251

At June 30, 2002, the Company had $48 million of unused lines of credit that may be drawn as needed. Lines of credit in use at June 30, 2002 were $1 million.

	(Dollars in millions) June 30, 2002	December 31, 2001
LONG-TERM:		
6.60% notes due 2027	100	100
6.625% notes due 2003	125	125
11.125% senior notes due 2007	400	400
8% convertible subordinated debentures due 2010	3	3
Term loan tranche A due in varying amounts through 2003	--	543
Term loan tranche D due 2005	--	372
Revolving credit agreement due 2003	--	516
ESOP debt	--	84
Term notes at various rates from 5.23% to 9.60% due in varying amounts through 2006	53	52
Other	4	6
	$ 685	$ 2,201
Current maturities of long-term debt	(140)	(242)
Net long-term debt	$ 545	$ 1,959

In 1998, the Company entered into a $3,650 million credit facility with a syndicate of banks which included varying maturity term loans totaling $2,750 million, of which no amount was outstanding at June 30, 2002. In addition, the facility included a $900 million revolving credit agreement, of which no amount was outstanding at June 30, 2002.

As of June 30, 2002, $200 million of the multi-currency revolver was available for use. The Company's incremental borrowing capacity was greater than the amount available for use at June 30, 2002. Actual availability under the revolving credit agreement has been constrained in the past, and could be constrained in the future, by the Company's ability to meet covenants in its senior credit facility.

Both the Company's senior credit facility and its ESOP credit facility require quarterly compliance with certain financial covenants, including a debt/EBITDA ratio ("leverage ratio"), an interest coverage ratio and minimum net worth. Effective March 6, 2002, the facilities were amended to (i) modify certain financial covenants (ii) change the mandatory prepayment provisions; (iii) permit the reorganization of the Company in order to effect the separation of the Water Treatment Business; and (iv) permanently reduce the revolving committed amount under the credit facility to $200 million. The amendment to the credit facility also included provisions that became effective upon the consummation of the sale of the Water Treatment Business and the prepayment of the credit facility, which occurred on April 29, 2002. These additional provisions included the following: (i) the release of the subsidiary stock pledged to the collateral agent; (ii) the elimination of the requirement that stock of any additional subsidiaries be pledged in the future; and (iii) the revision of the permitted amount of asset purchases and dispositions.

The Company used the net proceeds of approximately $1.7 billion from the sale of the Water Treatment Business (see Note 3) to permanently reduce long-term debt, repaying in full the following borrowings: Term Loan Tranche A, Term Loan Tranche D, the Revolving Credit Agreement and the ESOP credit facility. A portion of the net proceeds ($73 million) was used to collateralize the Company's outstanding letters of credit.

Effective with the consummation of the sale of the Water Treatment Business and the application of the net proceeds, the revolving credit facility was permanently reduced from $900 million to $200 million. Of the $200 million revolving credit facility, $170 million can be used for multi-currency denominated borrowings and $30 million is restricted to U.S. dollar-denominated debt. The amendment also resulted in the cancellation of the Canadian revolving credit facility. In addition, as a result of these repayments, in the second quarter of 2002 the Company recognized a $43 million charge (included in other expense (income), net) for debt prepayment penalties and the write-off of debt issuance costs relating to the debt that was repaid from the proceeds of the sale of the Water Treatment Business (see Notes 3 and 9).

12. Company-obligated Preferred Securities of Subsidiary Trusts consists of:

	(Dollars in millions) June 30, 2002	December 31, 2001
9.42% Trust Originated Preferred Securities	$362	$362
6 1/2% CRESTS Units	262	262
	$624	$624

13. Commitments and Contingencies

ENVIRONMENTAL

In the ordinary course of its business, the Company is subject to numerous environmental laws and regulations covering compliance matters or imposing liability for the costs of, and damages resulting from, cleaning up sites, past spills, disposals and other releases of hazardous substances. Changes in these laws and regulations may have a material adverse effect on the Company's financial position and results of operations. Any failure by the Company to adequately comply with such laws and regulations could subject the Company to significant future liabilities.

Hercules has been identified as a potentially responsible party (PRP) by U.S. federal and state authorities, or by private parties seeking contribution, for the cost of environmental investigation and/or cleanup at numerous sites. The estimated range of the reasonably possible share of costs for the investigation and cleanup is between $83 million and $251 million. The Company believes that the actual cost will more likely approximate $83 million based on its estimation methods and prior experience. The actual costs will depend upon numerous factors, including the number of parties found responsible at each environmental site and their ability to pay; the actual methods of remediation required or agreed to; outcomes of negotiations with regulatory authorities; outcomes of litigation; changes in environmental laws

and regulations; technological developments; and the years of remedial activity required, which could range from 0 to 30.

Hercules becomes aware of sites in which it may be named a PRP in investigatory and/or remedial activities through correspondence from the U.S. Environmental Protection Agency or other government agencies or from previously named PRPs, who either request information or notify the Company of its potential liability. The Company has established procedures for identifying environmental issues at its plant sites. In addition to environmental audit programs, the Company has environmental coordinators who are familiar with environmental laws and regulations and act as a resource for identifying environmental issues.

United States, et al. v. Vertac Corporation, et al., USDC No. LR-C-80-109 and LR-C-80-110 (E.D. Ark.)

This case, a cost-recovery action based upon the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA, or the Superfund statute), as well as other statutes, has been pending since 1980, and involves liability for costs expended and to be expended in connection with the investigation and remediation of the Vertac Chemical Company (Vertac) site in Jacksonville, Arkansas. Hercules owned and operated the site from December 1961 until 1971. The site was used for the manufacture of certain herbicides and, at the order of the United States, Agent Orange. In 1971, the site was leased to Vertac's predecessor. In 1976, Hercules sold the site to Vertac. The site was abandoned by Vertac in 1987, and Vertac was subsequently placed into receivership by the Court. Both prior to and following the abandonment of the site, the U.S. Environmental Protection Agency (EPA) and the Arkansas Department of Pollution Control and Ecology (ADPC&E) were involved in the investigation and remediation of contamination at and around the site. Pursuant to several orders issued pursuant to CERCLA, Hercules actively participated in many of these activities. The cleanup is essentially complete, except for certain on-going maintenance and monitoring activities. This litigation primarily concerns the responsibility for and the allocation of liability for the costs incurred in connection with these activities.

Although the case initially involved many parties, as a result of various United States District Court rulings and decisions, as well as a trial, Hercules and Uniroyal were held jointly and severally liable for the approximately $100 million in costs allegedly incurred by the EPA, as well as costs to be incurred in the future. That decision was made final by the District Court on September 13, 1999. Both Hercules and Uniroyal timely appealed that judgment to the United States Court of Appeals for the Eighth Circuit.

On February 8, 2000, the District Court issued a final judgment on the allocation between Hercules and Uniroyal finding Uniroyal liable for 2.6 percent and Hercules liable for 97.4 percent of the costs at issue. Hercules timely appealed that judgment. Oral argument in both appeals was held before the Eighth Circuit on June 12, 2000.

On April 10, 2001, the United States Court of Appeals for the Eighth Circuit issued an opinion in the consolidated appeals described above. In that opinion, the Appeals Court reversed the District Court's decision which had held Hercules jointly and severally liable for costs incurred and to be incurred at the Jacksonville site, and remanded the case back to the District Court for a determination of whether the harms at the site giving rise to the government's claims were divisible, as well as other findings of the District Court. The Appeals Court also vacated the District Court's allocation decision holding Hercules liable for 97.4 percent of the costs at issue, ordering that these issues be revisited following further proceedings with respect to divisibility. Finally, the Appeals Court affirmed the judgment of liability against Uniroyal.

The trial on remand commenced on October 8, 2001 and continued through October 19, 2001, and resumed on December 11, 2001, concluding on December 14, 2001. At the trial, the Company presented both facts and law to the District Court in support of its belief that the Company should not be liable under CERCLA for some or all of the costs incurred by the government in connection with the site because those harms are divisible. Should the Company prevail on remand, any liability to the government will be either eliminated or reduced from the prior judgment.

Hercules Incorporated v. Aetna Casualty & Surety Company, et al., Del. Super., C.A. No. 92C-10-105 and 90C-FE-195-1-CV (consolidated)

In 1992, Hercules brought suit against its insurance carriers for past and future costs for cleanup of certain environmental sites. In April 1998, the trial regarding insurance recovery for the Jacksonville, Arkansas, site (see discussion above) was completed. The jury returned a "Special Verdict Form" with findings that, in conjunction with the Court's other opinions, were used by the Court to enter a judgment in August 1999. The judgment determined the amount of Hercules' recovery for past cleanup expenditures and stated that Hercules is entitled to similar coverage for costs incurred since September 30, 1997 and in the future. Hercules has not included any insurance recovery in the

estimated range of costs above. Since entry of the Court's August 1999 order, Hercules has entered into settlement agreements with several of its insurance carriers and has recovered certain settlement monies. The terms of those settlements and the amounts recovered are confidential. On August 15, 2001, the Delaware Supreme Court issued a decision in Hercules Incorporated v. Aetna Casualty & Surety Company, et al., Del. Super., C.A. No. 92C-10-105 and 90C-FE-195-1-CV (consolidated). In its decision, the Delaware Supreme Court affirmed the trial court in part, reversed the trial court in part and remanded the case for further proceedings. The specific basis upon which the Delaware

Supreme Court reversed the trial court was the trial court's application of pro rata allocation to determine the extent of the insurers' liability. At this time, proceedings at the trial court have not yet commenced.

The Allegany Ballistics Laboratory ("ABL") is a government-owned facility which was operated by Hercules from 1945 to 1995. The United States Department of the Navy has notified Hercules that the Navy would like to negotiate with Hercules with respect to certain environmental liabilities which, the Navy alleges, are attributable to Hercules' past operations at ABL. The Navy alleges that, pursuant to CERCLA, it has spent a total of $24.8 million and that it expects to spend an additional $60 million over the next 10 years. The Company is currently investigating the Navy's allegations, including the basis of the Navy's claims, and whether the Company's contracts with the government pursuant to which the Company operated ABL may insulate the Company from some or all of the amounts sought. At this time, however, the Company cannot reasonably estimate its liability, if any, with respect to ABL and, accordingly, has not included this site in the range of its environmental liabilities reported above.

At June 30, 2002, the accrued liability of $83 million for environmental remediation represents management's best estimate of the probable and reasonably estimable costs related to environmental remediation. The extent of liability is evaluated quarterly. The measurement of the liability is evaluated based on currently available information, including the progress of remedial investigations at each site and the current status of negotiations with regulatory authorities regarding the method and extent of apportionment of costs among other PRPs. While it is not feasible to predict the outcome of all pending suits and claims, the ultimate resolution of these environmental matters could have a material effect upon the results of operations and the financial position of Hercules, and the resolution of any of these matters during a specific period could have a material effect on the quarterly or annual results of that period.

LITIGATION

The Company is a defendant in numerous asbestos-related personal injury lawsuits and claims which typically arise from alleged exposure to asbestos fibers from resin-encapsulated pipe and tank products which were sold by one of the Company's former subsidiaries to a limited industrial market ("products claims"). The Company is also a defendant in lawsuits alleging exposure to asbestos at facilities formerly or presently owned or operated by the Company ("premises claims"). Claims are received and settled or otherwise resolved on a regular basis. In late December 1999, the Company entered into a settlement agreement to resolve the majority of the claims then pending. In connection with that settlement, the Company also entered into an agreement with several of the insurance carriers which sold that former subsidiary primary and first level excess insurance policies. Under the terms of that agreement, the majority of the amounts paid to resolve those products claims will be insured, subject to the limits of the insurance coverage provided by those policies. The terms of both settlement agreements are confidential.

Since entering into those agreements, the Company has continued to receive and settle or otherwise resolve claims on a regular basis, with the number of new claims averaging approximately 2,200 per year during 2000 and 2001, but at a higher rate to date for 2002. We are evaluating whether this increase in claims is an anomaly or a new trend. As of June 2002, the Company had pending approximately 8,950 unresolved claims, of which approximately 665 are premises claims. In addition, as of June 2002, there were pending approximately 4,139 unpaid claims which have been settled or are subject to the terms of a settlement agreement. In accordance with the terms of the previously mentioned agreement with several insurance carriers, as well as agreements with two other excess insurance carriers, the majority of the amounts paid and to be paid to resolve those unpaid settled claims will be insured.

The Company anticipates that the primary and first level excess insurance policies referenced above will exhaust over the next 12 to 24 months, assuming that the rate of settlements and payments remains relatively consistent with the Company's past experience. Nonetheless, based on the current number of claims pending, the amounts the Company presently pays to resolve those claims, and anticipated future claims (the Company's assumption being that the number of future claims filed per year and claim resolution payments remain relatively consistent with the Company's past experience, and that these matters cease to be an ongoing liability after 2012), the Company believes that it and its former subsidiary together have sufficient additional insurance to cover the majority of its current and future asbestos-related liabilities. The Company is seeking defense and indemnity payments or an agreement to pay from those carriers responsible for excess coverage whose levels of coverage have been or will soon be reached. Although those excess

carriers have not yet agreed to defend or indemnify it, the Company believes that it is likely that they will ultimately agree to do so, and that the majority of future asbestos related costs will ultimately be paid or reimbursed by those carriers. However, if the Company is not able to reach satisfactory agreements with those carriers prior to exhaustion of the primary and first level excess insurance policies now covering the majority of its current asbestos related claims, then beginning as early as sometime in 2003, the Company might be required to completely fund these matters while it seeks reimbursement from its carriers.

Based on the assumptions set forth in the preceding paragraph, the reasonably possible future financial exposure for these matters is estimated to be less than $200 million. As stated above, the Company presently believes that the majority of this financial exposure will be funded by insurance proceeds. Cash payments related to this exposure are expected to be made over an extended number of years.

Due to the dynamic nature of asbestos litigation and the present uncertainty concerning the participation of its excess insurance carriers, however, the Company's estimates are inherently uncertain, and these matters may present significantly greater and longer lasting financial exposures than presently anticipated. As a result, the Company's liability with respect to asbestos-related matters could exceed the amount noted above. If the Company's liability does exceed that amount, the Company presently believes that the majority of any additional liability it may reasonably anticipate will be paid or reimbursed by its insurance carriers.

The Company has estimated and, therefore, has a recorded gross liability for asbestos-related matters in its June 30, 2002 balance sheet of $73 million. The Company believes that it is probable that $56 million of that amount will be funded by or recovered from insurance carriers. Accordingly, the Company has recorded an asset in this amount in its June 30, 2002 balance sheet.

In June 1998, Hercules and David T. Smith Jr., a former Hercules employee and a former plant manager at the Brunswick plant, along with Georgia-Pacific Corporation and AlliedSignal Inc., were sued in Georgia State Court by 423 plaintiffs for alleged personal injuries and property damage. This litigation is captioned Coley, et al. v. Hercules Incorporated, et al., No. 98 VSO 140933 B (Fulton County, Georgia). Plaintiffs allege they were damaged by the discharge of hazardous waste from the companies' plants. On February 11, 2000, the Georgia State Court dismissed Georgia-Pacific Corporation and AlliedSignal Inc., without prejudice. In September 2000, David T. Smith Jr., was dismissed by the Georgia State Court with prejudice. On July 18, 2000, the

Company was served with a complaint in a case captioned Erica Nicole Sullivan, et al. v. Hercules Incorporated and David T. Smith, Jr., Civil Action File No. 00-1-05463-99 (Cobb County, Georgia). Based on the allegations contained in the complaint, this matter is very similar to the Coley litigation, and is brought on behalf of approximately 700 plaintiffs for alleged personal injury and property damage arising from the discharge of hazardous waste from Hercules' plant. Although venue had been removed to the United States District Court for the Northern District of Georgia, the case was ultimately remanded back to state court. Both the Coley and the Erica Nicole Sullivan cases are in the early stages of motion practice and discovery. The Company denies any liability to plaintiffs, and it will vigorously defend both of these cases.

In August 1999, the Company was sued in an action styled as Cape Composites, Inc. v. Mitsubishi Rayon Co., Ltd., Case No. 99-08260 (U.S. District Court, Central District of California), one of a series of similar purported class action lawsuits brought on behalf of purchasers (excluding government purchasers) of carbon fiber and carbon prepreg in the United States from the named defendants from January 1, 1993 through January 31, 1999. The lawsuits were brought following published reports of a Los Angeles federal grand jury investigation of the carbon fiber and carbon prepreg industries. In these lawsuits, plaintiffs allege violations of Section 1 of the Sherman Antitrust Act for alleged price fixing. In September 1999, these lawsuits were consolidated by the Court into a case captioned Thomas & Thomas Rodmakers v. Newport Adhesives and Composites, Case No. CV-99-07796-GHK (CTx) (U.S. District Court, Central District of California), with all related cases ordered dismissed. This lawsuit is in the early stages of motion practice and discovery. On March 11, 2002, the Court tentatively granted plaintiffs' Motion to Certify Class. That Order was made final on May 2, 2002. The Company is named in connection with its former Composites Products Division, which was sold to Hexcel Corporation in 1996, has denied liability and will vigorously defend this action.

Beginning in September 2001, Hercules, along with the other defendants in the Thomas & Thomas Rodmakers action referred to above, has been sued in nine California state court purported class actions brought on behalf of indirect purchasers of carbon fiber. In January 2002, these were consolidated into a case captioned Carbon Fiber Cases I, II, and III, Judicial Council Coordination Proceedings Nos. 4212, 4216 and 4222, Superior Court of California, County of San Francisco. These actions all allege violations of the California Business and Professions Code relating to alleged price fixing of carbon fiber and unfair competition. The Company denies liability and will vigorously defend each of these actions.

In June 2002, a purported class action was filed in Massachusetts under the caption Saul M. Ostroff, et al. v. Newport Adhesives, et al., Civil Action No. 02-2385, Superior Court of Middlesex County. This matter is a purported class action brought on behalf of consumers who purchased merchandise manufactured by carbon fiber, and alleges the same types of price fixing activities alleged in the actions described in the above two paragraphs. Further, in April 2002, a related "Qui Tam" action was unsealed by the U.S. District Court for the Southern District of California. That action is captioned Randall M. Beck, et al. v. Boeing Defense and Space Group, Inc., et al. (Civil Action No. 99 CV 1557 JM JAH), was filed under seal in 1999, and is a "False Claims" action brought pursuant to the False Claims Act (31 U.S.C. Section 729 et seq.). In that action, the Relators, in the name of the United States Government, allege the same price fixing activities which are the subject of the above-described actions. The Relators then allege that those alleged price fixing activities resulted in inflated prices being charged by the defendant carbon fiber manufacturers to the defendant defense contractors, who, in turn,

submitted claims for payment to the United States Government under various government contracts. It is alleged that those claims for payment were "false claims" because the prices charged for the carbon fiber and carbon prepreg were "fixed" contrary to the laws of the United States. The Company denies liability and will vigorously defend each of these actions.

In connection with the grand jury investigation noted above, in January 2000, the United States Department of Justice (DOJ), Antitrust Division, served a grand jury subpoena duces tecum upon Hercules. The Company has been advised that it is one of several manufacturers of carbon fiber and carbon prepreg that have been served with such a subpoena.

In 1999, the Company was sued by Hexcel Corporation (Hexcel) in a case captioned Hexcel Corporation v. Hercules Incorporated, Index No. 602293/99, Supreme Court of New York, County of New York. In that case, Hexcel sought recovery of a total of approximately $8,422,000 (plus interest) in alleged "post-closing" adjustments to the purchase price paid by Hexcel for Hercules' former Composite Products Division. The basis for these alleged "adjustments" derive from the Sale and Purchase Agreement between Hercules and Hexcel dated as of April 15, 1996. In June 2000, the Court granted Hexcel's motion for summary judgment as to liability, finding the Company liable to Hexcel on technical grounds, but reserved ruling on the amount of damages. The Court then referred the damages determination to a Special Referee. In January 2001, the Special Referee issued a report, recommending that the Company be found liable to Hexcel for a total of approximately $7,300,000 plus interest, costs and expenses. In February 2001, Hexcel moved to confirm the Special Referee's Report and the Company moved to confirm in part and reject in part the Special Referee's Report. The Company specifically challenged the majority of the Special Referee's findings, and argued that a $2,000,000 indemnity "basket" established by the terms of the April 1996 Sale and Purchase Agreement should apply, reducing any award to Hexcel by $2,000,000. In May 2001, the Court accepted the Special Referee's Report and rejected the Company's position. As a result, judgment was entered against the Company in the amount of $10,219,685, which included pre-judgment interest, costs and expenses. The Company appealed to the Supreme Court, Appellate Division, First Department. On February 5, 2002, the Supreme Court of New York, Appellate Division, First Department, affirmed the decision of the trial court, entering judgment in favor of Hexcel in the full amount. The Company then filed a Motion for Reargument or for Leave to Appeal to the Court of Appeals, which was denied on March 19, 2002. On April 8, 2002, the Company filed a motion for Leave to Appeal to the New York Court of Appeals directly with the Court of Appeals, which motion was denied on June 13, 2002, exhausting all available avenues of appeal. In addition to the foregoing, in October 2000, Hexcel brought an action against Hercules to compel arbitration to determine the proper "Working Capital Adjustment" under the terms of the Sale and Purchase Agreement. Hexcel claimed it was owed approximately $1,500,000, while the Company claimed that it was owed approximately $129,000. In late 2001, this matter was submitted to binding arbitration. In December 2001, the arbitrator found in the Company's favor and awarded damages to the Company of $129,000. As a result of the foregoing, in June 2002 the Company paid Hexcel a total of $11,052,682, representing the net amount owed to Hexcel, including interest.

On September 28, 2000, the Company sold its Food Gums Division to CP Kelco ApS, a joint venture that the Company entered into with Lehman Brothers Merchant Banking Partners II, L.P. CP Kelco also acquired the biogums business of Pharmacia Corporation (formerly Monsanto Company). In April 2001, CP Kelco U.S., Inc., a wholly-owned subsidiary of CP Kelco ApS, sued Pharmacia (CP Kelco U.S., Inc. v. Pharmacia Corporation, U.S. District Court for the District of Delaware, Case No. 01-240-RRM) alleging federal securities fraud, common law fraud, breach of warranties and representations, and equitable fraud. In essence, the lawsuit alleges that Pharmacia misrepresented the value of the biogums business, resulting in damages to CP Kelco U.S., including the

devaluation of CP Kelco U.S.'s senior debt by the securities markets. The complaint seeks over $430 million in direct damages, as well as punitive damages. In June 2001, Pharmacia filed a third-party complaint against the Company and Lehman. That complaint seeks contribution and indemnification from the Company and Lehman, jointly and severally, for any damages that may be awarded to CP

Kelco U.S. in its action against Pharmacia. The Company believes that the third-party lawsuit against it and Lehman is without merit. The Company has denied any liability to Pharmacia and is vigorously defending this action.

At June 30, 2002, the consolidated balance sheet reflects a current liability of approximately $32 million and a long-term liability of approximately $44 million for litigation and claims. These amounts represent management's best estimate of the probable and reasonably estimable losses related to litigation or claims. The extent of the liability and recovery is evaluated quarterly. While it is not feasible to predict the outcome of all pending suits and claims, the ultimate resolution of these matters could have a material effect upon the financial position of Hercules, and the resolution of any of the matters during a specific period could have a material effect on the quarterly or annual operating results for that period.

14. Segment Information

Upon the decision to divest the Water Treatment Business, the Company realigned its reportable segments. The new reportable segments are Performance Products and Engineered Materials and Additives. The Performance Products segment is comprised of the Pulp and Paper Division and the Aqualon Division; the Engineered Materials and Additives segment is composed of FiberVisions and the Rosin and Terpenes Division.

(Dollars in millions)	Three Months Ended June 30,		Six Months End
	2002	2001 (a)	2002
Net Sales:			
Performance Products	$ 356	$ 349	$ 683
Engineered Materials and Additives (b)	81	110	156
Consolidated	$ 437	$ 459	$ 839
Profit from Operations:			
Performance Products	$ 62	$ 35	$ 120
Engineered Materials and Additives (b)	3	1	6
Reconciling Items (c)	(12)	67	(19)
Consolidated	$ 53	$ 103	$ 107

(a) As discussed above, the reportable segments of the Company have been realigned subsequent to the sale of the BetzDearborn Water Treatment Business. In addition, substantially all the reconciling items have been allocated to the segments.

(b) Net sales and Profit from operations in 2001 include the results of hydrocarbon resins, select rosin resins and the peroxy chemicals businesses which were divested in May 2001. Net sales and Profit from operations in 2001 have been reclassified to conform to the current year presentation.

(c) Reconciling Items for the three and six months ended June 30, 2002 include restructuring charges, environmental costs and other corporate costs not allocated to the businesses. Reconciling items for the three and six months ended June 30, 2001 include environmental costs, other corporate costs not allocated to the businesses and the net gains from the sale of the hydrocarbon resins, select rosins resins and peroxy chemicals businesses.

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

RESULTS OF OPERATIONS

Within the following discussion, unless otherwise stated, "quarter" and "six-month period" refer to the second quarter of 2002 and the six months ended June 30, 2002. All comparisons are with the corresponding periods in the previous year, unless otherwise stated.

On April 29, 2002, the Company completed the sale of its BetzDearborn Water Treatment Business (the "Water Treatment Business"). Accordingly, the Water Treatment Business has been treated as a discontinued operation. Following the divestiture, the Company realigned its reportable segments. The new reportable segments are Performance Products, consisting of the Pulp and Paper and Aqualon Divisions, and Engineered Materials and Additives, consisting of FiberVisions and the Rosin and Terpenes Divisions. In addition, substantially all reconciling items have been allocated to the segments. The reconciling items primarily include corporate expenses. Results of operations for 2001 have been restated to conform to the current year presentation.

Effective January 1, 2002, with the adoption of Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets," the Company ceased amortization of goodwill and other indefinite lived intangible assets. Goodwill amortization totaled $13 million and $25 million in the three and six months ended June 30, 2001, of which approximately $4 million and $8 million was related to continuing operations for the corresponding periods, and $9 million and $17 million was related to discontinued operations in the three and six months ended June 30, 2001.

In May 2001, the Company completed divestitures of its hydrocarbon resins business, select portions of its rosin resins business, and its peroxy chemicals business (the "Resins Divestitures").

The following tables reconcile reported sales and profit from operations for the three and six-month periods ended June 30, 2002 and 2001 to sales and profit from operations for the respective periods excluding non-recurring items, divested businesses and goodwill amortization.

(Dollars in millions)		(Unaudited)	
	Non-Recurring	Divested	G

	Reported	Items	Businesses	Am
THREE MONTHS ENDED JUNE 30, 2002:				
Net Sales by Industry Segment				
Performance Products	$ 356	$ --	$ --	
Engineered Materials and Additives	81	--	--	
Total	$ 437	$ --	$ --	
Profit from Operations by Industry Segment				
Performance Products	$ 62	$ 6 (1)	$ --	
Engineered Materials and Additives	3	--	--	
Reconciling Items	(12)	9 (2)	--	
Total	$ 53	$ 15	$ --	
THREE MONTHS ENDED JUNE 30, 2001:				
Net Sales by Industry Segment				
Performance Products	$ 349	$ --	$ --	
Engineered Materials and Additives	110	--	(31)(4)	
Total	$ 459	$ --	$ (31)	
Profit from Operations by Industry Segment				
Performance Products	$ 35	$ 1	$ --	
Engineered Materials and Additives	1	--	(2)(4)	
Reconciling Items	67	(68)(3)	--	
Total	$ 103	$ (67)	$ (2)	

(Dollars in millions)

	Reported	Non-Recurring Items	(Unaudited) Divested Businesses	A
SIX MONTHS ENDED JUNE 30, 2002:				
Net Sales by Industry Segment				
Performance Products	$ 683	$ --	$ --	
Engineered Materials and Additives	156	--	--	
Total	$ 839	$ --	$ --	
Profit from Operations by Industry Segment				
Performance Products	$ 120	$ 6 (1)	$ --	
Engineered Materials and Additives	6	--	--	
Reconciling Items	(19)	11 (2)	--	
Total	$ 107	$ 17	$ --	

SIX MONTHS ENDED JUNE 30, 2001:

Net Sales by Industry Segment			
Performance Products	$ 683	$ --	$ --
Engineered Materials and Additives	274	--	(113)(4)
Total	$ 957	$ --	$(113)
Profit from Operations by Industry Segment			
Performance Products	$ 73	$ 1	$ --
Engineered Materials and Additives	14	--	(8)(4)
Reconciling Items	62	(67)(3)	--
Total	$ 149	$ (66)	$ (8)

(1) Asset impairment charge.
(2) Primarily restructuring charges.
(3) Net gains on Resins Divestitures.
(4) Sales and operating profit from divested Resins businesses.

Consolidated net sales declined $22 million, or 5%, for the quarter and $118 million, or 12%, for the six-month period versus the corresponding periods in 2001. The decline in net sales primarily reflects the effects of the Resins Divestitures. Unfavorable foreign currency exchange translation, principally due to the weaker Euro, contributed approximately $8 million to the decrease in net sales for the six-month period; however, $1 million of favorable foreign currency translation was recognized in the quarter. Profit from operations decreased $50 million, or 49%, for the quarter and $42 million, or 28%, for the six-month period versus 2001. Profit from operations in 2002 includes non-recurring charges for restructuring and an asset impairment. Profit from operations in 2001 includes $67 million of pre-tax non-recurring gains resulting from the sales of the hydrocarbon resins, select portions of the rosin resins business and the peroxy chemicals business. Total volumes decreased 6% and 19% for the quarter and six-month period, respectively, reflecting the effects of the Resins Divestitures. Excluding divested businesses, consolidated net sales increased $9 million, or 2%, for the quarter and declined less than 1% for the six-month period. Volumes on the same basis increased 7% and 2%, respectively, for the three and six-month periods. Excluding non-recurring items, divested businesses and the effects of goodwill amortization from 2001 results, profit from operations improved $30 million, or 79%, for the quarter and $41 million, or 49% for the six-month period. The improvement in profit from operations is due primarily to cost reductions generated by the work process redesign programs partially offset by lower pricing across most of the businesses. The Company experienced normal seasonal pickup in its businesses in the second quarter. However, demand in the underlying markets for these businesses remains weak. The Company expects that earnings improvements will be generated primarily by continued cost savings realized from the implementation of work process improvements.

In the Performance Products segment, net sales were up $7 million, or 2%, for the quarter and remained flat for the six-month period versus the corresponding periods in 2001. Profit from operations improved $27 million, or 77%, for the quarter and $47 million, or 64%, for the six-month period. In the Pulp and Paper Division, net sales increased 5% and 1% for the quarter and six-month period versus the prior year periods. Excluding non-recurring items from all comparative periods and goodwill amortization from 2001 results, profit from operations improved 200% in Pulp and Paper for the quarter and 72% for the six-month period versus the same periods last year. The improvement in profit from operations was largely due to higher volumes and cost improvements,

partially offset by unfavorable pricing and recognition of an asset impairment. Net sales in the Aqualon Division declined 2% in both the quarter and six-month periods and profit from operations, excluding goodwill amortization from 2001 results, improved 31% for the quarter

and 48% for the six-month period. The increase in profit from operations was driven by lower raw material costs, cost reductions and favorable product mix, partially offset by lower pricing.

In the Engineered Materials and Additives segment, excluding divested businesses and goodwill amortization from 2001 operating profit results, net sales increased $2 million, or 3%, for the quarter and decreased $5 million, or 3%, for the six-month period. On the same basis, profit from operations improved $3 million in the quarter and decreased 25% for the six-month period versus the prior year period. FiberVisions net sales declined 4% and 7% for the quarter and six-month period, respectively. Lower sales in the quarter and six-month period were largely driven by contractual customer pass through of lower polypropylene costs. Profit from operations improved marginally in the quarter versus the second quarter 2001 and decreased 50% in the six-month period. The unfavorable variance in profit from operations in the six-month period versus the prior year is largely due to a revision of an estimate favorably benefiting the first quarter 2001. Excluding divested businesses, Rosin and Terpenes net sales improved 17% and 6% for the quarter and six-month period, respectively, and profit from operations improved versus both the prior year quarter and six-month period. The improvement in profit from operations resulted from the 2002 hiring of a full time sales team to support the business. Prior to 2002, sales were sourced through distribution channels.

Interest and debt expense and preferred security distributions of subsidiary trusts decreased $28 million for the quarter and $47 million for the six-month period, primarily due to lower outstanding debt balances, reflecting the application of proceeds from the sale of the Water Treatment Business on April 29, 2002 and 2001 assets sales, as well as lower interest costs. The Company used the proceeds from 2001 asset sales to reduce debt balances by approximately $336 million in 2001. Following the sale of the Water Treatment Business, the Company applied the proceeds to permanently reduce long-term debt by approximately $1.6 billion and collaterize $73 million of the Company's outstanding letters of credit (see Note 11).

Other expense, net increased $49 million primarily due to the write-off of debt issuance costs associated with the repayment of debt with the proceeds from the sale of the Water Treatment Business (see Notes 3, 9 and 11) and lower foreign currency gains recognized in the three months ended June 30, 2002 versus the prior year.

The effective tax rate for the quarter for continuing operations was 28% versus 63% for the same period in 2001. The anticipated tax rate for continuing operations for 2002 is approximately 62%.

DISCONTINUED OPERATIONS

On April 29, 2002, Hercules completed the sale of the Water Treatment Business to GE Specialty Materials, a unit of General Electric Company. The sale price was $1.8 billion in cash, resulting in net after tax proceeds of approximately $1.7 billion. The Company used the net proceeds to prepay debt under its senior credit facility and ESOP credit facility (see Note 11). Pursuant to SFAS 144, the Water Treatment Business has been treated as a discontinued operation as of February 12, 2002, and accordingly, 2001 financial

information has been restated. The loss from discontinued operations for the three and six months ended June 30, 2002 includes an after-tax loss on the disposal of the business of $0 and $230 million, respectively.

The Paper Process Chemicals Business, representing approximately one-third of the business of BetzDearborn Inc. originally acquired in 1998, was fully integrated into and continues to be reported within the Pulp and Paper Division.

ADOPTION OF SFAS NO. 142

The Company implemented Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142") during the first quarter 2002. Under the provisions of this standard, goodwill and intangible assets with indefinite useful lives are not amortized but instead are reviewed for impairment at least annually and written down only in periods in which it is determined that the fair value is less than the recorded value. In connection with the Company's transitional review, recorded goodwill was determined to be impaired in the BetzDearborn and FiberVisions reporting units. The Company recognized after tax impairment charges of $262 million in the BetzDearborn reporting unit and $87 million in the FiberVisions reporting unit. In addition, an after tax impairment charge of $19 million was recognized for the Company's equity investment in CP Kelco. After recognition of this impairment charge, the Company's book carrying value in CP Kelco is zero.

FINANCIAL CONDITION

Liquidity and Financial Resources. Net cash used in continuing operations was $271 million for the second quarter 2002 compared to cash used in continuing operations of $16 million in the second quarter 2001. The increase

primarily reflects higher working capital requirements due largely to tax payments and a $65 million pension contribution. The current ratio has decreased to .90 at June 30, 2002, compared with .92 at December 31, 2001. The quick ratio was .66 at December 31, 2001 and June 30, 2002. As of June 30, 2002, the Company had $200 million available under its revolving credit agreement and $48 million of short-term lines of credit. The Company's incremental borrowing capacity was greater than the amount available for use at June 30, 2002. The Company expects to meet short-term cash requirements from operating cash flow and availability under lines of credit. However, actual availability is constrained by the Company's ability to meet covenants in its senior credit facility. Future compliance with debt covenants is dependent upon generating sufficient EBITDA and cash flow which are, in turn, impacted by business performance, economic climate, competitive uncertainties and possibly the resolution of contingencies.

Effective March 6, 2002, the Company amended its senior credit facility and ESOP credit facility to (i) modify certain financial covenants; (ii) change the mandatory prepayment provisions; (iii) permit the reorganization of the Company in order to effect the separation of the Water Treatment Business; and (iv) permanently reduce the revolving committed amount under the credit facility to $200 million. The amendment to the credit facilities also included provisions that became effective upon the consummation of the sale of the Water Treatment Business and the prepayment of the credit facility, both of which were completed on April 29, 2002. These additional provisions include the following: (i) the release of the subsidiary stock pledged to the collateral agent; (ii) the elimination of the requirement that stock of any additional subsidiaries be pledged in the future; and (iii) the revision of the permitted amount of asset

purchases and dispositions. The Company used the net proceeds of approximately $1.7 billion from the Water Treatment Business sale to permanently reduce long-term debt, repaying in full the following borrowings: Term Loan Tranche A, Term Loan Tranche D, the Revolving Credit Agreement and the ESOP credit facility. A portion of the net proceeds ($73 million) was used to collateralize the Company's outstanding letters of credit. The revolving credit facility was permanently reduced from $900 million to $200 million. Of the $200 million revolving credit facility, $170 million can be used for multi-currency denominated borrowings and $30 million is restricted to U.S. dollar-denominated debt. The amendment also resulted in the cancellation of the Canadian revolving credit facility. In addition, as a result of these repayments, in the second quarter of 2002 the Company recognized a $43 million charge (included in other expense (income), net) for debt prepayment penalties and the write-off of debt issuance costs relating to the debt that was repaid from the proceeds of the sale of the Water Treatment Business (see Notes 3 and 9).

Capital Structure and Commitments. Total capitalization (stockholders' equity, Company obligated preferred securities of subsidiary trusts and debt) decreased to $1.5 billion at June 30, 2002, from $3.5 billion at year-end 2001. The ratio of debt-to-total capitalization decreased to 45% at June 30, 2002 from 62% at December 31, 2001.

RISK FACTORS

Market Risk - Fluctuations in interest and foreign currency exchange rates affect the Company's financial position and results of operations. The Company uses several strategies from time to time to actively hedge interest rate and foreign currency exchange rate exposure and minimize the effect of such fluctuations on reported earnings and cash flow. Sensitivity of the Company's financial instruments to selected changes in market rates and prices, which are reasonably possible over a one-year period, are described below. Market values are the present value of projected future cash flows based on the market rates and prices chosen. The market values for interest rate risk are calculated by utilizing a third-party software model that utilizes standard pricing models to determine the present value of the instruments based on the market conditions as of the valuation date.

The Company's derivative and other financial instruments subject to interest rate risk consist of debt instruments, interest rate swaps and currency swaps. At June 30, 2002, net market value of these combined instruments was a liability of $1.3 billion. The sensitivity analysis assumes an instantaneous 100-basis point move in interest rates from their current levels, with all other variables held constant. A 100-basis point increase in interest rates at June 30, 2002 would result in a $68 million decrease in the net market value of the liability. A 100-basis point decrease in interest rates at June 30, 2001 would result in a $76 million increase in the net market value of the liability. The change in the net market value of derivative and other financial instruments from year-end 2001 is primarily due to the repayment of both syndicated and revolving debt as a result of the sale of the Water Treatment Business on April 29, 2002 (see Notes 3 and 11).

The Company's financial instruments subject to foreign currency exchange risk consist of foreign currency forwards and options and represent a net liability position of $3 million at June 30, 2002. The following sensitivity analysis assumes an instantaneous 10% change in foreign currency exchange rates from year-end levels, with all other variables held constant. A 10% strengthening of the U.S. dollar versus other currencies at June 30, 2002 would result in

a $5 million increase in the net liability position which would result in a net asset position, while a 10% weakening of the dollar versus all currencies would result in a $6 million decrease in the net asset position.

Foreign exchange forward and option contracts have been used to hedge the Company's firm and anticipated foreign currency cash flows. Thus, there is either an asset or cash flow exposure related to all the financial instruments in the above sensitivity analysis for which the impact of a movement in exchange rates would be in the opposite direction and substantially equal to the impact on the instruments in the analysis. There are presently no significant restrictions on the remittance of funds generated by the Company's operations outside the United States.

The Company has not designated any derivative as a hedge instrument under Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended, and accordingly, changes in the fair value of derivatives are recorded each period in earnings.

Environmental Litigation - Hercules has been identified by U.S. federal and state authorities as a "potentially responsible party" for environmental cleanup at numerous sites. The estimated range of reasonably possible costs for remediation is between $83 million and $251 million. The Company does not anticipate that its financial condition will be materially affected by environmental remediation costs in excess of amounts accrued, although quarterly or annual operating results could be materially affected (see Note 13 in Notes to Financial Statements).

Environmental remediation expenses are funded from internal sources of cash. Such expenses are not expected to have a significant effect on the Company's ongoing liquidity. Environmental cleanup costs, including capital expenditures for ongoing operations, are a normal, recurring part of operations and are not significant in relation to total operating costs or cash flows.

Other Litigation - Hercules is a defendant in numerous lawsuits that arise out of, and are incidental to, the conduct of its business. These suits concern issues such as product liability, contract disputes, labor-related matters, patent infringement, environmental proceedings, property damage and personal injury matters. While it is not feasible to predict the outcome of all pending suits and claims, the ultimate resolution of these matters could have a material effect upon the financial position of Hercules, and the resolution of any of the matters during a specific period could have a material effect on the quarterly or annual operating results for that period (see Note 13 in Notes to Financial Statements).

FORWARD-LOOKING STATEMENT

This quarterly report on Form 10-Q/A includes forward-looking statements, as defined in the Private Securities Litigation Reform Act of 1995, reflecting management's current analysis and expectations, based on reasonable assumptions. Forward-looking statements may involve known and unknown risks, uncertainties and other factors, which may cause the actual results to differ materially from those projected, stated or implied, depending on such factors as: ability to generate cash, ability to raise capital, the result of the pursuit of strategic alternatives, ability to execute work process redesign and reduce costs, business climate, business performance, economic and competitive uncertainties, higher manufacturing costs, reduced level of customer orders, changes in strategies, risks in developing new products and technologies, environmental and safety regulations and clean-up costs, foreign exchange rates, adverse legal and regulatory developments, including increases in the number or financial exposures of claims, lawsuits, settlements or judgments, or

the inability to eliminate or reduce such financial exposures by collecting indemnity payments from insurers, and adverse changes in economic and political climates around the world. Accordingly, there can be no assurance that the Company will meet future results, performance or achievements expressed or implied by such forward-looking statements. As appropriate, additional factors are contained in other reports filed with the Securities and Exchange Commission. This paragraph is included to provide safe harbor for forward-looking statements, which are not generally required to be publicly revised as circumstances change.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

For discussion of quantitative and qualitative disclosure about market risk, see "Risk Factors" under Item 2, Management's Discussion and Analysis of Results of Operations and Financial Condition.

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PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

For information related to Legal Proceedings, see Notes to Financial Statements.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Below is a summary of the final voting results from our Annual Meeting of Stockholders that was held on June 27, 2002. A quorum of 92,489,150, or 84.79% of the outstanding voting shares as of the record date, was present in person or by proxy at the annual meeting.

1. Election of Directors

Four of our 13 directors had terms that expired during 2002 and stood for re-election this year.

Directors were elected to serve for three-year terms, expiring at the 2005 Annual Meeting of Shareholders, or until their successors are elected and qualified.

Name	For	Withhold Authority
William H. Joyce	76,916,057	15,573,093
Robert D. Kennedy	76,608,500	15,880,650
Jeffrey M. Lipton	76,729,155	15,759,995
Peter McCausland	77,121,384	15,367,766

Directors continuing in office after the meeting were: Richard Fairbanks, Samuel J. Heyman, Alan R. Hirsig, Edith E. Holiday, Sunil Kumar, Gloria Schaeffer, Paula A. Sneed, Raymond S. Troubh and Joe B. Wyatt. John G. Drosdick retired from the Board effective April 25,

2002.

2. Ratification of PricewaterhouseCoopers LLP as Independent Accountants, which proposal received more than a majority of the votes necessary for ratification.

For	Against	Abstain
87,593,885	4,300,612	594,653

3. Approval of the extension of the expiration date of the Hercules Incorporated Long Term Incentive Compensation Plan and change in the limit for stock options awarded to any individual, which proposal received more than a majority of the votes necessary for ratification.

For	Against	Abstain
59,583,888	19,028,492	1,318,136

4. Approval of the continued use of the Hercules Incorporated Non-Employee Director Stock Accumulation Plan and the conversion of unused stock options into available shares of restricted common stock, which proposal received more than a majority of the votes necessary for ratification.

For	Against	Abstain
66,232,233	12,218,417	1,479,866

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ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.

(a) Exhibits.

None.

(b) Reports on Form 8-K.

Date of Report	Item No.	Fina
April 29, 2002	5, 7	No

May 20, 2002 5 No

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SIGNATURES

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

HERCULES INCORPORATED

By: /s/ Stuart C. Shears

Stuart C. Shears
Vice President and Treasurer
(Principal Financial Officer and
duly authorized signatory)
August 20, 2002

By: /s/ Fred G. Aanonsen

Fred G. Aanonsen
Vice President and Controller
(Principal Financial Officer and
duly authorized signatory)
August 20, 2002

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