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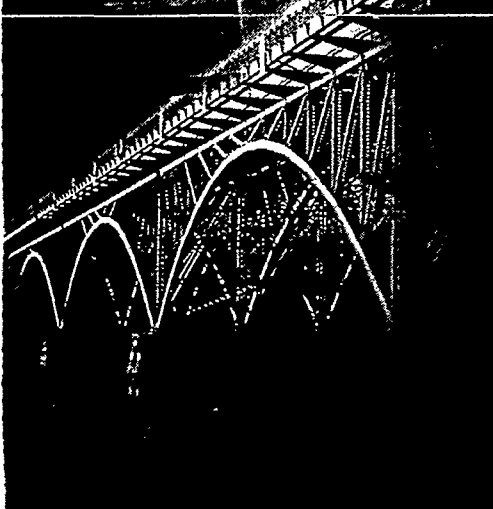
**SOLUTIA**

Applied Chemistry,  
Creative Solutions™

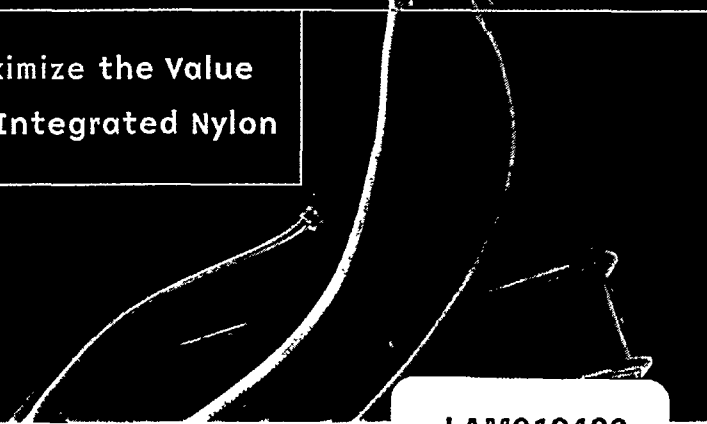
## 2000 ANNUAL REPORT



Expand and Grow  
Performance Films



Aggressively Grow  
Select Specialty  
Products Businesses



Maximize the Value  
of Integrated Nylon

SAR 000252

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## About Our

# BUSINESSES

Solutia is a world-class applied chemistry company. We deliver a wide range of products and services that solve challenging technical problems for our customers or help them seize opportunities in their markets. Our products and services enhance the performance of consumer goods used throughout the world and provide the building blocks needed to deliver on Solutia's growth objectives.

### Solutia's Three Business Platforms

- **Performance Films.** Solutia is the world's largest producer of plastic interlayer for laminated glass used in automotive and architectural applications. The interlayer imparts multiple attributes: improved safety and security, solar protection, energy efficiency and sound reduction. Solutia's interlayer is marketed under the following trademarks: *Saflex*, *KeepSafe*, *Saflex Inside* (in Europe) and *KeepSafe Maximum*. Solutia's CPFilms business is also a leading producer of solar control and safety window films for aftermarket installation on automobile and building windows. The best-selling brands are *Llumar*, *Gila*, *Vista*, and *FormulaOne Performance Automotive Film*. Other products include custom-coated films for electronic displays, and pressure-sensitive adhesives for self-stick postage stamps.
- **Specialty Products.** Solutia is a world leader in resins and additives. We offer a complete product range of performance ingredients for automotive and architectural specialty coatings and products for technical resin applications. Branded products include *Resydrol* waterborne alkyd resins for liquid coatings, *Alftalat* and *Synthacryl* solid resins for powder coatings, and *Resimene* crosslinkers for more durable coatings. Within pharmaceutical services, *CarboGen* and *AMCIS* provide world-class services in support of pharmaceutical drug development. Solutia also makes a wide range of high-performance industrial products for specialized applications, including *Skydrol* aviation hydraulic fluids, *SkyKleen* cleaning solvent, *Therminol* heat transfer fluids and *Dequest* water treatment phosphonates.
- **Integrated Nylon.** Solutia is one of the world's few fully integrated producers of nylon 6,6, from intermediates to polymers, plastics and fibers. Our nylon and acrylic fibers are used to make finished goods such as carpeting, tires, apparel, specialty upholstery and fabrics. Many of Solutia's synthetic fibers are sold under widely recognized brand names such as *Wear-Dated* and *Ultron VIP*. We also produce nylon 6,6 resins, sold under the *Vydyne* and *Ascend* brand names, to the engineered thermoplastic and polymer markets. The intermediates business produces feedstock for Solutia's internal consumption and for sale to other manufacturers.

Solutia is executing a focused three-part portfolio strategy.

Solutia is a market leader in providing quality performance glazing systems for residential, commercial and automotive applications. We have secured a strong foundation for sustainable and profitable growth.

Expand and Grow  
Performance Films

SAR 000253

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For a complete set of consolidated financial statements, please refer to Solutia's annual report on Form 10-K for the year ended December 31, 2000, which can be found in the pocket inside the back cover of this annual report.

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Aggressively Grow  
Select Specialty  
Products Businesses

Solutia's technical expertise and superior product performance allow it to capitalize on changing industry dynamics. We deliver premium customer solutions and services through three specialty businesses: resins and additives, pharmaceutical services and industrial products.

# HIGHLIGHTS

| Dollars in millions, except per share amounts       | 2000    | 1999    | 1998    |
|-----------------------------------------------------|---------|---------|---------|
| Net Sales .....                                     | \$3,185 | \$2,830 | \$2,835 |
| Net Income* .....                                   | \$ 49   | \$ 206  | \$ 249  |
| Diluted Earnings per Share* .....                   | \$ 0.46 | \$ 1.80 | \$ 2.03 |
| Dividends per Share .....                           | \$ 0.04 | \$ 0.04 | \$ 0.04 |
| Depreciation and Amortization .....                 | \$ 191  | \$ 151  | \$ 147  |
| Capital Expenditures .....                          | \$ 221  | \$ 257  | \$ 158  |
| Percent of Total Debt to Total Capitalization ..... | 103%    | 94%     | 101%    |
| Number of Registered Shareholders at Year-End ..... | 36,703  | 39,171  | 41,864  |
| Shares Outstanding at Year-End (in millions) .....  | 102.9   | 109.5   | 112.8   |
| Employees .....                                     | 10,200  | 10,600  | 8,700   |

\*Net income includes net charges for special items of \$74 million, or \$0.68 per share, in 2000, and \$40 million, or \$0.35 per share, in 1999.

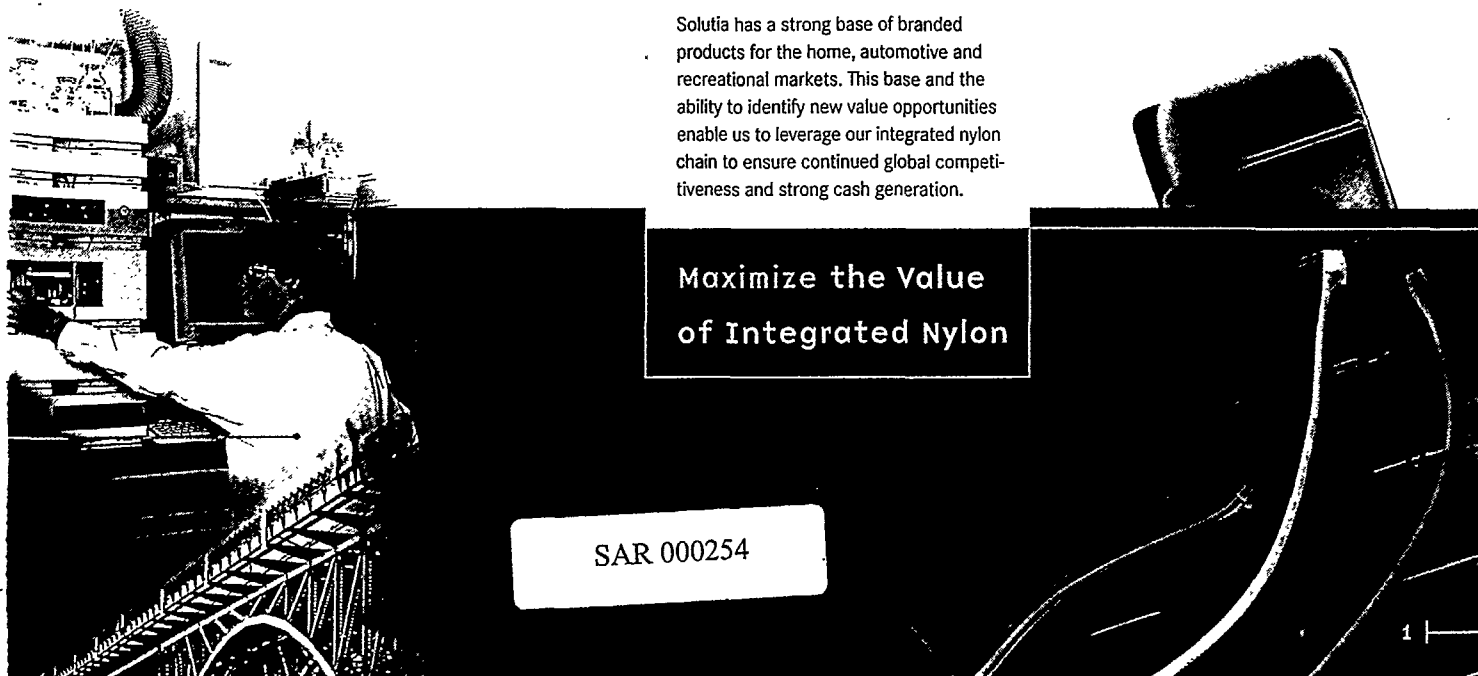
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Solutia has a strong base of branded products for the home, automotive and recreational markets. This base and the ability to identify new value opportunities enable us to leverage our integrated nylon chain to ensure continued global competitiveness and strong cash generation.

**Maximize the Value  
of Integrated Nylon**

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# WE HAVE WHAT IT TAKES

In what proved to be a very challenging year for the chemical industry as a whole, **Solutia continued to make progress on its growth strategy for the future.** However, the economic realities of 2000 were undeniable. Despite increased revenue in 2000, we experienced unprecedented raw material and energy costs, a weak euro, which reduced reported sales and earnings, and weakening demand as the economy began to slow in the fourth quarter. Solutia's employees worked tirelessly, and offset almost half of the impact of these negative factors through aggressive pricing actions and relentless cost management.

The year's global economic realities challenged Solutia to review the company's direction. Out of that review, we created a refined portfolio strategy. It will get us through the difficult times, and set us on a path toward renewed, focused growth. **Our portfolio strategy is as follows:**

- Expand and Grow Performance Films
- Aggressively Grow Select Specialty Products Businesses
- Maximize the Value of Integrated Nylon

In line with our portfolio strategy, we intend to grow *Saflex*, our plastic interlayer product, into expanded automotive and architectural applications and our CPFilms custom-coated films into high-value, high-tech marketplaces. Our Resins and Additives business will grow through geographic expansion, technological innovation and product specialization. Our Pharmaceutical Services business will capitalize on its leadership position to ensure that Solutia is the recipient of increased drug research and development outsourcing. Our Integrated Nylon businesses will support our growth efforts with strong cash generation, while staying healthy and serving their markets.

Our portfolio strategy also will drive every capital decision we make. And as the global economy turns around, Solutia will be better positioned to capitalize on opportunities in the markets we serve.

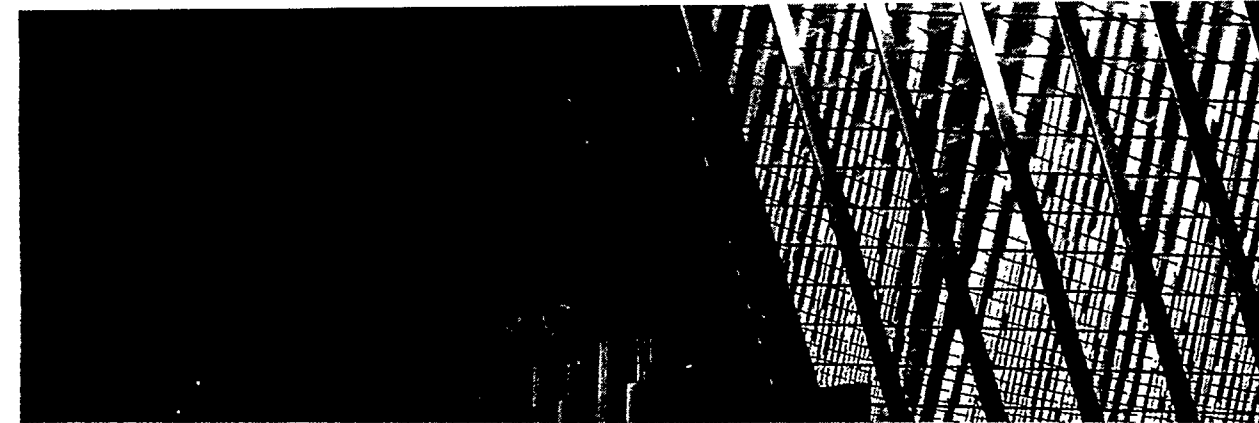
We are gratified by the dedication our employees showed in a challenging year. They remained committed to Solutia's success, and they stayed the course, executing our strategy and delivering results. We are confident that our talented employees, strong global presence, proven technologies, and world-class business systems and processes will drive value for both our employees and our shareholders, fulfilling Solutia's goal of sustainable growth and profitability.

**"We are investing in businesses and technologies with faster growth characteristics, higher margins and higher returns. We are transforming Solutia's growth dynamics and creating bottom-line value for our employees and our shareholders."**

John C. Huhner III  
Chairman, President and  
Chief Executive Officer



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More than 100,000 square meters of laminated glass with Safflex were used in the construction of Shanghai Pudong International Airport.

## BUILDING BLOCKS

With our portfolio strategy as our framework, we are redefining Solutia's value proposition. We are investing in businesses and technologies with faster growth characteristics, higher margins and higher returns. We are transforming Solutia's growth dynamics and creating bottom-line value for our employees and our shareholders.

We work from our long-standing skill base of applied chemistry and creative solutions to influence people's lives in a positive way every day. We offer safer glass for autos and homes, provide environmentally friendly coatings ingredients to paint and coatings manufacturers, and deliver new drug therapies to pharmaceutical companies that serve the expanding global population.

Solutia's position as a market leader provides the platform for us to invest prudently in faster growth. We will remain a global leader in several high-margin, niche markets. We are dedicated to developing attractive new market opportunities and delivering a strong, reliable cash flow to shareholders.

Solutia's employees remained focused during a challenging year. Our people have shown that they have the experience, the confidence, and the resources to innovate, take risks, and quickly respond to rapidly changing global demands.

## SOLUTIA'S SUCCESSES

Our Safflex business gained approval from two North American automotive manufacturers to use Safflex Enhanced Protective Glass (EPG) for the side and rear windows of two, 2003 automotive models.

Our CPFilms solar control products offer premium performance. Their superior color stability comes from internally developed and patented dyeing processes. Precision custom-coated films, principally our extensive range of indium tin oxide products, have contributed significantly to the rapid development of touch-screen computers and display screens on computers and handheld electronics.

Our Resins and Additives business worked to fully integrate its Vianova acquisition into the Solutia portfolio. This business successfully exceeded its cost savings target of \$20 million, while growing revenue and volume. The business is now focusing on delivering further revenue opportunities.

The formation of our Pharmaceutical Services business with the acquisitions of CarboGen and AMCIS, created a full-service, state-of-the-art organization. The businesses provide process research and development, and small-scale manufacturing in support of new drug therapy development. This organization is uniquely positioned to capitalize on the rapid growth of pharmaceutical services outsourcing.

## POSITIONED FOR GROWTH

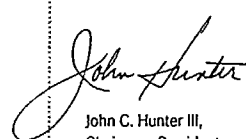
Our Performance Films platform continues to cultivate new opportunities. We see tremendous potential in this platform as more automotive models incorporate EPG, architectural applications continue to expand, custom-coated films applications grow across global markets, and new products are developed from our combined film technologies.

In our Resins and Additives business, the integration of Vianova is exceeding expectations. We now have the most extensive global manufacturing presence and the most comprehensive products portfolio in the market. Our broad offering results in expanded partnerships with our customers and increased value creation.

New drug candidates are being developed at a record pace for an aging population. The demand for cost-effective "quality of life" drugs for such conditions as baldness and obesity contribute to the growing trend in drug therapies as the preferred treatment. Solutia has created a division offering world-class services in support of drug development, process research and small-scale manufacturing. We help pharmaceutical companies screen drug candidates and bring them to consumers more quickly.

The people of Solutia will continue to capitalize on these opportunities. Their talent, determination and enthusiasm will allow us to achieve our vision.

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John C. Hunter III,  
Chairman, President and  
Chief Executive Officer

Michael E. Miller,  
Vice Chairman

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# CASH IS THE TOP PRIORITY

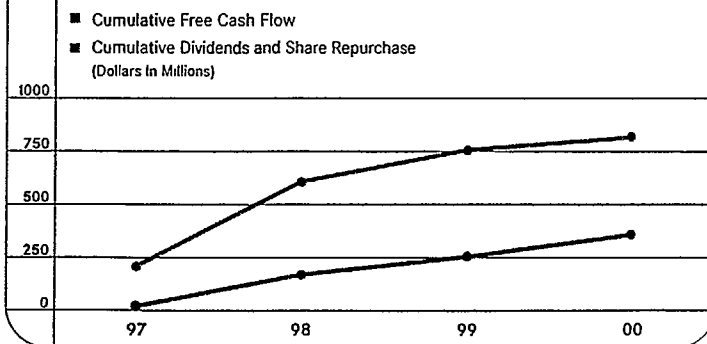
→ Generating healthy amounts of cash and ensuring we are investing that cash responsibly are critical components for increasing the value of your investment in Solutia. Free cash flow, including funds from divestitures, amounted to \$244 million in 2000. Approximately half of the proceeds were used to drive shareholder value in the form of dividends and share repurchases. The remainder of the cash was used to pay down Solutia's debt and to support capital expenditures.

Every cash decision we make, whether it is regarding capital expenditures, debt repayment, dividends, share repurchase or growth strategy investment, will be judged against our **portfolio strategy**:

- Expand and Grow Performance Films
- Aggressively Grow Select Specialty Products Businesses
- Maximize the Value of Integrated Nylon

Although we fully expect cash generated by our operations to remain strong, we are also dedicated to generating cash from other sources. We will continue to prune from our portfolio the assets that do not fit our portfolio strategy. In addition, we remain intensely focused on managing Solutia's businesses for stronger cash generation.

## CASH GENERATION AND VALUE RETURNED TO SHAREHOLDERS



1997 figures represent activity from 9/01/97 through 12/31/97

The evolution of our business mix and its improved growth dynamics will enhance cash generation and increase the value of your investment in Solutia.

William A. ...  
Solutia's President and Chief Executive Officer





Our state-of-the-art facilities and people are positioned to capitalize on the pharmaceutical industry's outsourcing of process research, process development and small-scale manufacturing.

## RESHAPING OUR PORTFOLIO

As we added higher-growth businesses to our portfolio, we have restructured or sold other businesses to help fund these acquisitions. The evolution of our business mix and its improved growth dynamics will enhance cash generation and increase the value of your investment in Solutia.

In April, we formed a 50-50 joint venture with FMC Corporation to manufacture and market phosphorus-based products. It was incorporated as Astaris LLC. Solutia was able to extract working capital and an attractive dividend from the new venture.

In June, Solutia sold its Polymer Modifiers business to Ferro Corporation. The sale generated more than \$100 million in cash.

In September, we sold the Light Denier Industrial nylon fibers business to South African Nylon Spinners. This sale was a valuable opportunity to exit a business that did not warrant further cash investment by Solutia.

The year's successful transactions have positioned Solutia for even faster, more focused growth. To complement our growth, we continue to look for modest, value-enhancing acquisitions. Future acquisitions will broaden our growth opportunities and allow our businesses to deliver improved margins and more reliable cash generation.

## FOCUSED ON CASH

Performance Films continues to reduce costs and working capital through manufacturing and supply chain excellence. Process improvements and manufacturing quality have both produced more value from the businesses in this platform.

In Resins and Additives, the integration of Vianova is exceeding expectations for revenue and cost savings synergies. The implementation of integrated resource software also is helping to optimize costs worldwide.

During 2000, the Integrated Nylon chain reduced costs and eliminated bottlenecks to deliver cost-competitive materials to a global marketplace. Future investment will be focused on maintaining the health of the business while increasing cash generation.

Throughout Solutia, our employees and our processes are poised to deliver innovative solutions for producing and delivering products and services to our expansive customer base. For example, we are improving employee training and leveraging our enterprise software, enabling Solutia to more fully integrate the management of our supply chain. This puts us in position to set new standards in cost containment, inventory control and customer service.

## DELIVERING VALUE

Portfolio transformation provided funds for continued share repurchases and debt repayment. Under the current share repurchase authorizations, Solutia repurchased 7.7 million shares in 2000 at a cost of \$106 million. Since becoming a public company in 1997, we have repurchased 17.7 million of our outstanding shares at a total cost of approximately \$345 million.

In 2000, Solutia managed its debt level to maintain attractive debt ratings. Favorable ratings facilitate the sale of debt securities and the issuance of commercial paper in both the United States and Europe.

We have streamlined our portfolio strategy into three components. We believe that this strategy will allow us to deliver greater value from our businesses.

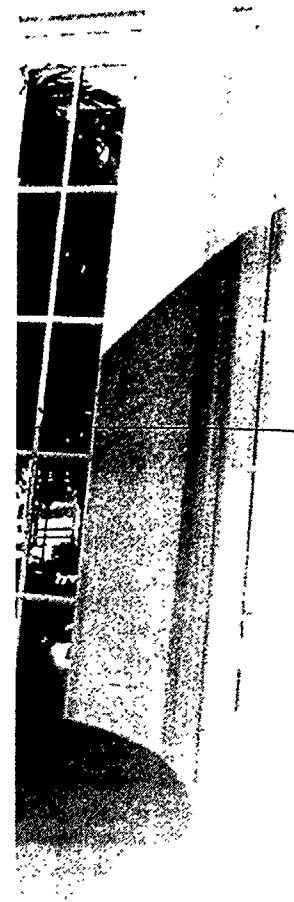
This simplified strategy sharpens management focus and contributes to a clearer understanding of Solutia among investors, employees and customers. We are committed to this portfolio strategy. We believe it holds the power to streamline our business decisions and deliver improved cash generation.

After reading the following pages, we think you will agree that our strategy will create dynamic growth and deliver bottom-line value.

Expand and Grow

## PERFORMANCE FILMS

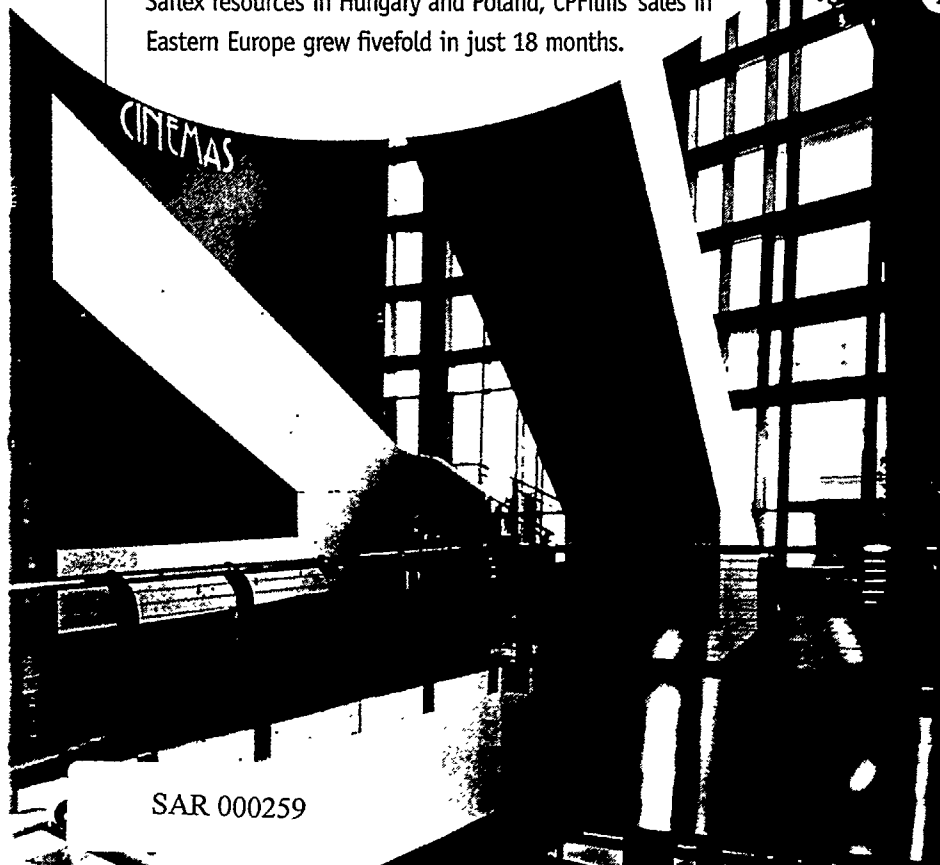
- **We are touching lives every day** with our *Saflex* and CPFilms brand products, which increase the safety, security and comfort of your office, home and automobile. You can even find our products at your local automated bank teller machine. Our custom-coated films make the touch-screen possible. Our leadership and attention to quality in performance-glazing systems provide a strong foundation for continued growth in this business segment.
- **Our passion for innovation** is reflected in *Saflex HP* (High Performance), a product that allows Solutia to provide enhanced window systems for large, commercial applications in hurricane-prone areas. Throughout the Performance Films segment, we continue to improve supply chain management with fully integrated software, process improvements and leading-edge e-business techniques. These innovations bring us closer to our customers, who benefit from the enhanced value of interconnecting supply chains.
- **We are using our global market leadership** to expand our expertise into new applications and new geographies. By combining the technology, facilities and resources of *Saflex* and CPFilms, we deliver broader product and service offerings to our customers, and generate faster growth and higher margins for ourselves. For example, with the help of the *Saflex* resources in Hungary and Poland, CPFilms' sales in Eastern Europe grew fivefold in just 18 months.



### SAFLEX

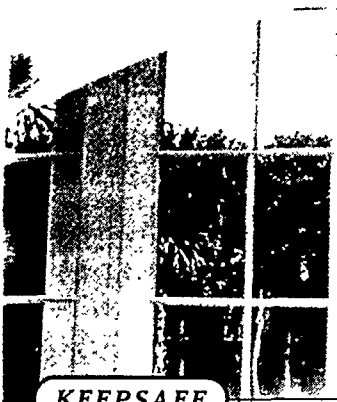
Moviegoers who enter this new cinema in Miami Beach are greeted by a 42-foot-high block wall of multi-colored laminated glass made with *Saflex* plastic interlayer. Sunlight passing through the glass transforms the atrium into a cascading kaleidoscope of color. The beauty of the structure is breathtaking, and the safety properties of laminated glass made with *Saflex* were essential to meet stringent building codes in coastal Florida.

Since the introduction of *Saflex HP*, many commercial building designs that require massive window areas now specify glass laminated with *Saflex*. This product not only brings tremendous opportunity to the *Saflex* business, but it also delivers security, safety, sound control, energy efficiency, and protection from ultraviolet rays to every application.



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### KEEPSAFE

KeepSafe glass with Saflex (sold in Europe as Saflex Inside) is used in residential windows primarily for intrusion resistance. But the product offers other valued benefits as well: sound reduction, safety, energy efficiency and ultraviolet protection. Laminated glass provides a tough layer of passive protection without compromising your home's aesthetics.

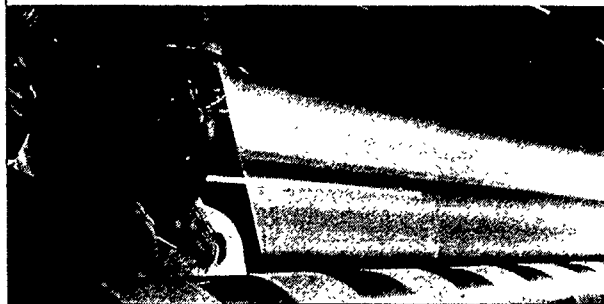
Saflex's extra-strength glass, *KeepSafe Maximum*, can withstand hurricane-force winds up to 110 mph. That meets the stringent new building codes adopted in Florida and South Carolina. These stronger codes represent a significant opportunity for increased penetration of *KeepSafe Maximum* into architectural window systems.

### CPFILMS

CPFilms' indium tin oxide, custom-coated products leverage proprietary technologies to expand applications for transparent, conductive and anti-reflective coatings. These coatings are used on computer touch-screens, cellular telephone displays, electronic organizers and watches. The market is growing by more than 60 percent annually.

Solutia is investing in this explosive growth. New production capacity for vacuum sputter custom-coated films was brought on line in early 2000 to ensure that CPFilms remains a leader in these markets.

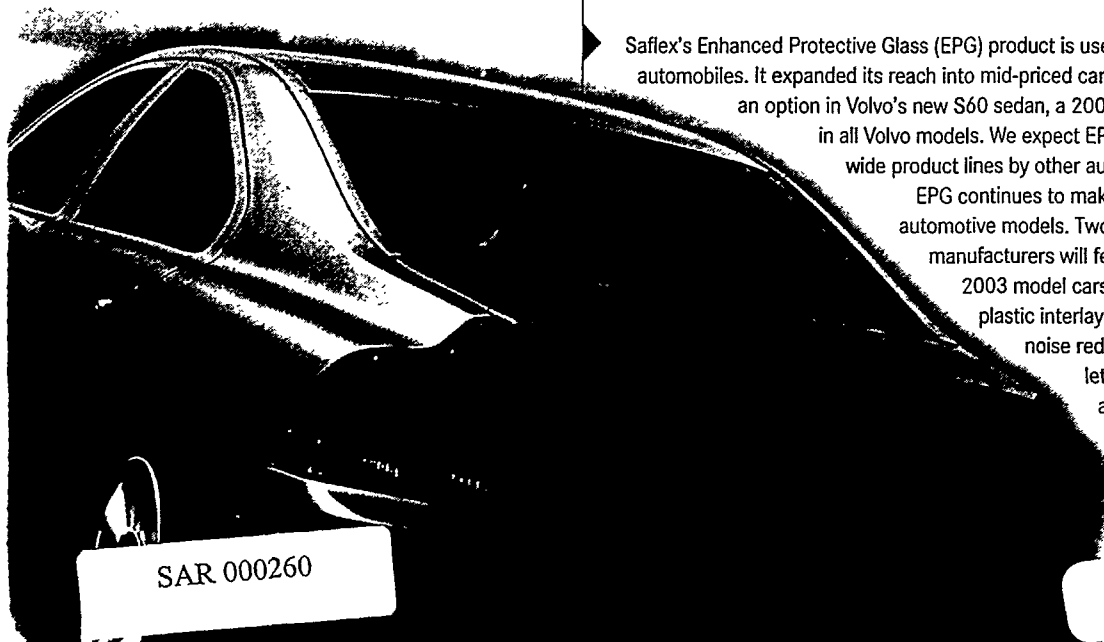
CPFilms also makes a wide range of residential, commercial and automotive window films that help increase safety, reduce glare and heat from sunlight, and minimize the damage caused by ultraviolet rays. These products can be found under the brands *Vista*, *Llumar*, *Gila* and *FormulaOne Performance Automotive Film*.



### ENHANCED PROTECTIVE GLASS

Saflex's Enhanced Protective Glass (EPG) product is used in side and rear windows of automobiles. It expanded its reach into mid-priced car models when it was offered as an option in Volvo's new S60 sedan, a 2001 model. EPG is now an option in all Volvo models. We expect EPG to be used throughout worldwide product lines by other automakers, too.

EPG continues to make strides in its adoption into new automotive models. Two North American automotive manufacturers will feature the product in two of their 2003 model cars. The strong polyvinyl butyral plastic interlayer provides intrusion resistance, noise reduction, protection from ultraviolet rays, improved solar control, and increased protection from occupant ejection in accidents and vehicle rollovers.



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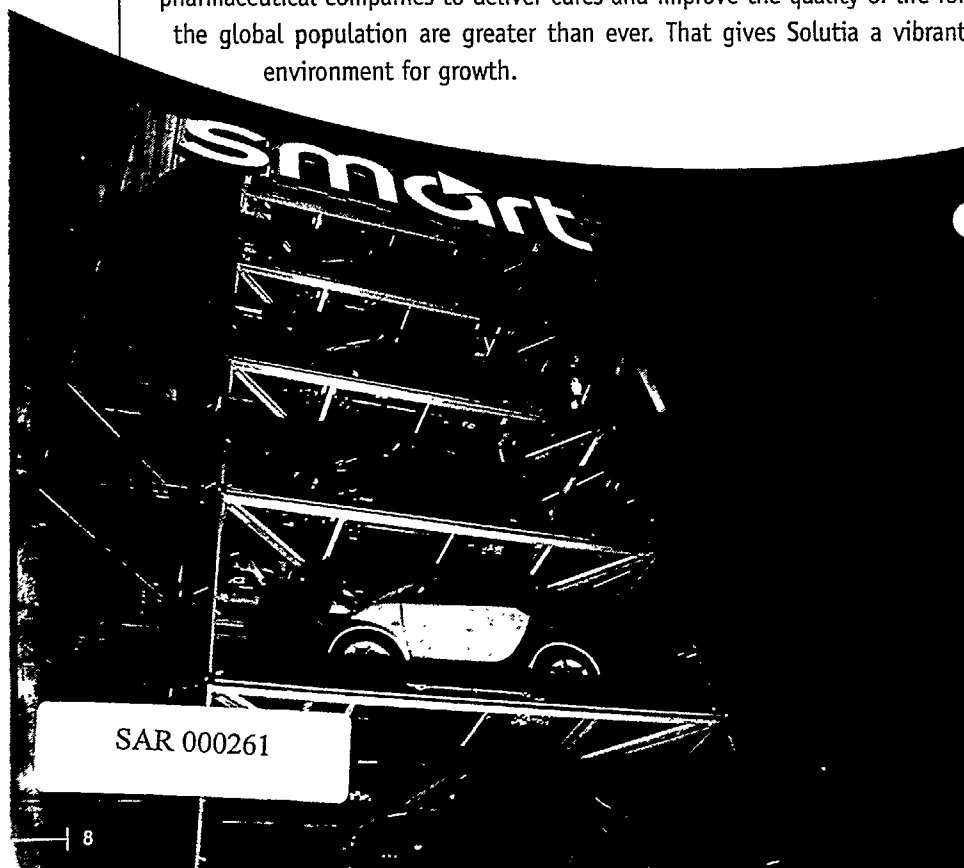
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**Aggressively Grow Select**

## **SPECIALTY PRODUCTS**

### **Businesses**

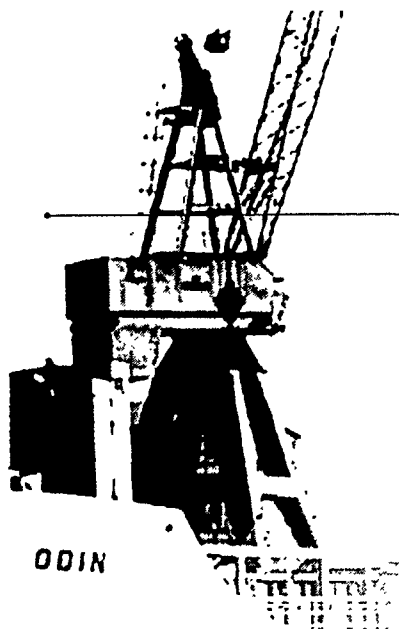
- **Geographic expansion, technical development, coatings specialization, and industry consolidation** are the forces driving strong growth in the Resins and Additives business. Solutia's technical expertise positions it to capitalize on these trends and become a preferred supplier to a growing global customer base. Our coatings solutions, superior product performance, and value-added technical service make it easy for customers to choose to outsource a larger portion of their specialized coatings needs to Solutia's Resins and Additives business.
- **Technical expertise is critical to growth** in performance coatings ingredients. Environmentally friendly waterborne and powder resins offer high-margin opportunities in specialty products, which have greater performance characteristics and deliver more value to customers. Today's end-users expect long-lasting, durable finishes and enhanced appearance — hardware that doesn't tarnish, appliances that don't chip, cars and shipping containers that don't rust. Solutia is focused on delivering complex technical solutions to its customers.
- **State-of-the-art resources** in our newly formed Pharmaceutical Services business enable CarboGen and AMCIS to provide value to pharmaceutical customers. We provide know-how, expeditious research and process development in the early stages of molecule screening for drug therapies. The demands on pharmaceutical companies to deliver cures and improve the quality of life for the global population are greater than ever. That gives Solutia a vibrant environment for growth.



#### **WATERBORNE RESINS**

A vertical showroom encased in laminated glass displays the Smart Car, a mini-car aimed at the European youth market. Designed by Swatch and built by Daimler-Chrysler, the Smart Car features an all-plastic body in bright colors. Solutia's environmentally friendly waterborne coatings ingredients allow paint to adhere well to the plastic body panels, and provide a durable finish. Continued development of coatings technology gets Solutia in on the ground floor of new applications, as we meet the increasing performance expectations of our customers and their end-users.

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ODIN

## LIQUID RESINS

Broad experience in liquid coatings resins enables Solutia to deliver innovative and cost-effective package solutions to meet almost any challenge. Our customers want help with the harsh weather and saltwater conditions that shipping containers and ocean-going vessels face. Solutia, a technology leader in liquid resins that enable coatings to withstand the harshest environments, offers coatings ingredients that provide better protection and longer life for our customers' products.

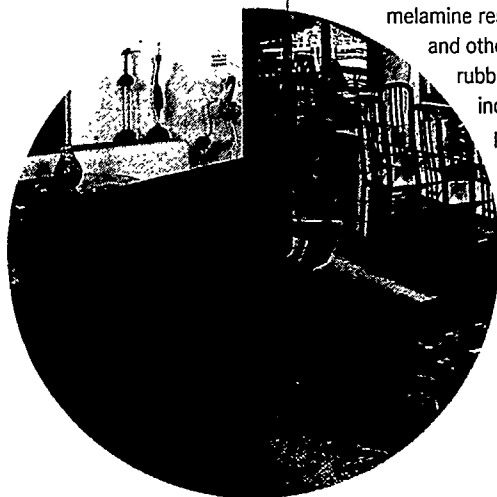


## PHARMACEUTICAL SERVICES

With state-of-the-art analytical capabilities and leading-edge researchers, Solutia helps pharmaceutical companies reduce development time and deliver drug therapies to market more quickly. The stakes are high, as the reward for getting new products to market first can be as much as \$1 million a day in increased revenue. With the need for increased speed also comes a need for experience and precision – key qualities offered by Solutia's CarboGen and AMCIS. The two companies have been instrumental in supporting the outsourcing revolution in drug development for the last 20 years.

## TECHNICAL RESINS

Solutia is one of the leading suppliers of technical melamine resins, frequently used for binding and other applications in the wood finishing, rubber, paper, textile and electronic industries. Our strong competitive position makes it possible for Solutia to deliver quality, expert technical service and product reliability.



SAR 000262

## POWDER COATINGS

Solutia is a market leader in polyester resins for powder coatings, a rapidly growing segment of the industrial finishing market. Environmentally friendly powder coatings, which are used on everything from power tools to appliances, and bicycles to heavy equipment, eliminate the need to apply coatings with solvents.

Superior performance and quality characteristics have propelled growth for powder coatings. An increasing number of coatings processors are adopting this preferred technology. Solutia's Romano d'Ezzelino, Italy, plant is one of the world's largest and most cost-effective producers of resins for powder coatings.



Maximize the Value of

## INTEGRATED NYLON

- A strong base of brands, including *Vydyne*, *Ascend*, *Ultron VIP*, *Wear-Dated*, *Wear-Dated ThermoSealed* and *Pet-Agree*, gives Solutia a foundation for increasing its branded presence in the global marketplace. Solutia's superior nylon 6,6 has been part of consumers' homes and daily activities for years. It is used in everything from air bags to specialty upholstery and carpet to engineered thermoplastic molded auto parts.
- Delivering value for end-users by finding new applications is a strong suit of the Integrated Nylon businesses. Solutia is working in partnership with customers to develop products for customer-specific needs. The *Ascend* nylon group has uncovered significant market opportunities in which *Ascend* offers processors greater value from more flexible manufacturing.
- As the market leader in many of its product lines, the Integrated Nylon businesses were able to pass along price increases to partially offset the unprecedented rise in critical raw material and energy costs we experienced in 2000. Our aggressive cost management, engineering and manufacturing excellence, and pricing actions continue to ensure that we remain a globally competitive supplier.

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### ENGINEERED THERMOPLASTICS

*Vydyne* engineered thermoplastic molding resins are used in a wide range of automotive components. Because of *Vydyne*'s superior strength and heat-resistance, it is used in many under-the-hood automobile components, including air filter housings, intake manifolds, valve covers, reservoirs, fan shrouds and fuel lines. Marketed and sold through an alliance with Dow Chemical Co., *Vydyne* is being specified in a growing number of applications.

### WEAR-DATED CARPET

*Wear-Dated* carpet has been a staple floor covering in residential applications for years. It offers superior stain and fade resistance as well as exceptional bounce-back wear characteristics.



Commercial applications of our nylon 6,6 staple and bulk continuous fiber can be found in many applications. This brightly colored carpeting made with *Ultron VIP* nylon is at the new headquarters of OurHouse.com in suburban Chicago. Solutia's product was a critical element in this innovative design. Our market-leading fiber lets carpet manufacturers combine performance with popular colors, textures and styles.

### INTERMEDIATES

Solutia produces the building block chemicals of the nylon chain, providing our company with a competitive edge through economies of scale and predictability of supply. We are one of the few companies in the world with a fully integrated infrastructure for manufacturing nylon. Solutia strengthened its position in 2000 with a new acrylonitrile facility in Texas, which supplies internal needs as well as the needs of three key customers. The facility doubles Solutia's production capacity of acrylonitrile, an important ingredient in nylon carpet, acrylic fibers and various nylon plastics and polymers.

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## Key Financial

# STATISTICS

Dollars in millions, except per share amounts

|                                                                                                                                                  | 2000     | 1999    | 1998   |
|--------------------------------------------------------------------------------------------------------------------------------------------------|----------|---------|--------|
| <b>Working Capital</b><br>(Current assets less current liabilities).....                                                                         | \$ (334) | \$(213) | \$ 259 |
| <b>Current Ratio</b><br>(Current assets divided by current liabilities).....                                                                     | 0.8      | 0.8     | 1.4    |
| <b>Trade Receivables—</b><br><b>Days' Sales Outstanding<sup>(1)</sup></b><br>(Average receivables divided by net sales times 365 days).....      | 50       | 49      | 50     |
| <b>Inventory Turnover Ratio<sup>(2)</sup></b><br>(Cost of goods sold divided by inventory).....                                                  | 7.2      | 7.1     | 6.3    |
| <b>Interest Coverage Ratio</b><br>(Income before interest expense and income taxes divided by total interest cost).....                          | 1.2      | 6.5     | 8.5    |
| <b>Cash From Operations/Total Debt<sup>(3)</sup></b> .....                                                                                       | 19%      | 54%     | 90%    |
| <b>Total Debt/Total Capitalization</b><br>(Total capitalization equals the sum of short-term debt, long-term debt and shareholders' equity)..... | 103%     | 94%     | 101%   |

<sup>(1)</sup> Days' Sales Outstanding for the 2000 period was adjusted to exclude trade receivables associated with the Polymer Modifiers business sold in the third quarter of 2000, and the Phosphorus Derivatives business contributed to the Astaris joint venture in the second quarter of 2000. Days' Sales Outstanding for the 1999 period was adjusted to include trade receivables purchased in the May 1999 acquisition of CPFilms, to annualize net sales derived from CPFilms, and to exclude trade receivables purchased in the December 1999 acquisition of Vianova Resins.

<sup>(2)</sup> Inventory Turnover Ratio for the 2000 period was adjusted to exclude cost of goods sold associated with the Polymer Modifiers business sold in the third quarter of 2000, and the Phosphorus Derivatives business contributed to the Astaris joint venture in the second quarter of 2000. Inventory Turnover Ratio for the 1999 period was adjusted to annualize CPFilms' cost of goods sold, and to exclude inventories purchased in the December 1999 acquisition of Vianova Resins.

<sup>(3)</sup> Cash from Operations/Total Debt for 1999 was adjusted to exclude debt associated with the December 1999 Vianova Resins acquisition.

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## SHARE DATA

|                                                                     | 2000    | 1999    | 1998    |
|---------------------------------------------------------------------|---------|---------|---------|
| <b>Diluted Earnings per Share</b> .....                             | \$ 0.46 | \$ 1.80 | \$ 2.03 |
| <b>Common Stock Price:</b>                                          |         |         |         |
| High.....                                                           | 17.19   | 26.31   | 32.00   |
| Low.....                                                            | 10.38   | 13.50   | 18.69   |
| Close.....                                                          | 12.00   | 15.44   | 22.38   |
| <b>Price/Earnings Ratio</b><br><b>on Year-end Stock Price</b> ..... | 26      | 9       | 11      |
| <b>Dividends per Share</b> .....                                    | \$ 0.04 | \$ 0.04 | \$ 0.04 |
| <b>Other Share Data:</b>                                            |         |         |         |
| Number of registered shareholders.....                              | 36,703  | 39,171  | 41,864  |
| Year-end shares outstanding (in millions).....                      | 102.9   | 109.5   | 112.8   |
| Shares repurchased (in millions).....                               | 7.7     | 3.8     | 6.2     |
| Average daily share trading volume (in thousands).....              | 518     | 458     | 401     |

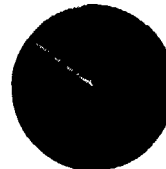
### Capital Expenditures by Operating Segment

- 12% Performance Films
- 13% Specialty Products
- 62% Integrated Nylon
- 13% Unallocated



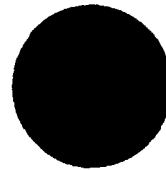
### Capital Expenditures by World Area

- 85% United States
- 13% Europe-Africa
- 2% Other

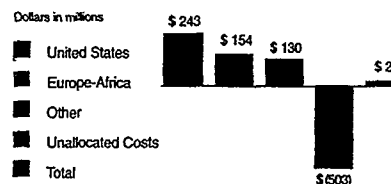


### Net Sales by World Area

- 61% United States
- 25% Europe-Africa
- 14% Other

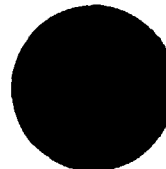


### Operating Income by World Area



### 2000 Shareholder Composition

- 59% U.S. Institutions
- 18% Brokers
- 12% Employee Plans
- 6% Individuals
- 4% Banks
- 1% Directors & Officers



Based upon estimated information provided by EquiServe.

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# INFORMATION

### STOCK LISTING

Solutia's stock is traded principally on the New York Stock Exchange. Our stock symbol is SOI.

### DIVIDEND POLICY

The declaration and payment of dividends is made at the discretion of Solutia's Board of Directors. The Board anticipates that its current dividend policy, 4 cents/year, paid annually in December, will remain unchanged for the foreseeable future. Solutia also uses its share repurchase program as an additional means of returning net income to shareholders.

### DIVIDEND REINVESTMENT PLAN

Solutia shareholders who wish to have their dividends automatically reinvested in Solutia common stock may choose to enroll in the Dividend Reinvestment Plan (DRIP). To receive a DRIP brochure that explains the details of the plan, please contact EquiServe as noted in the section that follows.

### SHAREHOLDER SERVICES

EquiServe, our transfer agent, can help you with a variety of shareholder-related services, including:

- Change of address
- Lost stock certificates
- Transfer of stock to another person
- Dividend checks
- Dividend reinvestment plan
- Additional matters pertaining to your account

You can call our transfer agent toll-free at: (888) 987-6588 (from the United States or Canada).

You can also write or send an e-mail to: EquiServe  
P.O. Box 2500  
Jersey City, NJ 07303-2500  
[www.equiserve.com](http://www.equiserve.com)

### ADDITIONAL INFORMATION

You can access financial and other information, such as significant news releases, Forms 10-K and 10-Q, and the text of this annual report on the Internet at <http://Investor.Solutia.com>.

We also will send financial information such as Forms 10-K and 10-Q free of charge if you call us at (314) 674-4520 or send a request in writing to:

Solutia Inc.  
Investor Relations, 3N  
P.O. Box 66760  
St. Louis, MO 63166-6760

We post our quarterly earnings conference calls on the Internet for approximately five days after our earnings announcement. To listen to them, please visit the investor section of our home page at <http://Investor.Solutia.com>.

### ANNUAL MEETING

The annual meeting of Solutia's shareholders will be held on Wednesday, April 25, 2001, at 1:45 p.m., at St. Louis Marriott West Hotel, 660 Maryville Centre Drive, St. Louis, MO 63141.

A formal notice of the meeting and a proxy statement are being mailed to shareholders.

### CAUTIONARY STATEMENT

This annual report contains forward-looking statements that involve risks and uncertainties. Solutia's actual results may differ materially from those anticipated in these forward-looking statements. Please see page 1 of Solutia's annual report on Form 10-K for the year ended December 31, 2000, as filed with the Securities and Exchange Commission and included in the pocket of this annual report, for important risk factors that could cause actual results to differ from those contained in the forward-looking statements. These factors include general economic, business and market conditions; customer acceptance of new products; efficacy of new technology and facilities; ability to acquire and integrate new businesses; changes in U.S. and foreign laws and regulations; shortages and pricing of raw materials and energy; currency fluctuations; ability to implement cost-reduction initiatives in a timely manner; exposure to product liability and other litigation; cost of environmental remediation; and increased competitive and/or customer price pressure.

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### EXECUTIVE OFFICERS

**Karl R. Barnickol**  
Senior Vice President,  
General Counsel and Secretary

**Russell J. Belle**  
Vice President and General  
Manager, Industrial Products

**Robert A. Clausen**  
Senior Vice President and  
Chief Financial Officer,  
Advisory Director

**Sheila B. Feldman**  
Vice President, Human Resources  
and Public Affairs

**John J. Ferguson**  
Senior Vice President,  
Integrated Nylon

**Johnnie M. Foster**  
Vice President and  
Chief Information Officer

**G. Bruce Greer, Jr.**  
Vice President, New Ventures  
and Digital Strategy

**Sharon A. Henry**  
Vice President, Joint Ventures  
and Operating Agreements

**Bradley W. Hill**  
Vice President, Sales,  
Integrated Nylon

**Vicki M. Holt**  
Vice President and General  
Manager, Performance Films

**James E. Howard**  
Vice President, Marketing,  
Integrated Nylon

**John C. Hunter III**  
Chairman, President and  
Chief Executive Officer

**Todd B. Imhoff**  
Vice President, Corporate Services

**Michael E. Miller**  
Vice Chairman

**Edward R. Robinson**  
Vice President and General  
Manager, Pharmaceutical Services

**Glenn S. Ruskin**  
Vice President, Public Affairs

**John F. Saucier**  
Vice President, Strategy and  
Corporate Development

**James M. Sullivan**  
Vice President and Controller

**Robert B. Toth**  
Vice President and General  
Manager, Resins and Additives

**C. Kevin Wilson**  
Vice President and Treasurer

\*Executive Officers as defined by the U.S. Securities and Exchange Commission

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## Board of

# DIRECTORS

**John C. Hunter III**

54, Chairman, President, and Chief Executive Officer, Solutia. He also serves as a director of Penford Corporation and Missouri Baptist Hospital.

**Michael E. Miller**

59, Vice Chairman, Solutia. He also serves as a director of Watlow Electric Manufacturing Company and Alpha Technologies and as a trustee of Fontbonne College.

**Robert T. Blakely<sup>1</sup>**

59, Executive Vice President and Chief Financial Officer, Lyondell Chemical Company. He also serves as a director of Vlastic Foods International Inc. and as a trustee of Cornell University.

**Paul H. Hatfield<sup>2</sup>**

65, Principal, Hatfield Capital Group. He also serves as a director of Penford Corporation and Maritz, Inc.

**Robert H. Jenkins<sup>2,3</sup>**

58, retired Chairman of the Board and Chief Executive Officer, Sundstrand Corporation. He serves as a director of AK Steel Holdings Corporation, CLARCOR Inc., Pella Corporation, Sentry Insurance, and Visteon Corporation.

**Frank A. Metz, Jr.<sup>1,2</sup>**

67, retired Senior Vice President, Finance and Planning, and Chief Financial Officer, International Business Machines Corporation. He serves as a director of Allegheny Energy, Inc.

**J. Patrick Mulcahy<sup>1</sup>**

57, Chief Executive Officer and director, Energizer Holdings, Inc.

**Sally G. Narodick<sup>1</sup>**

55, educational technology and e-learning consultant. She also serves as a director of Penford Corporation, Puget Sound Energy, Inc., and click2learn.com, inc.

**William D. Ruckelshaus<sup>1</sup>**

68, Strategic Partner, Madrona Venture Fund, and Principal, Madrona Investment Group, L.L.C. He also serves as a director of Coinstar, Inc.; Cummins Engine Co., Inc.; Nordstrom, Inc.; Pharmacia Corporation; and Weyerhaeuser Company.

**John B. Slaughter<sup>1,2</sup>**

66, President and Chief Executive Officer, The National Action Council for Minorities in Engineering (NACME), Inc. He also serves as a director of International Business Machines Corporation and Northrop Grumman Corp.

**SECRETARY****Karl R. Barnickol**

59, Senior Vice President, General Counsel, and Secretary, Solutia

**ADVISORY DIRECTOR****Robert A. Clausen**

56, Senior Vice President and Chief Financial Officer, Solutia

<sup>1</sup>Audit and Finance Committee

<sup>2</sup>Executive Compensation and Development Committee

<sup>3</sup>Governance Committee

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Solutia Inc.  
575 Maryville Centre Drive  
P.O. Box 66760  
St. Louis, Missouri 63166-6760  
(314) 674-1000  
[www.solutia.com](http://www.solutia.com)

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10 percent postconsumer fiber

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2000  
Form 10-K

10-K

SAR 000270

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2000

OR

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

Commission file number 001-13255

**SOLUTIA INC.**

(Exact name of Registrant as specified in its charter)

DELAWARE

(State or Other Jurisdiction of  
Incorporation or Organization)

43-1781797

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

575 MARYVILLE CENTRE DRIVE, P.O. BOX 66760, ST. LOUIS, MISSOURI

(Address of Principal Executive Offices)

63166-6760

(Zip Code)

(314) 674-1000

Registrant's Telephone Number, Including Area Code

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

Title of Each Class

\$01 Par Value Common Stock  
Preferred Stock Purchase Rights

Name of Each Exchange  
on Which Registered

New York Stock Exchange  
New York Stock Exchange

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

None

(Title of class)

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

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

State the aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant: approximately \$1.36 billion as of the close of business on February 26, 2001.

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date: 103,419,837 shares of common stock, \$.01 par value, outstanding as of the close of business on February 26, 2001.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of Solutia Inc.'s Notice of Annual Meeting of Stockholders and Proxy Statement dated March 15, 2001 (Part III of Form 10-K).

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## CAUTIONARY STATEMENT ABOUT FORWARD-LOOKING STATEMENTS

We make statements in this Annual Report on Form 10-K that are considered forward-looking statements under the federal securities laws. We consider all statements about the following to be forward-looking statements:

- our expected future financial position, liquidity, results of operations and cash flows;
- dividends;
- financing plans;
- business strategy;
- budgets;
- projected cost reductions;
- plans and objectives of management for future operations;
- competitive position;
- growth opportunities for existing products;
- price increases;
- benefits from new technology; and
- share repurchases.

These statements are not guarantees of our future performance. They represent our estimates and assumptions only on the date we made them. There are risks, uncertainties and other important factors that could cause our actual performance or achievements to be materially different from those we may project. These risks, uncertainties and factors include:

- customer acceptance of new products;
- efficacy of new technology and facilities;
- general economic, business and market conditions that affect us because some of our customers are in cyclical businesses;
- changes in U.S. and foreign laws and regulations;
- exposure to product liability and other litigation and cost of environmental remediation;
- shortages or pricing of raw materials and energy;
- currency fluctuations;
- ability to acquire and integrate new businesses;
- lower prices for our products or a decline in our market share due to competition or price pressure by customers; and
- ability to implement cost reduction initiatives in a timely manner.

## PART I

### Item 1. BUSINESS.

Solutia Inc. and its subsidiaries produce and market a variety of high performance chemical-based materials. Solutia's strategic focus is built on key strengths, including:

- Complex manufacturing capabilities;
- Process engineering expertise;
- Technical service;
- Customer problem solving;
- Polymer chemistry; and
- Fiber technology.

We use these world-class skills to create solutions and products for customers in the consumer, household, automotive, industrial products and pharmaceutical industries. Solutia's products and services include:

- SAFLEX® plastic interlayer, used to make laminated glass for automotive and architectural applications; LLUMAR® and VISTA® window films; and industrial films;
- RESYDROL® waterborne resins, ALFTALAT® and SYNTHACRYL® powder resins, RESIMENE® amino crosslinkers and MODAFLOW® flow and leveling agents, used to produce high-performance coatings for various products such as automobiles, bicycles, bridges and compact discs;

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- Process research and development and small scale-up manufacturing in support of new chemical entity development in the pharmaceutical industry; and
- VYDYNE® and ASCEND® nylon polymers; chemical intermediates; and nylon fibers such as WEAR-DATED® and ULTRON VIP®.

Solutia was incorporated in Delaware in April 1997 as a wholly-owned subsidiary of the former Monsanto Company (now known as Pharmacia Corporation). By September 1, 1997, most of Monsanto's chemical businesses were transferred to Solutia. On that date, Monsanto distributed all of the outstanding shares of Solutia common stock as a dividend to Monsanto's stockholders, and Solutia became an independent publicly-held company. This event is referred to in this document as the "spinoff."

#### **Recent Developments**

During 2000, Solutia refined its portfolio strategy to:

- Expand and grow its Performance Films segment;
- Aggressively grow select Specialty Products businesses; and
- Maximize the value of its Integrated Nylon segment.

During the first quarter of 2000, Solutia completed the acquisition of two companies that provide custom process and technology services to the global pharmaceutical industry. The first was CarboGen Holdings AG on February 10, 2000. CarboGen is a leading process research and development firm. The second was AMCIS AG on March 24, 2000. AMCIS develops production processes and manufactures active ingredients for clinical trials and small-volume commercial drugs. The combined purchase price for these acquisitions was approximately \$118 million.

In April 2000, Astaris LLC, a joint venture between Solutia and FMC Corporation, officially started operations to manufacture and market phosphorus chemicals. Solutia contributed its Phosphorus Derivatives business to the joint venture in exchange for a 50 percent ownership share. Net assets contributed to the venture totaled approximately \$87 million. See "Principal Equity Affiliates" on page 6 below.

During the third quarter of 2000, Solutia completed the sale of its Polymer Modifiers business and related manufacturing facilities to Ferro Corporation for approximately \$130 million. As a result of this transaction, Solutia recognized a \$73 million pretax gain (\$46 million aftertax). Solutia's results of operations for the nine months ended September 30, 2000, included net sales of approximately \$93 million and operating income of approximately \$16 million, from the Polymer Modifiers business.

In December 2000, Solutia's Board of Directors approved cost reduction initiatives that are expected to achieve \$100 million in annual savings. These cost savings will result from a smaller senior management team, efficiencies realized from the implementation of enterprise-wide systems in support of improved work design processes, work force reductions and the streamlining of operations primarily within the Integrated Nylon segment. Approximately 50 percent of these savings are expected to be achieved in 2001, with the full amount achieved in fiscal year 2002.

#### **Segments; Principal Products**

For 2000, Solutia reported its business under three segments:

- Performance Films;
- Specialty Products; and
- Integrated Nylon.

The tabular and narrative information contained in Note 16 of "Notes to Consolidated Financial Statements" appearing on pages 49 through 51 is incorporated by reference into this section.

## Performance Films Segment

| Major End-Use Markets             | Major Products                                                                                                                                                                             | Major End-Use Products & Applications                                                                                                                                                                                                  | Major Competitors                                                                  | Major Raw Materials                                                                  | Major Plants                                                   |
|-----------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------|----------------------------------------------------------------|
| Construction and Home Furnishings | Polyvinyl butyral for KEEPSAFE®, SAFLEX INSIDE® (used in Europe), and KEEPSAFE MAXIMUM® laminated window glass; LLUMAR® and VISTA® professional window films and GILA® retail window films | Products to increase the safety, security, sound attenuation, energy efficiency and ultraviolet protection of architectural glass for residential and commercial structures; after-market films for solar control, security and safety | DuPont; HT Troplast<br><br>Materials Science Corp. (MSC); Lintec; 3M               | Butyraldehyde; ethanol; polyvinyl alcohol; vinyl acetate monomer; polyester film     | Ghent, Belgium; Springfield, MA; Trenton, MI; Martinsville, VA |
| Vehicles                          | SAFLEX® plastic interlayer for windshields and for side and rear windows of vehicles; LLUMAR®, FORMULAONE PERFORMANCE AUTOMOTIVE FILMS® and GILA® retail window films                      | Products to increase the safety, security, sound attenuation and ultraviolet protection of automotive glass                                                                                                                            | DuPont; Sekisui<br><br>MSC; Lintec; Madico                                         | Butyraldehyde; ethanol; polyvinyl alcohol; vinyl acetate monomer; polyester film     | Ghent, Belgium; Springfield, MA; Trenton, MI; Martinsville, VA |
| Industrial Applications           | GELVA® pressure sensitive adhesives; industrial films; release liners and deep-dyed films                                                                                                  | Packaging; medical devices; tapes and graphic arts                                                                                                                                                                                     | DuPont; Akzo Nobel; Bayer; Lintec; MSC; 3M; Southwall; Rexam; IST; National Starch | Ethanol; formaldehyde; maleic anhydride; melamine; polyester film; butanol; chlorine | Ghent, Belgium; Springfield, MA; Trenton, MI; Martinsville, VA |
| Electronics                       | Performance films; conductive and anti-reflective coated films                                                                                                                             | Computer touch-screens; electroluminescent displays and watches; cathode ray tube monitors                                                                                                                                             | 3M; Lintec; MSC; Southwall; Sheldahl                                               | Ethanol; formaldehyde; maleic anhydride; melamine; polyester film                    | Martinsville, VA; Canoga Park, CA                              |

## Specialty Products Segment

| Major End-Use Markets   | Major Products                                                                                                                                                                                                               | Major End-Use Products & Applications                                                                                                                                 | Major Competitors                                               | Major Raw Materials                                                           | Major Plants                                                                                                      |
|-------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------|-------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------|
| Capital Equipment       | THERMINOL® heat transfer fluids; DEQUEST® water treatment chemicals                                                                                                                                                          | Heat transfer fluids; water treatment; oil field chemicals                                                                                                            | Dow Chemical Co.; Nippon Steel Chemical Co.; Rhodia; Bayer      | Benzene; phenol; phosphorus trichloride                                       | Alvin, TX; Anniston, AL; Newport, Wales (U.K.)                                                                    |
| Industrial Applications | MODAFLOW® flow and leveling agents; RESIMENE® crosslinkers; MAPRENAL® and MADURIT® resins                                                                                                                                    | Coatings and adhesives; caulks and sealants; paints; coated fabric; wire and cable; liquid coating systems; fiberboard; technical laminates; paper coatings           | Cytec Industries; Neste                                         | Acrylate esters; butanol; formaldehyde; melamine                              | Springfield, MA; Rayong, Thailand; Frankfurt-Fechenheim, Germany; Romano d'Ezzelino, Italy                        |
| Aviation/Transportation | SKYDROL® aviation hydraulic fluids; SKYKLEEN® aviation solvents                                                                                                                                                              | Hydraulic fluids for commercial aircraft; environmentally friendly solvents for aviation maintenance                                                                  | Exxon Mobil                                                     | Phosphorus oxychloride; methanol                                              | St. Louis, MO                                                                                                     |
| Vehicles                | MODAFLOW® flow and leveling agents; RESIMENE® crosslinkers; VIACRYL™, MACRYNAL®, VIALKYD®, DUROXYN™, VIAKTIN®, VIAMIN®, and HOSTAFLEX® resins; RESYDROL® waterborne resins; ALFTALAT®, SYNTHACRYL® and VIAKTIN® solid resins | Coatings and adhesives; caulks and sealants; paints; coated fabric; wire and cable; automotive, industrial and decorative coatings; environmentally friendly coatings | Cytec Industries; DSM; Cray Valley/Total; Eastman; UCB; Ashland | Acrylate esters; butanol; formaldehyde; melamine; methanol; terephthalic acid | Springfield, MA; Frankfurt-Fechenheim, Hamburg and Wiesbaden, Germany; Rayong, Thailand; Romano d'Ezzelino, Italy |
| Pharmaceuticals         | Process research and development services and small scale-up manufacturing services                                                                                                                                          | New pharmaceuticals                                                                                                                                                   | Millennium Chemical; Evotec                                     |                                                                               | Aarau and Basel, Switzerland                                                                                      |

## Integrated Nylon Segment

| Major End-Use Markets                    | Major Products                                                                                     | Major End-Use Products & Applications                                                                                                                          | Major Competitors                           | Major Raw Materials                                    | Major Plants                                                                  |
|------------------------------------------|----------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------|--------------------------------------------------------|-------------------------------------------------------------------------------|
| <b>Construction and Home Furnishings</b> | Nylon carpet staple; nylon bulk continuous filament; ACRILAN® acrylic fiber; ASCEND™ nylon polymer | WEAR-DATED® residential and ULTRON VIP® commercial carpet; area rugs; bath mats; WEAR-DATED® upholstery fabrics; blankets; non-woven reinforcement and linings | DuPont; Honeywell; BASF                     | Acrylonitrile; ammonia; cyclohexane; propylene         | Pensacola, FL; Greenwood, SC; Decatur and Foley, AL                           |
| <b>Personal Products</b>                 | ACRILAN® acrylic fiber; ASCEND™ nylon polymer                                                      | Sweaters; knit apparel; half-hose; active wear; craft yarns; hand-knit yarns; apparel; dental floss; intimate apparel; bedding; shoes                          | Sterling Chemicals; Acordis; DuPont; Radici | Acrylonitrile; ammonia; cyclohexane; propylene         | Pensacola, FL; Decatur, AL; Greenwood, SC                                     |
| <b>Vehicles</b>                          | Nylon filament; VYDYNE® nylon molding resins; ASCEND™ nylon polymer; ACRILAN® acrylic fiber        | Tires; air bags; brakes; convertible tops; automotive interior, exterior and under-the-hood molded parts; carpet; non-woven reinforcement and linings          | Acordis; DuPont; Rhodia; Asahi Chemical     | Acrylonitrile; ammonia; cyclohexane; propylene         | Pensacola, FL; Decatur, AL; Greenwood, SC                                     |
| <b>Industrial Applications</b>           | ACRILAN® acrylic fiber; ASCEND™ nylon polymer; industrial nylon fiber                              | Conveyer belts; awnings and tents; nylon film cooking bags; specialized food packaging                                                                         | Acordis; DuPont; Honeywell; BASF            | Acrylonitrile; ammonia; cyclohexane; propylene         | Pensacola, FL; Decatur, AL; Greenwood, SC                                     |
| <b>Intermediate Chemicals</b>            | Nylon salt; adipic acid; hexamethylenediamine; acrylonitrile; chlorobenzenes                       | Nylon and acrylic fiber; nylon plastics; herbicides; feed supplements                                                                                          | DuPont; Rhodia; BASF; Asahi Chemical        | Natural gas; propylene; benzene; chlorine; cyclohexane | Anniston and Decatur, AL; Alvin, TX; Greenwood, SC; Sauget, IL; Pensacola, FL |

### Principal Equity Affiliates

Solutia participates in a number of joint ventures in which it shares management control with other companies. Solutia's equity earnings from affiliates were \$35 million in 2000, \$36 million in 1999, and \$25 million in 1998. Principal joint ventures include Flexsys, L.P., Advanced Elastomer Systems, L.P. and Astaris LLC.

Flexsys, headquartered in Belgium, is a leading supplier of process chemicals to the rubber industry. Its product line includes a number of branded accelerators (SANTOCURE®, THIOFIDE® and THIOTAX®), pre-vulcanization inhibitors (SANTOGARD®), antidegradants and antioxidants (FLECTOL® and SANTOWHITE®) and insoluble sulphur (CRYSTEX®). Flexsys is a 50/50 joint venture between Solutia and Akzo Nobel N.V.

Advanced Elastomer Systems, headquartered in the United States, produces and sells thermoplastic elastomers—materials that combine the processability of thermoplastics and the functional performance of thermoset rubber products. The joint venture's product lines include SANTOPRENE® thermoplastic rubber and VIS-TAFLEX® thermoplastic elastomer. Advanced Elastomer Systems is a 50/50 joint venture between Solutia and Exxon Mobil Corporation.

Astaris, headquartered in the United States, produces and sells phosphorus and phosphate salts. Its product line includes a number of branded products such as LEVN-LITE®, PAN-O-LITE® and LEVERAGE® phosphate, which are sold into the bakery markets. The business also services the pharmaceutical, meat and poultry, and industrial marketplaces. Astaris is a 50/50 joint venture between Solutia and FMC Corporation.

### Sale of Products

Solutia's products are sold directly to end users in various industries, principally by Solutia's own sales force, and, to a lesser extent, by distributors. Under a marketing alliance between Solutia and Dow Plastics, a business unit of The Dow Chemical Company, Dow markets Solutia's VYDYNE® nylon 6,6 molding resins for injection molding applications worldwide. Solutia's marketing and distribution practices do not result in unusual working capital requirements on a consolidated basis. Inventories of finished goods, goods in process and raw materials are maintained to meet customer requirements and Solutia's scheduled production. In general, Solutia does not manufacture its products against a backlog of firm orders; production is scheduled to meet the level of incoming orders and the projections of future demand. Solutia generally is not dependent upon one or a group of customers, and it has no material contracts with the government of the United States, or any state or local, or foreign government. In general, Solutia's sales are not subject to seasonality. While no single customer or customer group accounts for 10 percent or more of Solutia's net sales, sales to the carpet mill industry and the European auto glass industry each represent a significant portion of Solutia's net sales.

### Competition

Solutia encounters substantial competition in each of its product lines. This competition, from other manufacturers of the same products and from manufacturers of different products designed for the same uses, is expected to continue in both U.S. and ex-U.S. markets. Depending on the product involved, various types of competition are encountered, including price, delivery, service, performance, product innovation, product recognition and quality. Overall, Solutia regards its principal product groups as competitive with many other products of other producers and believes that it is an important producer of many of these product groups. For information regarding competition in specific markets, see the charts under "Segments; Principal Products" above.

### Raw Materials and Energy Resources

Solutia is a significant purchaser of basic, commodity raw materials, including propylene, cyclohexane, benzene and natural gas. Major requirements for key raw materials are typically purchased pursuant to medium- to long-term contracts. Solutia is not dependent on any one supplier for a material amount of its raw materials or energy requirements, but certain important raw materials are obtained from a few major suppliers. In general, where Solutia has limited sources of raw materials, it has developed contingency plans to minimize the effect of any interruption or reduction in supply. For information regarding specific raw materials, see the charts under "Segments; Principal Products" above.

While temporary shortages of raw materials and energy may occasionally occur, these items are generally sufficiently available to cover current and projected requirements. However, their continuing availability and price are subject to unscheduled plant interruptions occurring during periods of high demand, or due to domestic and world market and political conditions, as well as to the direct or indirect effect of U.S. and other countries' government regulations. The impact of any future raw material and energy shortages on Solutia's business as a whole or in specific world areas cannot be accurately predicted.

For additional information on raw materials and energy, see "Outlook and Economic Conditions" on page 21 below.

#### **Patents and Trademarks**

Solutia owns a large number of patents which relate to a wide variety of products and processes, has pending a substantial number of patent applications and is licensed under a small number of patents owned by others. Solutia owns a considerable number of established trademarks in many countries under which it markets its products. These patents and trademarks in the aggregate are of material importance in the operations of Solutia and to its Performance Films, Specialty Products, and Integrated Nylon segments.

#### **Research and Development**

Research and development constitute an important part of Solutia's activities. Solutia's research and development expenses amounted to approximately \$67 million in 2000, \$58 million in 1999, and \$60 million in 1998, or about 2% of sales on average. Solutia focuses its research and development expenditures on process improvements and select product development.

Our Performance Films segment launched SAFLEX® HP (high performance) plastic interlayer for hurricane protection and security in large commercial applications. Our Integrated Nylon segment's improved new singed staple fiber was introduced in new carpet grades from the major carpet mills, and its cotton-like GINNY™ acrylic product was successfully commercialized in the upholstery market. Our Specialty Products segment commercialized environmentally friendly adhesives that meet U.S. Postal Service requirements. It also developed and commercialized a family of water-based, pressure-sensitive adhesives that meet and exceed the performance properties of solvent-based adhesives.

#### **Environmental Matters**

The narrative information appearing under "Environmental Matters" on pages 22 and 23 below is incorporated here by reference.

#### **Employee Relations**

On December 31, 2000, Solutia had approximately 10,200 employees worldwide. In general, satisfactory relations have prevailed between Solutia and its employees. Solutia uses self-directed work teams, incentive programs and other initiatives to keep employees actively involved in the success of the business. Approximately 20% of Solutia's workforce is represented by various labor unions.

#### **International Operations**

Solutia and its subsidiaries are engaged in manufacturing, sales and research and development in areas outside the United States, including Europe, Canada, Latin America and Asia. Nearly 40% of Solutia's consolidated sales in 2000 were made into markets outside the United States. Operations outside the United States are potentially subject to a number of risks and limitations that are not present in domestic operations, including fluctuations in currency values, trade restrictions, investment regulations, governmental instability and other potentially detrimental governmental practices or policies affecting companies doing business abroad. Solutia's Performance Films and Specialty Products segments are particularly dependent on their international operations. Approximately one-half and three-fourths of their 2000 sales, respectively, were made into markets outside the United States.

## **Item 2. PROPERTIES.**

Solutia's general offices are located in a leased facility in St. Louis County, Missouri. Solutia's principal European offices are located in Louvain La Neuve, Belgium, in premises leased from the University of Louvain. Solutia also has research laboratories, research centers and manufacturing locations worldwide. Information about Solutia's major manufacturing locations worldwide and segments that used these locations on January 1, 2001, appears under "Segments; Principal Products" in Item 1 of this report and is incorporated here by reference.

Solutia's principal plants are suitable and adequate for their use. Utilization of these facilities may vary with seasonal, economic and other business conditions, but none of the principal plants is substantially idle. The facilities generally have sufficient capacity for existing needs and expected near-term growth. Solutia has plans in place to expand facilities that are anticipated to reach capacity in the next two to three years.

Solutia owns most of its principal plants. However, at Antwerp, Belgium and Sao Jose dos Campos, Brazil, both of which are Monsanto sites, Solutia owns certain buildings and production equipment and leases the underlying land. In addition, Solutia leases the land for its Vianova Resins facilities at Suzano, Brazil and Frankfurt-Fechenheim, Germany from Clariant or a subsidiary of Clariant and the land for its facilities at Wiesbaden, Germany from InfraServ with site services also provided by InfraServ.

Monsanto and Solutia have operating agreements with respect to each of the two Monsanto facilities listed above and Solutia's Chocolate Bayou facility in Alvin, Texas. Under these operating agreements, Solutia is the guest and Monsanto is the operator at the facilities except the Chocolate Bayou facility, at which Monsanto is the guest and Solutia is the operator. The initial term of each of the operating agreements is 20 years. After the initial term, the operating agreements continue indefinitely unless and until terminated by either party on at least 24 months' prior written notice. Each of the operating agreements also provides that, under certain circumstances, either the operator or the guest may terminate the operating agreement prior to the expiration of its initial term. Solutia operates several facilities for other third parties, principally within the Chocolate Bayou; Sauget, Illinois; Pensacola, Florida; Trenton, Michigan and Newport, Wales (U.K.) sites, under long-term lease and operating agreements.

Solutia has completed construction and begun operation of a world-scale acrylonitrile production facility at Chocolate Bayou. The facility employs Solutia's proprietary catalyst system and is capable of producing approximately 550 million pounds annually. Solutia has product sale agreements with three customers, Bayer, Novus International Inc. and Asahi, which made advance payments in connection with this project. In addition, Solutia has constructed a phenol processing facility at the Pensacola, Florida site to produce intermediates in the nylon manufacturing process.

Solutia is an active participant in the safety and health Voluntary Protection Program ("VPP") administered by the Occupational Safety and Health Administration for sites in the U.S., and implemented by Solutia for sites outside the U.S. Currently, ten Solutia sites in the U.S. qualify for the OSHA VPP "Star" designation, a rating designating full compliance. Three other Solutia sites, two in Europe and one in Canada, have achieved the Solutia "Star" designation, which is an internal equivalent to the OSHA designation.

## **Item 3. LEGAL PROCEEDINGS.**

Because of the size and nature of its business, Solutia is a party to numerous legal proceedings. Most of these proceedings have arisen in the ordinary course of business and involve claims for money damages. In addition, at the time of the spinoff, Solutia assumed from the former Monsanto Company (now Pharmacia Corporation), under an agreement known as the Distribution Agreement, liabilities related to specified legal proceedings. As a result, although Monsanto remains the named defendant, Solutia is required to manage the litigation and indemnify Monsanto for costs, expenses and judgments arising from the litigation. The results of litigation cannot be predicted with certainty. However, based upon currently available facts, Solutia does not believe that the ultimate resolution of any of these pending matters, except those cases described below involving the alleged discharge of polychlorinated biphenyls ("PCBs") from the Anniston, Alabama plant site, will have a material adverse effect on Solutia's financial position, liquidity or profitability in any one year. Resolution of those Anniston, Alabama cases may have a material adverse effect on Solutia's net income in a given year, although it is impossible at this time to estimate the range or

amount of any such liability. The following paragraphs describe several proceedings to which Solutia is a party or to which Monsanto is a party and for which Solutia assumed any liabilities.

On April 12, 1985, Monsanto was named as a defendant in *Alanis, et al. v. Farm & Home Savings, et al.*, filed in the District Court in Harris County, Texas, the first of a number of lawsuits in which plaintiffs claimed injuries resulting from alleged exposure to substances present at or emanating from the Brio Superfund site near Houston, Texas. Monsanto is one of a number of companies that sold materials to the chemical reprocessor at that site. The following two matters were settled recently: (1) Monsanto was one of a number of defendants in an action brought in Harris County District Court on behalf of 412 plaintiffs who were former employees of the owners/operators of the Brio site, or members of the employees' families. Plaintiffs claimed physical and emotional injury and sought compensatory and punitive damages in an unspecified amount. On April 24, 2000, the Company reached a tentative agreement to settle this matter for \$6 million. On December 15, 2000, the settlement was approved by the court and has been implemented. (2) Monsanto was one of a number of defendants in an action brought in Harris County District Court on behalf of 76 plaintiffs who lived in a subdivision near the Brio site, who attended school near the site or who used nearby recreational baseball fields. Plaintiffs claimed to have suffered various personal injuries and fear future disease; they asserted the need for medical monitoring. Plaintiffs sought compensatory and punitive damages in an unspecified amount. The Company reached a tentative agreement in October, 2000 to settle this matter for \$631,000. The settlement was approved by the court and was implemented on February 26, 2001. This leaves only two cases, one pending in Harris County District Court, the other in U.S. District Court for the Southern District of Texas, on behalf of 39 plaintiffs who owned homes or lived in subdivisions near the Brio site, attended school near the site or used nearby recreational baseball fields. Monsanto is one of a number of defendants in these cases. Plaintiffs claim to have suffered various personal injuries and fear future disease; they assert the need for medical monitoring, and, in the case of the homeowners, claim property damage. Plaintiffs seek compensatory and punitive damages in an unspecified amount. Solutia believes there are meritorious defenses to these lawsuits, including lack of proximate cause, lack of negligent or improper conduct on the part of Monsanto or Solutia and negligence of plaintiffs (or their parents) and/or of the builders and developers of the Southbend subdivision. Solutia is vigorously defending these actions.

On November 15, 1993, Monsanto was named as a defendant in *Dyer, et al. v. Monsanto Company, et al.*, filed in Circuit Court in St. Clair County, Alabama, the first of a number of lawsuits in which plaintiffs claim to have sustained personal injuries or property damage as a result of the alleged release of PCBs and other materials from its Anniston, Alabama plant site. The following matters are currently pending: (1) Monsanto is one of a number of defendants in two actions, one pending in Circuit Court for Talladega County, Alabama, the other, in Circuit Court for St. Clair County, Alabama, brought on behalf of 107 plaintiffs who are owners of property along waterways near the Anniston plant. Plaintiffs allege fear of toxic contamination, mental and emotional distress, increased risk of disease and fear of cancer as well as diminished value of their properties. They seek compensatory and punitive damages in an unspecified amount. Plaintiffs in these cases opted out of a certified class of property owners along waterways near the Anniston plant. That class action, which was pending in Circuit Court for St. Clair County, Alabama, has been settled. (2) Monsanto is a defendant in one additional action brought in Circuit Court in Shelby County, Alabama on behalf of a purported class of property owners farther downstream along waterways near the plant. Plaintiffs seek compensatory and punitive damages in an unspecified amount for an alleged increased risk of physical injury or illness, emotional distress caused by fear of future injury or illness, medical monitoring and diminishment in the value of their properties and their riparian rights. On October 5, 1999, the trial court granted Solutia's motion for summary judgment, holding that plaintiffs had, in an action not involving Monsanto or Solutia, recovered for the damages they claim in this action. In addition, the court found that plaintiffs' claims were barred by the statute of limitations. Plaintiffs timely filed their appeal with the Alabama Supreme Court. The matter has been fully briefed and the parties await the decision of that Court. (3) Monsanto is the sole defendant in one additional action pending in United States District Court for the Northern District of Alabama brought on behalf of a purported class of "[a]ll persons who reside, or who at one time did reside, in the areas contaminated by the Defendant's Anniston, Alabama plant and were thereby directly or indirectly exposed to PCBs." Plaintiffs allege that as a result of this exposure, they are at an increased risk of suffering personal injuries and seek an injunction mandating medical monitoring and funding of a study of the alleged adverse health effects of this exposure. On December 27, 2000, the District Court certified the following question of law to the Alabama Supreme Court: "Does a complaint which does not allege any past or

present personal injury to the plaintiff state a cause of action for medical monitoring and study when the plaintiff alleges that he has been exposed to hazardous contamination and pollution by the conduct of the defendant?" On February 12, 2001, the Alabama Supreme Court consented to answer this question and ordered the parties to submit briefs. (4) Monsanto is one of a number of defendants in one additional action brought in Circuit Court for Calhoun County, Alabama on behalf of a purported class of all Alabama residents who have been exposed to PCBs or other materials allegedly released from the Anniston plant. Plaintiffs claim to suffer from unspecified personal injuries and seek compensatory and punitive damages in an unspecified amount. (5) Monsanto and Solutia were named as defendants in one additional action brought in Circuit Court for Calhoun County, Alabama on behalf of a purported class of owners of property upon which was deposited soil allegedly contaminated with PCBs and taken from the site of a nearby commercial development. Plaintiffs seek compensatory and punitive damages in an unspecified amount. (6) Monsanto is one of a number of defendants in an additional 8 cases brought in Circuit Court for Calhoun County, Alabama and two additional cases brought in United States District Court for the Northern District of Alabama on behalf of a total of 5,419 individuals who own or rent homes, own or operate businesses, attend churches, or who have otherwise resided or visited in neighborhoods near the Anniston plant, and one commercial entity which owns property near the Anniston plant. Plaintiffs seek compensatory and punitive damages in an unspecified amount or in the amount of \$3 million for each individual and injunctive relief requiring the defendants to remove alleged contamination in Anniston. The individual plaintiffs claim to have suffered permanent adverse health effects and fear future disease. They assert the need for medical monitoring, diminution in the value of their properties in the case of residential and commercial property owners and commercial losses in the case of business owners. On March 8, 1999, the Alabama Supreme Court stayed all proceedings in several consolidated cases pending in Circuit Court for Calhoun County brought on behalf of 2,714 plaintiffs after Solutia filed a petition for a writ of mandamus. Solutia sought the intervention of the Alabama Supreme Court on a number of grounds, including the failure of the trial court to rule on Solutia's motions for change of venue, for exclusion of certain evidence that lacks a valid scientific basis, for specification of procedures to govern trial of plaintiffs' claims, including procedures governing jury selection, and other relief. On May 16, 2000, the Alabama Supreme Court issued an order lifting the stay of proceedings for the sole purpose of allowing the trial court to enter orders on the pending motions. On October 12, 2000, the trial court entered its orders. These cases are now back before the Alabama Supreme Court and the parties await the court's decision. (7) In addition to the matters described above, Solutia has been advised of approximately 90 additional potential plaintiffs who may file new actions or intervene in actions already pending. Solutia believes that there are meritorious defenses to all these matters, including lack of any physical injury or property damage to plaintiffs, lack of any imminent or substantial endangerment to health or the environment and lack of negligence or improper conduct on the part of Monsanto or Solutia. These actions are being vigorously defended.

Monsanto is one of several defendants added on February 7, 1997, to *Pennsylvania Department of General Services, et al. v. United States Mineral Products Company, et al.*, a case then pending in the Commonwealth Court of Pennsylvania. This action was originally filed against United States Mineral Products Company in 1990 by the Commonwealth of Pennsylvania, seeking damages caused by the presence of asbestos fireproofing in the Transportation and Safety Building ("T & S Building"), which was part of the Commonwealth's Capital Complex in Harrisburg, Pennsylvania. In June 1994, a fire broke out in the T & S Building. Testing following the fire revealed the presence of low levels of PCBs at various locations in the building, which the Commonwealth alleges necessitated its demolition. The Commonwealth seeks recovery of costs it allegedly incurred in testing, monitoring, cleanup, demolition and relocation caused by the alleged contamination. In addition, the Commonwealth seeks the cost of constructing a new building on the site of the T & S Building. Trial of this action commenced with the selection of a jury in April 1999. On August 23, 2000, the jury returned a verdict of \$90 million against Monsanto. The verdict was reduced to \$45 million by the trial court to account for a settlement reached with the Commonwealth by a codefendant during trial. Prejudgment interest in an amount to be determined by the court will be added to the verdict. Solutia believes that there are meritorious defenses, including lack of any hazard or danger to occupants of or visitors to the T & S Building caused by the presence of PCBs; a determination by the Pennsylvania Department of Health that the building was safe for use and occupancy; the failure of the Commonwealth to act prudently following the fire to mitigate its alleged damages; the impropriety of using replacement cost as a measure of damages; and the fact that most of plaintiffs' damages would have been incurred during the removal of asbestos fireproofing and the installation of fire sprinklers required to comply with the 1987 Harrisburg Fire Safety Code, and thus cannot be attributed to the presence of PCBs. Solutia will vigorously pursue its post-trial and appellate remedies.

On December 4, 1998, the U.S. Environmental Protection Agency ("EPA") issued a notice of violation to Solutia, Monsanto and P4 Production, L.L.C., alleging violations of the Wyoming Environmental Quality Act, the Wyoming Air Quality Standards & Regulations and a permit issued in 1994 by the Wyoming Department of Environmental Quality to Sweetwater Resources, Inc., a former subsidiary of Monsanto, for a coal coking facility in Rock Springs, Wyoming. This facility is currently owned by P4 Production, a joint venture formed in conjunction with the spinoff of Solutia by Monsanto on September 1, 1997, which is now both operated and controlled by Pharmacia. Despite the sale of substantially all of Solutia's interest in this joint venture, Solutia continues to be a party to this litigation. On November 22, 1999, the United States, on behalf of the EPA, demanded \$2,500,000 from P4 Production, Solutia and Monsanto and injunctive relief ensuring compliance with the permit requirements. On January 18, 2000, P4 Production, Solutia and Monsanto filed a complaint for declaratory relief in the United States District Court for the District of Wyoming against the EPA. The companies are seeking a determination that the action the EPA is threatening against them is precluded by the doctrine of *res judicata*, among other things, since the issues are the same matters that were resolved by a June 25, 1999 consent decree between the three companies and the State of Wyoming. On May 5, 2000, the United States filed its memorandum in opposition to the companies' motion for summary judgment and its cross-motion for summary judgment against the companies. Oral argument on the merits of these motions occurred on June 7, 2000.

#### **Risk Management**

Solutia has evaluated risk retention and insurance levels for product liability, property damage and other potential areas of risk. Solutia will continue to devote significant effort to maintaining and improving safety and internal control programs, which reduce its exposure to certain risks. Management decides the amount of insurance coverage to purchase from unaffiliated companies and the appropriate amount of risk to retain based on the cost and availability of insurance and the likelihood of a loss. Management believes that the levels of risk which it has retained are consistent with those of other companies in the chemical industry. There can be no assurance that Solutia will not incur losses beyond the limits, or outside the coverage, of its insurance. Solutia does not expect its consolidated financial position, profitability and liquidity to be affected materially by the levels of risk retention that it accepts.

Under the Distribution Agreement that Solutia and Monsanto entered into at the time of the spinoff, Solutia is entitled to the benefit of liability insurance coverage under certain Monsanto policies, to the extent coverage existed and coverage limits are not exhausted, for claims for which Solutia assumed responsibility. That insurance coverage generally is shared with Monsanto for other liabilities existing prior to the spinoff which Monsanto has retained, on an as available basis, without allocation.

#### **Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.**

Solutia did not submit any matters to the security holders during the fourth quarter of 2000.

## PART II

### Item 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS.

Solutia's stock is traded principally on the New York Stock Exchange under the Symbol "SOI."

The following table shows the high and low sales prices for each quarter during 2000 and 1999 as reported in the New York Stock Exchange Composite Transactions.

| 2000                | High    | Low     | 1999                 | High    | Low     |
|---------------------|---------|---------|----------------------|---------|---------|
| First Quarter ..... | \$17.19 | \$11.63 | First Quarter .....  | \$24.38 | \$15.88 |
| Second Quarter..... | 15.56   | 11.25   | Second Quarter ..... | 26.31   | 16.06   |
| Third Quarter.....  | 15.69   | 10.38   | Third Quarter .....  | 22.94   | 16.13   |
| Fourth Quarter..... | 13.00   | 10.88   | Fourth Quarter ..... | 18.88   | 13.50   |

On December 31, 2000, Solutia had 36,703 registered shareholders.

The declaration and payment of dividends is made at the discretion of Solutia's Board of Directors. The Board's current policy is to pay cash dividends on an annual basis in December. The Board anticipates that the current 4-cent annual dividend will remain unchanged for the foreseeable future.

# Item 6. SELECTED FINANCIAL DATA.

The following selected financial information has been derived from the audited consolidated financial statements. The information set forth below is not necessarily indicative of results of future operations and should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the consolidated financial statements and related notes thereto included elsewhere in this Form 10-K.

## Financial Summary

(Dollars in millions, except per share amounts)

### Operating Results:

|                                                           | 2000     | 1999     | 1998     | 1997     | 1996    |
|-----------------------------------------------------------|----------|----------|----------|----------|---------|
| Net Sales.....                                            | \$ 3,185 | \$ 2,830 | \$ 2,835 | \$ 2,969 | \$2,977 |
| Gross Profit.....                                         | 486      | 652      | 750      | 653      | 652     |
| As percent of net sales.....                              | 15%      | 23%      | 26%      | 22%      | 22%     |
| Marketing, Administrative and Technological Expenses..... | 429      | 355      | 364      | 363      | 427     |
| As percent of net sales.....                              | 13%      | 13%      | 13%      | 12%      | 14%     |
| Amortization Expense.....                                 | 33       | 3        | —        | —        | —       |
| Operating Income <sup>(1)</sup> .....                     | 24       | 294      | 386      | 290      | 33      |
| As percent of net sales.....                              | 1%       | 10%      | 14%      | 10%      | 1%      |
| Income Before Income Taxes.....                           | 41       | 303      | 375      | 290      | 33      |
| Net Income <sup>(2)</sup> .....                           | 49       | 206      | 249      | 192      | 32      |
| As percent of net sales.....                              | 2%       | 7%       | 9%       | 6%       | 1%      |

### Share Data:

|                                                 |         |         |         |         |         |
|-------------------------------------------------|---------|---------|---------|---------|---------|
| Basic Earnings per Share <sup>(3)</sup> .....   | \$ 0.46 | \$ 1.86 | \$ 2.16 | \$ 1.63 | \$ 0.28 |
| Diluted Earnings per Share <sup>(3)</sup> ..... | 0.46    | 1.80    | 2.03    | 1.55    | 0.27    |
| Dividends per Share.....                        | 0.04    | 0.04    | 0.04    | 0.01    | —       |

### Common Stock Price:

|                                                |        |        |        |        |   |
|------------------------------------------------|--------|--------|--------|--------|---|
| High.....                                      | 17.19  | 26.31  | 32.00  | 27.75  | — |
| Low.....                                       | 10.38  | 13.50  | 18.69  | 18.69  | — |
| Close.....                                     | 12.00  | 15.44  | 22.38  | 26.69  | — |
| Price/Earnings Ratio on Year-End Stock Price   | 26     | 9      | 11     | 17     | — |
| Number of Registered Shareholders.....         | 36,703 | 39,171 | 41,864 | 57,894 | — |
| Year-End Shares Outstanding (in millions)..... | 102.9  | 109.5  | 112.8  | 117.4  | — |
| Shares Repurchased (in millions).....          | 7.7    | 3.8    | 6.2    | 1.6    | — |
| Average Daily Trading Volume (in thousands) .. | 518    | 458    | 401    | 1,053  | — |

### Other Data:

|                                       |        |        |       |       |       |
|---------------------------------------|--------|--------|-------|-------|-------|
| Interest Expense <sup>(4)</sup> ..... | \$ 83  | \$ 40  | \$ 43 | \$ 41 | \$ 36 |
| Income Taxes (Benefit).....           | (8)    | 97     | 126   | 98    | 1     |
| Depreciation and Amortization.....    | 191    | 151    | 147   | 145   | 166   |
| Total Assets.....                     | 3,581  | 3,770  | 2,765 | 2,768 | 2,483 |
| Capital Expenditures.....             | 221    | 257    | 158   | 165   | 192   |
| Long-Term Debt.....                   | 784    | 802    | 597   | 597   | —     |
| Employees (year-end).....             | 10,200 | 10,600 | 8,700 | 8,800 | —     |

(1) Operating income includes restructuring charges and other items of \$158 million in 2000, \$61 million in 1999, \$1 million in 1998, \$84 million in 1997 and \$248 million in 1996.

(2) Net income includes restructuring charges and other items of \$74 million, or \$0.68 per share in 2000, \$38 million, or \$0.33 per share in 1999, \$1 million, or \$0.01 per share in 1998, \$53 million, or \$0.43 per share, in 1997 and \$164 million, or \$1.37 in 1996.

(3) For the 1996 period which ended prior to the spinoff, the number of Monsanto weighted average shares outstanding and common share equivalents were adjusted for the distribution ratio in the spinoff of one share of Solutia's common stock for every five shares of Monsanto common stock.

(4) Monsanto used a centralized approach to cash management and the financing of its operations. As a result, cash and cash equivalents and debt were not allocated to Solutia in the historical financial statements. Interest expense was allocated to Solutia in its consolidated financial statements to reflect Solutia's pro rata share of the financing structure of Monsanto.

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

The following discussion and analysis should be read in conjunction with the consolidated financial statements and related notes thereto included elsewhere in this Form 10-K.

### Overview

Solutia's reportable segments and their major products are as follows:

| Performance Films                                                                                                                                              | Specialty Products                                                                                                                                                                                     | Integrated Nylon                                                                                                           |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------|
| SAFLEX® plastic interlayer<br>KEEPSAFE®, SAFLEX INSIDE® (in Europe only) and KEEPSAFE MAXIMUM® glass for residential security and hurricane protection windows | Resins and additives, including ALFTALAT® polyester resins, RESIMENE® and MAPRENAL® crosslinkers and SYNTHACRYL® acrylic resins                                                                        | Intermediate "building block" chemicals                                                                                    |
| LLUMAR®, VISTA® and GILA® professional and after-market window films                                                                                           | THERMINOL® heat transfer fluids                                                                                                                                                                        | Merchant polymer and nylon extrusion polymers, including VYDYNE® and ASCEND™                                               |
| Conductive and anti-reflective coated films and deep-dyed films                                                                                                | DEQUEST® water treatment chemicals                                                                                                                                                                     | Carpet fibers, including the WEAR-DATED® and ULTRON VIP® brands                                                            |
| GELVA® pressure-sensitive adhesives                                                                                                                            | SKYDROL® hydraulic fluids and SKYKLEEN® cleaning fluids for aviation<br><br>Process research, process development, scale-up capabilities and small scale manufacturing for the pharmaceutical industry | Industrial nylon fibers<br><br>ACRILAN® acrylic fibers for apparel, upholstery fabrics, craft yarns and other applications |

See Note 16 to the Consolidated Financial Statements for further information.

### Results of Operations

Solutia's net sales for 2000 of \$3.185 billion were 13 percent higher than 1999 net sales of \$2.830 billion and 12 percent higher than 1998 net sales of \$2.835 billion. A number of events affect the comparability of 2000 results with those in 1999 and 1998. These events include the acquisitions of the Vianova Resins Group in December 1999, CarboGen Holdings AG in February 2000 and AMCIS AG in March 2000. In addition, Solutia contributed its Phosphorus Derivatives business to the Astaris joint venture in April 2000 and sold its Polymer Modifiers business in August 2000. Excluding the sales associated with these businesses, net sales for 2000 were up 3 percent from the comparable periods of 1999 and 1998. The net sales increases reflected higher average selling prices, partially offset by unfavorable currency exchange rate fluctuations and lower volumes. Operating income for the year ended December 31, 2000, was \$24 million, 92 percent lower than 1999 operating income of \$294 million, and 94 percent lower than 1998 operating income of \$386 million. The decline in 2000 operating income was caused by higher raw material and energy costs that resulted from the sharp increase in petrochemical and natural gas prices and by special charges taken in the second and fourth quarters of 2000 related to certain workforce reductions, asset impairments and facility closures. The remainder of the decline resulted from higher marketing, administrative, technological and amortization expenses associated with the acquisition and integration of newly acquired companies and other growth programs.

#### Performance Films

Net sales for Performance Films were \$731 million in 2000, compared with \$713 million in 1999 and \$614 million in 1998. The 3 percent increase in 2000 net sales over 1999 resulted from the full year's effect of the CPFilms acquisition and higher volumes in the SAFLEX® plastic interlayer business, partially offset by the loss of sales from

the Polymer Modifiers business and unfavorable currency exchange movements. Excluding CPFilms and the Polymer Modifiers businesses, 2000 net sales were essentially equal to 1999 net sales. Higher year-over-year volumes in the SAFLEX® plastic interlayer business were driven primarily from increased demand by North American and European automotive glass manufacturers. Also, to a lesser extent, businesses in this segment achieved higher average selling prices than those of the year-ago period. Offsetting the increases in sales volumes and average selling prices were unfavorable currency exchange movements due to the devaluation of the euro in relation to the U.S. dollar.

The Performance Films segment's net sales for 1999 increased 16 percent over 1998 net sales because of an overall volume gain of more than 20 percent, partially offset by selling price declines. The sales volume increase was attributable to the May 1999 acquisition of CPFilms, and to a greater than 10 percent increase in SAFLEX® plastic interlayer sales volumes. Volume gains for SAFLEX® plastic interlayer resulted from the full global commercialization of SAFLEX IIIG®, the continued commercialization of KEEPSAFE®, SAFLEX INSIDE® (in Europe only) and KEEPSAFE MAXIMUM® brand products and the launch of a SAFLEX® product for Enhanced Protective Glass. Contractual pricing provisions that adjust pricing downward for increased volume caused the selling price declines.

Segment profit was \$185 million in 2000, versus \$189 million in 1999, and \$168 million in 1998. The 2 percent decrease in 2000 segment profit compared with 1999 primarily resulted from increased raw material costs in the SAFLEX® plastic interlayer business and the loss of sales from the Polymer Modifiers business. The decrease was partially offset by lower employee benefits cost. The 13 percent improvement in 1999 segment profit over 1998 was due to higher year-over-year net sales, lower raw material costs and employee benefits cost and other cost reductions, partially offset by increased marketing expenditures related to the promotion of KEEPSAFE®, SAFLEX INSIDE® (in Europe only) and KEEPSAFE MAXIMUM® brands and Enhanced Protective Glass.

#### *Specialty Products*

Solutia's Specialty Products segment had net sales of \$866 million in 2000, compared with \$615 million in 1999 and \$613 million in 1998. The 41 percent increase in 2000 net sales over 1999 was due to the acquisitions of Vianova Resins, CarboGen and AMCIS, partially offset by the impact of contributing the Phosphorus Derivatives business to the Astaris joint venture. Excluding the effects of the acquisitions and the loss of sales associated with the Phosphorous Derivatives business, net sales declined by 6 percent. Net sales decreased primarily due to unfavorable currency exchange movements associated with the devaluation of the euro in relation to the U.S. dollar, and to a lesser extent, the loss of sales from the Scriptsets line of business which was sold in August 1999.

The slight increase in 1999 net sales over 1998 resulted from increased sales volumes of Solutia's resins and additives products and SKYDROL® 5 hydraulic fluid for aviation applications, partially offset by unfavorable currency exchange movements. The growth in sales volumes for resins and additives was attributable to strong sales in the coatings market, especially during the fourth quarter of 1999. Also during 1999, Solutia became the sole supplier of hydraulic fluid to Boeing Corporation for its new commercial aircraft.

Specialty Products' segment profit was \$182 million in 2000, compared with \$159 million in 1999 and \$152 million in 1998. The 14 percent increase in 2000 profit resulted from higher net sales from the acquired companies, partially offset by the loss of sales from the Phosphorus Derivatives business and unfavorable manufacturing variances for specialty chemicals products. The 5 percent improvement in 1999 profit was due to improved manufacturing performance for Solutia's phosphorus derivatives products, and to a lesser extent, lower raw material costs.

#### *Integrated Nylon*

Solutia's Integrated Nylon segment had net sales in 2000 of \$1.580 billion, compared with \$1.508 billion in 1999 and \$1.613 billion in 1998. The 5 percent increase in 2000 net sales compared to 1999 net sales was attributable to the effect of higher average selling prices in each of the segment's businesses, partially offset by volume declines in the carpet fiber and nylon plastics and polymer businesses. The majority of the segment's price increases were in the carpet fiber and intermediates businesses, and to a lesser extent, the ACRILAN® acrylic fiber business. Considerable pricing actions were taken in the carpet business during 2000 in response to rapid raw material cost increases. Price

increases in the intermediates business were primarily attributable to contract business with formula pricing tied to raw material costs. ACRILAN® acrylic fiber products experienced higher average selling prices in the export markets because of the economic recovery in the Asia Pacific region. Despite the increases in average selling prices, Solutia offset only approximately 40 percent of the raw material cost increases. Carpet fiber sales volumes decreased in the second half of 2000 as carpet mills reduced inventory levels in response to lower retail demand. Decreased sales volumes in the nylon plastics and polymer business resulted from lower shipments of VYDYNE® nylon molding resins to Dow Plastics and lower demand for textile polymers principally because of the bankruptcy of a Taiwanese textile polymer customer.

The 7 percent decline in this segment's 1999 net sales compared with 1998 resulted from lower selling prices for almost all products and lower ACRILAN® acrylic fiber volumes, partially offset by improved sales volumes of carpet fiber and nylon polymers. Lower selling prices and sales volumes for ACRILAN® acrylic fibers were caused by weak market conditions in the Asia Pacific region. In addition, that region's lower demand depressed markets in the Americas as acrylic fiber producers sought alternative outlets for their products. The impact of these events began early in the third quarter of 1998 and continued through the third quarter of 1999. Prices stabilized early in the fourth quarter of 1999 and increased slightly during the remainder of the year. For 1999 compared with 1998, ACRILAN® acrylic fiber accounted for more than half of Integrated Nylon's net sales decline. Nylon carpet selling prices were adversely affected in 1999 by the consolidation of the carpet mill industry in late 1998 and the resultant increase in the carpet mills' buying leverage. In addition, lower-priced polyester carpet fiber also put downward pressure on prices. Sales volumes for the segment's products were mixed, as improved carpet fiber and VYDYNE® nylon molding resins volumes were offset by lower ACRILAN® acrylic fiber volumes, lower chlorobenzenes volumes and Solutia's exit from the ammonia business in 1999.

Integrated Nylon segment profit was \$160 million in 2000, versus \$289 million in 1999 and \$376 million in 1998. The 45 percent decrease resulted almost exclusively from higher raw material and energy costs associated with the sharp increase in petrochemical and natural gas prices throughout 2000. The cost of propylene, a major feedstock for the segment, increased more than 60 percent over 1999 levels. The cost of cyclohexane, another major feedstock for the segment, increased more than 30 percent over 1999 levels. The cost of natural gas, which is used as an energy source and also affects the cost of various raw materials within the segment, increased approximately 80 percent over the year-ago period. The petrochemical and natural gas markets remain extremely volatile and upward pricing pressures continue because of low worldwide inventory levels. Elevated petrochemical and natural gas costs, as well as lower Integrated Nylon volumes, will continue to adversely affect profitability over the near term. The 23 percent decrease in 1999 segment profit from 1998 was caused by lower selling prices in 1999, which were partially offset by reduced manufacturing and overhead costs.

#### *Operating Income*

Solutia's operating income for 2000 was \$24 million, compared with \$294 million in 1999 and \$386 million in 1998. The decline in 2000 operating income was caused by higher raw material and energy costs that resulted from the sharp increase in petrochemical and natural gas prices and by special charges taken in the second and fourth quarters of 2000 related to certain workforce reductions, asset impairments and facility closures. The remainder of the decline resulted from higher marketing, administrative, technological and amortization expenses associated with the acquisition and integration of newly acquired companies and other growth programs.

As part of the integration of Vianova Resins with Solutia's resins businesses, Solutia identified excess production capacity for certain Solutia resins products that will allow for the consolidation of production facilities. As a result, Solutia decided to exit operations at the Port Plastics site in Addyston, Ohio and recorded a restructuring charge of \$8 million (\$5 million aftertax, or \$0.05 per share) to cost of goods sold during the second quarter of 2000. The financial impact will not be material to Solutia as production will be shifted to other production facilities. During the second quarter of 2000, Solutia also recorded an impairment charge of \$6 million (\$4 million aftertax, or \$0.04 per share), to administrative expenses for the write-down of capitalized software costs related to the formation of the Astaris joint venture.

During the fourth quarter of 2000, Solutia recorded restructuring charges of \$53 million (\$33 million aftertax, or \$0.31 per share) to cost of goods sold for costs associated with work force reductions of approximately 700 people

across all world areas of the company and the closure of certain non-strategic facilities. The restructuring is part of an enterprise-wide cost reduction initiative expected to achieve \$100 million in annual savings. Approximately 60 percent of the savings will come from these restructuring actions and will be reflected primarily in cost of goods sold. The balance of the savings will come from a variety of projects aimed at improving efficiencies and work processes and will be reflected primarily in cost of goods sold. Approximately half of the savings from the cost reduction initiative is expected to be achieved in 2001, with the full amount achieved in 2002. The cost savings will primarily result from work force reductions, a smaller senior management team, efficiencies realized from the full implementation of enterprise-wide systems and the streamlining of operations primarily within Integrated Nylon. The restructuring actions are expected to be carried out by the end of 2001. Cash outlays associated with the restructuring actions will be funded by operations. Approximately 80 percent of the workforce reductions are planned for North American business and manufacturing operations, and approximately 20 percent are planned for European, Asian and Latin American operations and sales offices. Management and senior management positions represent approximately one-third of the workforce reductions. The closure of non-strategic facilities is not anticipated to have a significant impact to future operations.

During the fourth quarter of 2000, Solutia recorded a \$76 million (\$47 million aftertax, or \$0.44 per share) impairment charge to cost of goods sold primarily for the write-off of certain non-performing and non-strategic fiber spinning, drawing and packaging equipment which supports several of Integrated Nylon's product lines. Solutia also recorded an impairment charge to cost of goods sold of \$15 million (\$10 million aftertax, or \$0.09 per share) for the write-off of chlorobenzenes' production equipment. The impairments were indicated by current period operating losses and projections of continued losses primarily because of the noncompetitive cost positions these businesses have and the competitive market conditions that they face. The carrying values of the assets were written off as determined by discounting expected future cash flows, using an appropriate discount rate. The assumptions used in the cash flow projections were not materially different from the market conditions experienced in 2000. These conditions are not expected to improve significantly in the foreseeable future. The cash flow assumptions included declining demand and market share combined with decreased operating margins. Lower operating margins reflect the non-competitive cost position of these businesses and the impact of lower selling prices associated with an extremely competitive operating environment. Annual depreciation charges associated with these assets of approximately \$10 million will no longer be reflected in cost of goods sold. Solutia will continue to operate these assets as they contribute to the recovery of fixed costs.

During February 1999, certain equipment critical to Solutia's ammonia production process failed. After analyzing the economics of purchased ammonia versus the cost to repair the equipment, Solutia decided to exit the ammonia business. A \$28 million (\$18 million aftertax, or \$0.16 per share) charge to cost of goods sold was recorded in the first quarter to complete the exit plan. The charge included \$2 million to write down the assets to their fair value of approximately \$4 million, \$4 million of dismantling costs and \$22 million of estimated costs for which Solutia is contractually obligated under an operating agreement. The contractually obligated costs represented an estimate of the direct manufacturing, overhead and utilities that Solutia was required to pay to a third-party operator during a 36-month termination period. Ammonia business net sales were \$1 million in 1999 and \$20 million in 1998. Operating income for those periods was minimal. During the first quarter of 2000, Solutia entered into an agreement for the dismantling of those assets by a third-party and as a result, transferred the liability for dismantling to the third-party. During the third quarter of 2000, Solutia reached an agreement with the plant operator for the final settlement of the contractually obligated costs. As a result, Solutia transferred the liability for the contractually obligated costs to accrued liabilities.

During the first quarter of 1999, an impairment charge of \$6 million (\$4 million aftertax, or \$0.03 per share) was recorded to cost of goods sold primarily to write down a bulk continuous filament spinning machine that was shut down due to a noncompetitive cost position. The adjusted carrying value of the machine is \$0.5 million. The charge resulted from a SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and Assets to Be Disposed Of" review, which indicated that the carrying amount of the assets exceeded the identifiable, undiscounted cash flows related to the assets. Fair value of the assets was determined based on estimates of market prices for the machinery. Operating income derived from the machinery was minimal in the years ended December 31, 1999 and 1998.

During the first quarter of 1999, Solutia also recorded a \$29 million (\$18 million aftertax, or \$0.16 per share) charge to cost of goods sold related to the anticipated settlement of two lawsuits concerning the alleged discharge of polychlorinated biphenyls ("PCBs") from the Anniston, Alabama, plant site. During the third quarter of 2000, Solutia paid approximately \$23 million for the settlement of these actions. The remainder of the reserve will cover costs associated with environmental remediation of the allegedly affected areas.

During the fourth quarter of 1999, Solutia reversed excess restructuring reserves due to the completion of the actions at a lower cost than the 1996 restructuring plan contemplated. A reversal of \$1 million (\$1 million aftertax, or \$0.01 per share) was made to eliminate a reserve for headcount reductions after the final stage of headcount reductions was carried out. A second reversal of \$1 million (\$1 million aftertax, or \$0.01 per share) was made to eliminate a reserve recorded to shutdown a non-strategic facility after that shutdown was completed at a lower cost.

See Notes 3 and 4 to the Consolidated Financial Statements for additional information regarding Solutia's restructuring activities and asset impairments.

The 24 percent decline in 1999 operating income from 1998 operating income was caused by lower Integrated Nylon segment profit and charges recorded in the first quarter of 1999, partially offset by higher profit in the Performance Films and Specialty Products segments and lower administrative and technological expenses. The comparison of operating income between 1999 and 1998 was affected by reversals of excess restructuring reserves to reflect lower cost estimates for restructuring actions. A reversal of \$3 million (\$2 million aftertax, or \$0.02 per share) was made in the second quarter of 1998 due to lower cost estimates for the shutdown of certain facilities included in the 1996 restructuring plan. Reversals made in the third and fourth quarters of 1998 of \$3 million (\$2 million aftertax, or \$0.02 per share) and \$3 million (\$2 million aftertax, or \$0.02 per share), respectively, were due to lower cost estimates to implement Solutia's employment reduction plans. Estimates were lowered because of higher than anticipated attrition, which reduced employment levels without additional cost to Solutia.

Operating income for 1998 was also affected by inventory charges of \$4 million (\$3 million aftertax, or \$0.03 per share) in the third quarter and \$6 million (\$4 million aftertax, or \$0.04 per share) in the fourth quarter. The third quarter charge was taken to reduce certain slow-moving inventories to their net realizable values. The fourth quarter charge was primarily caused by losses on the disposition of certain nonsalable inventories.

#### ***Equity Earnings from Affiliates***

Equity earnings from affiliates were \$35 million in 2000, compared with \$36 million in 1999 and \$25 million in 1998. The slight decrease in 2000 was primarily the result of special charges recorded by the Flexsys and Astaris joint ventures during the second quarter of 2000. The Flexsys joint venture recorded charges associated with the closure and impairment of certain manufacturing operations in the United Kingdom. Solutia's share of these charges was \$13 million (\$13 million aftertax, or \$0.12 per share). In addition, the Astaris joint venture recorded charges related to the closure of certain of its production facilities. Solutia's share of these charges was approximately \$2 million (\$2 million aftertax, or \$0.02 per share). Excluding these special charges, equity earnings from affiliates increased primarily because of the formation and startup of the Astaris joint venture in April 2000, and improved sales volumes at the Flexsys and Advanced Elastomer Systems joint ventures.

The improvement in 1999 equity earnings over 1998 was due to strong sales volumes for the Flexsys joint venture, and the Advanced Elastomer Systems joint venture, in which Solutia has 50 percent ownership interests. In addition, Flexsys had higher earnings as the result of good manufacturing performance in its PPD2 unit, which started operations in 1998. The PPD2 unit produces 4-amino-diphenylamine, a product that extends the life of rubber products.

#### ***Sale of Polymer Modifiers Business***

In August 2000, Solutia completed the sale of its Polymer Modifiers business and related manufacturing facilities to Ferro Corporation for approximately \$130 million. As a result of this transaction, Solutia recognized a \$73 million pretax gain (\$46 million aftertax, or \$0.43 per share). Solutia's results of operations included net sales of approximately \$90 million in 2000, \$145 million in 1999 and \$147 million in 1998 and operating income of approximately \$16 million in 2000, \$36 million in 1999 and \$36 million in 1998, from the Polymer Modifiers business.

#### ***Other Income (Expense)—Net***

Other expense in 2000 totaled \$8 million. This compares to other income in 1999 of \$13 million and \$7 million in 1998. The decline in income was principally attributed to a charge of \$10 million (\$6 million aftertax, or \$0.06 per share) to reserve for advances and working capital loans to an Asian equity affiliate, \$14 million (\$8 million aftertax, or \$0.07 per share) for the write-down of certain equity-method investments in Asia based upon indicators that the loss in their values was other than temporary, charges of \$5 million (\$3 million aftertax, or \$0.03 per share) to accrue for debt payments under certain loan guarantees associated with one of the Asian equity investments and charges of \$8 million (\$5 million aftertax, or \$0.05 per share) associated with the startup and formation of the Astaris joint venture incurred during the second quarter of 2000. Partially offsetting the special charges was a \$15 million gain (\$9 million aftertax, or \$0.08 per share) resulting from the sale of substantially all of Solutia's 40 percent interest in P4 Production L.L.C., a phosphorus manufacturing venture.

#### ***Income Taxes***

In July 2000, Germany reduced its corporate tax rate effective January 1, 2001. In accordance with SFAS No. 109, "Accounting for Income Taxes," Solutia recognized income of \$7 million to income taxes to record the net effect of the change on deferred income tax assets and liabilities. Other items reducing Solutia's overall effective tax rate include effective tax planning strategies and a greater percentage of after-tax equity earnings from affiliates in pretax operating income.

### Summary of Special Charges and Other Events Affecting Comparability

Special charges recorded in 2000, 1999 and 1998 and other events affecting comparability have been summarized in the table below (dollars in millions).

|                                                           | 2000                                                        | 1999                 | 1998                 |
|-----------------------------------------------------------|-------------------------------------------------------------|----------------------|----------------------|
| Cost of goods sold.....                                   | \$ 8 (a)<br>53 (b)<br><u>91</u> (c)                         | \$ 63 (k)<br>(2) (l) | \$ (9) (m)<br>10 (n) |
| Total cost of goods sold.....                             | 152                                                         | 61                   | 1                    |
| Marketing, administrative and technological expenses..... | 6 (d)                                                       | —                    | —                    |
| Operating Income.....                                     | (158)                                                       | (61)                 | (1)                  |
| Equity earnings from affiliates.....                      | (2) (d)<br>(13) (e)                                         | —                    | —                    |
| Gain on sale of Polymer Modifiers business.....           | 73 (f)                                                      | —                    | —                    |
| Other income (expense)-net.....                           | (8) (d)<br>15 (g)<br>(14) (h)<br>(5) (h)<br><u>(10)</u> (i) | —                    | —                    |
| Income Before Income Taxes.....                           | (122)                                                       | (61)                 | (1)                  |
| Income taxes (benefit).....                               | (48) (j)                                                    | (23)                 | —                    |
| Net Income (Loss).....                                    | <u>\$ (74)</u>                                              | <u>\$ (38)</u>       | <u>\$ (1)</u>        |

- (a) Restructuring charge related to exiting operations at the Port Plastics site in Addyston, Ohio (\$8 million pretax, \$5 million aftertax, or \$0.05 per share).
- (b) Restructuring charge (\$53 million pretax, \$33 million aftertax, or \$0.31 per share) to cost of goods sold for work force reductions of approximately 700 people across all world areas and functions of the company and the closure of certain non-strategic facilities.
- (c) Impairment charge (\$91 million pretax, \$57 million aftertax, or \$0.53 per share) to cost of goods sold primarily for the write down of certain non-performing and non-strategic production assets in the Integrated Nylon segment.
- (d) Special operations charge related to the formation and startup of the Astaris joint venture (\$16 million pretax, \$11 million aftertax, or \$0.10 per share).
- (e) Special operations charge associated with the impairment and closure of certain manufacturing operations in the United Kingdom for the Flexsys joint venture (\$13 million pretax, \$13 million aftertax, or \$0.12 per share).
- (f) A gain on the sale of the Polymer Modifiers business and related manufacturing facilities (\$73 million pretax, \$46 million aftertax, or \$0.43 per share).
- (g) A gain on the sale of P4 Production L.L.C., a phosphorus manufacturing venture (\$15 million pretax, \$9 million aftertax, or \$0.08 per share).
- (h) Charges to write-down certain investments in Asia based upon indicators that the loss in their values was other than temporary (\$14 million pretax, \$8 million aftertax, or \$0.07 per share), and to accrue for payment of debt obligations associated with one of the investments (\$5 million pretax, \$3 million aftertax, or \$0.03 per share).
- (i) A charge (\$10 million pretax, \$6 million aftertax, or \$0.06 per share) primarily to reserve for advances and working capital loans to an Asian equity affiliate.
- (j) Amount represents the tax effect of the special charges and other events affecting comparability. Included in this line is the impact of a \$7 million (or \$0.07 per share) reduction in income tax expense for changes in German tax rates.
- (k) Special charge related to exiting Integrated Nylon's ammonia business, the write down of an Integrated Nylon segment bulk continuous filament spinning machine and the anticipated settlement of certain pending property claims litigation related to the Anniston, Alabama plant site (\$63 million pretax, \$40 million aftertax, or \$0.35 per share).
- (l) Reversal of excess restructuring reserves related to headcount reductions and facilities closures (\$2 million pretax, \$2 million aftertax, or \$0.02 per share).
- (m) Reversal of excess restructuring reserves related to headcount reductions and facilities closures (\$9 million pretax, \$6 million aftertax, or \$0.05 per share).
- (n) Charge for the write-down of certain slow-moving inventories and losses on the disposition of certain nonsalable inventories (\$10 million pretax, \$7 million aftertax, or \$0.06 per share).

### ***Outlook and Economic Conditions***

Solutia is affected by economic conditions, particularly those in the domestic housing industry and global automotive and textile industries. Each of these industries is cyclical. A general weakening of the economy in the United States impacted consumer demand in these marketplaces which negatively affected Solutia's sales volumes in the latter half of 2000.

During 2000, the cost of many feedstocks increased significantly as the price of crude oil increased above \$30 a barrel. During the second half of 2000, natural gas escalated in price even more dramatically than crude oil. Natural gas prices affect both feedstock and energy costs. Recent forecasts indicate that crude oil and natural gas prices may be moderating somewhat, but appear to have settled at a price that is 20 to 30 percent higher than historical averages. These markets remain volatile, which could cause feedstock and energy costs to fluctuate significantly during 2001. Solutia expects that average selling prices will rise for those products with formula pricing. Most of Solutia's products, however, do not have contracts with formula pricing. Solutia will continue to announce and implement a number of price increases focused on restoring margins. However, the delay in adjusting formula pricing and the difficulty in obtaining price increases because of competitive factors and a weaker economy in the United States will continue to negatively impact operating margins in 2001.

### **Financial Condition and Liquidity**

During February 2000, Solutia completed the issuance of €200 million (\$196 million) of notes, due February 2005. Proceeds from the notes were used primarily to refinance outstanding commercial paper, and also for general corporate purposes. At December 31, 2000, Solutia had outstanding commercial paper balances of \$485 million, a \$227 million reduction from the December 31, 1999, balance of \$712 million.

Solutia's commercial paper program is supported by an \$800 million, five-year revolving credit facility (\$800 million facility) with a syndicate of commercial banks. The \$800 million facility is also available for working capital and other general corporate purposes. This agreement, which expires in August 2002, was amended during November 1999, principally to allow the issuance of commercial paper in euros, as well as U.S. dollars.

During November 2000, Solutia put into place a \$250 million, 364-day multi-currency revolving credit agreement (\$250 million facility) with a syndicate of commercial banks. The \$250 million facility has terms that are generally consistent with the terms of the \$800 million facility. The \$250 million facility supports Solutia's commercial paper program and is available for working capital and other general corporate purposes.

In February 2000, Solutia acquired CarboGen Holdings, AG, a leading process research and development firm serving the global pharmaceutical industry. In March 2000, Solutia purchased AMCIS AG, a company serving the global pharmaceutical industry by developing production processes and by manufacturing active ingredients for clinical trials and small-volume commercial drugs. The combined purchase price for these acquisitions was approximately \$118 million, which was financed with commercial paper and the assumption of debt. During August 2000, Solutia received approximately \$130 million of proceeds associated with the sale of its Polymer Modifiers business and related manufacturing facilities. Also during August 2000, Solutia received \$85 million from its 50 percent-owned Astaris joint venture that represented a cash distribution and repayment of working capital loans.

In connection with the finalization of the external financing agreement for Astaris during the third quarter of 2000, Solutia and FMC Corporation have independently contractually agreed to provide Astaris with funding in the event the joint venture fails to meet certain financial benchmarks. Subsequent to December 31, 2000, Solutia received notification that such a contribution will be required in 2001. Solutia believes that this obligation is not likely to have a significant impact on its consolidated financial position, liquidity or profitability.

Solutia's working capital at December 31, 2000, decreased to negative \$334 million from negative \$213 million at December 31, 1999. The decrease in the working capital position primarily resulted from the sale of the Polymer Modifiers business and the contribution of the Phosphorus Derivatives business to the Astaris joint venture during 2000. Solutia's working capital position was further reduced by the impact of slowing economic conditions experienced during the second half of the year. At December 31, 2000, Solutia had short-term debt of \$494 million.

Cash from operations was \$244 million in 2000 as compared to \$364 million in 1999. The decrease was primarily attributable to lower net earnings associated with the sharp increase in petrochemical and natural gas costs during 2000.

Capital expenditures for 2000 were \$221 million. These expenditures were used to fund various cost reduction, maintenance and capacity expansion projects. The company expects that its capital requirements will be approximately \$130 million in 2001, principally for capacity expansion and cost reduction projects. Approximately \$7 million of 2001 estimated capital requirements were committed at December 31, 2000.

Solutia had a shareholders' deficit of \$34 million at December 31, 2000, which compares with shareholders' equity of \$82 million at December 31, 1999. This \$116 million decline was principally caused by an \$86 million decline in the currency translation adjustment, principally related to the devaluation of the euro, included in Accumulated Other Comprehensive Income (Loss) and share repurchases which more than offset Solutia's net income in 2000.

During 2000, Solutia repurchased 7.7 million shares of its common stock at a cost of \$106 million. On April 26, 2000, the Board of Directors authorized the repurchase of up to 15 million additional shares of Solutia common stock. Under this authorization, Solutia has the authority to repurchase an additional 12.1 million shares of its common stock.

Solutia believes that its cash flow from operations and available borrowing capacity under the \$800 million facility and the \$250 million facility provide sufficient resources to finance its operations and planned capital needs for the next 12 months.

#### **Environmental Matters**

Solutia continues its strong commitment to comply with laws and government regulations concerning environmental matters and employee safety and health in the United States and other countries. U.S. environmental legislation that has a particular impact on the company includes the Toxic Substances Control Act; the Resource Conservation and Recovery Act; the Clean Air Act; the Clean Water Act; the Safe Drinking Water Act; and the Comprehensive Environmental Response, Compensation and Liability Act (commonly known as Superfund). The company is also subject to the Occupational Safety and Health Act and regulations of the Occupational Safety and Health Administration ("OSHA") concerning employee safety and health matters. The U.S. Environmental Protection Agency, OSHA and other federal agencies have the authority to promulgate regulations that have an impact on the company's operations. In addition to these federal activities, various states have been delegated certain authority under several of these federal statutes. Many state and local governments have adopted environmental and employee safety and health laws and regulations, many of which meet federal requirements for delegation of federal mandates to state entities. State or federal agencies having enforcement lead authority may seek fines and penalties for violation of these laws and regulations.

Solutia is dedicated to long-term environmental protection and compliance programs that reduce and monitor emissions of hazardous materials into the environment as well as to the remediation of identified existing environmental concerns. Solutia is among the leaders in Responsible Care, the chemical industry's performance-enhancement program.

Expenditures in 2000 were approximately \$12 million for environmental capital projects and approximately \$111 million for the management of environmental programs, including the operation and maintenance of facilities for environmental control, of which \$28 million was charged against recorded environmental liabilities. Solutia estimates that a total of approximately \$20 million will be spent during 2001 and 2002 on additional capital projects for environmental protection and that expenses for the management of environmental programs in 2001 and 2002 will increase slightly from the 2000 levels.

With respect to environmental remediation obligations, our policy is to accrue costs for remediation of contaminated sites in the accounting period in which the obligation becomes probable and the cost is reasonably estimable.

At the time of the spinoff, Solutia assumed from the former Monsanto Company (now Pharmacia Corporation), under the Distribution Agreement between Monsanto and Solutia, liabilities related to specified Superfund proceedings. As a result, while Monsanto remains the named potentially responsible party or defendant for actions that occurred before September 1, 1997, Solutia will manage these proceedings and litigation against Monsanto and indemnify it for any costs, expenses and judgments arising from these proceedings.

Solutia's estimates of its liabilities for Superfund sites are based on evaluations of currently available facts with respect to each individual site and take into consideration factors such as existing technology, laws and agency policy and prior experience in remediation of contaminated sites. As assessments and remediation activities progress at individual sites, these liabilities are reviewed periodically and adjusted to reflect additional technical, engineering and legal information that becomes available. Solutia has an accrued liability of \$33 million as of December 31, 2000, for Superfund sites. Major Superfund sites in this category include the noncompany-owned sites at Brio and MOTCO in Texas, and Fike/Artel in West Virginia, which account for \$23 million of the accrued amount. Solutia spent approximately \$7 million in 2000 for remediation of Superfund sites. Similar amounts can be expected in future years.

Solutia had an accrued liability of \$69 million as of December 31, 2000, for plants no longer in operation and third-party sites for which it assumed responsibility under the Distribution Agreement entered into with Monsanto. Solutia's estimate of its liability related to these sites is based on evaluations of currently available facts with respect to each individual site. The estimate takes into consideration factors such as existing technology, laws and agency policy and prior experience in remediation of contaminated sites. The company spent \$9 million in 2000 for remediation of these sites. Similar amounts can be expected in future years.

Solutia had an accrued liability of \$79 million as of December 31, 2000, for solid and hazardous waste remediation, and for post-closure costs at the company's operating locations. Solutia recognizes certain post-closure costs over the estimated remaining useful life of the related facilities. Solutia spent \$12 million in 2000 for remediation of these facilities. Similar amounts can be expected in future years.

Uncertainties related to all of Solutia's environmental liabilities include evolving government policy and regulations, the method and extent of remediation and future changes in technology. Because of these uncertainties, Solutia estimates that potential future expenses associated with these liabilities could be an additional \$20 million to \$30 million. Although the ultimate costs and results of remediation of contaminated sites cannot be predicted with certainty, they are not expected to result in a material adverse effect on Solutia's consolidated financial position, liquidity or profitability in any one year.

#### **Derivative Financial Instruments**

Solutia's business operations give rise to market risk exposures that result from changes in currency exchange rates, interest rates and certain commodity prices. To manage the volatility relating to these exposures, Solutia enters into various hedging transactions that enable it to alleviate the adverse effects of financial market risk. Solutia's hedging transactions are carried out under policies and procedures approved by the Audit and Finance Committee of the Board of Directors, which do not permit the purchase or holding of any derivative financial instruments for trading purposes.

Solutia uses value-at-risk ("VAR") testing and analysis to measure and control risks. VAR estimates the loss in fair market value, which Solutia would potentially incur, given a certain move in market prices over a certain period of time, using specified confidence levels. The tests discussed below for exposure to interest rate and currency rate exposures are based on a one-day horizon and a 95 percent confidence level. The model assumes that financial returns are normally distributed. The VAR model takes into account correlations and diversification across market factors, including currencies and interest rates. Estimates of volatility and correlations of market factors are drawn from the JP Morgan RiskMetrics dataset as of December 31, 2000. In cases where data is unavailable, a reasonable approximation is included. Solutia estimates that the maximum loss that could arise in one day is not material.

#### ***Foreign Currency Exchange Rate Risk***

Currency forward contracts are used to manage currency exposures for financial instruments denominated in currencies other than the entity's functional currency. Gains and losses on contracts that are designated and effective

as hedges are included in net income and offset the exchange gain or loss of the transaction being hedged. Solutia's policy prescribes the range of allowable hedging activity and the instruments that are permitted for use. Because the counterparties to these contracts are major international financing institutions, credit risk arising from these contracts is not significant, and Solutia does not anticipate any counterparty losses. This hedging activity is intended to protect Solutia from adverse fluctuations in foreign currency exchange rates.

At December 31, 2000, Solutia had currency forward contracts to purchase \$265 million and sell \$265 million of other currencies, principally the euro, Swiss Franc and United Kingdom Pound-Sterling, with average maturities of 10 months. Net unrealized hedging gains at December 31, 2000, were not material.

Based on the company's overall currency rate exposure at December 31, 2000, including derivative and other foreign currency sensitive instruments, a near-term change in currency rates, within a 95 percent confidence level based on historical currency rate movements, would not materially affect Solutia's consolidated financial position, results of operations or cash flows.

#### ***Interest Rate Risk***

Interest rate risk is primarily related to the changes in fair value of fixed-rate long-term debt and short-term, floating rate debt. Solutia does not actively manage interest rate risk. Based on the company's overall interest rate exposure at December 31, 2000, a near-term change in interest rates, within a 95 percent confidence level based on historical interest rate movements, would not materially affect the consolidated financial position, results of operations or cash flows of the company. This is consistent with the overall interest rate exposure at December 31, 1999.

#### ***Commodity Price Risk***

Certain raw materials and energy sources are subject to price volatility caused by weather, crude oil prices, supply and demand conditions and other unpredictable factors. Solutia periodically employs commodity price option contracts to hedge some of this exposure. The commodity price risk associated with the derivative instruments is not material to Solutia's consolidated financial position, results of operations or cash flow.

#### **Recently Issued Accounting Standards**

Effective January 1, 2001, Solutia adopted SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activity," which provides comprehensive and consistent standards for the recognition and measurement of derivative and hedging activities. The adoption of SFAS No. 133 did not have a material effect on Solutia's consolidated financial statements.

During the fourth quarter of 2000, Solutia adopted Staff Accounting Bulletin 101, "Revenue Recognition in Financial Statements" (SAB 101) which provides guidance related to revenue recognition. The adoption of SAB 101 did not have a material effect on Solutia's consolidated financial statements.

#### **Item 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.**

The information appearing under "Derivative Financial Instruments" on pages 23 and 24 above is incorporated here by reference.

**Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.**

**FINANCIAL SECTION—TABLE OF CONTENTS**

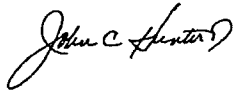
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## MANAGEMENT REPORT

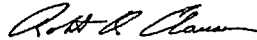
Management is responsible for the integrity, objectivity and preparation of Solutia Inc.'s consolidated financial statements and all of the related information appearing in this annual report. The statements have been prepared in accordance with accounting principles generally accepted in the United States of America. Where necessary, this information reflects estimates that are based upon currently available information and management's judgments.

Management is also responsible for maintaining a system of internal accounting controls designed to provide reasonable assurance that Solutia's assets are safeguarded against material loss from unauthorized use or disposition and that authorized transactions are properly recorded to permit the preparation of accurate financial information. Cost/benefit judgments are an important consideration in this regard. The effectiveness of internal controls is maintained by careful personnel selection and thorough training, division of responsibilities, establishment and communication of policies and ongoing internal review programs and audits.

Management believes that Solutia's system of internal accounting controls as of and for the period ended December 31, 2000, was effective and adequate to accomplish the objectives described above.



John C. Hunter III  
Chairman, President and  
Chief Executive Officer



Robert A. Clausen  
Senior Vice President and  
Chief Financial Officer

February 28, 2001

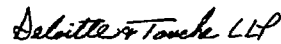
## REPORT OF INDEPENDENT AUDITORS

To the Shareholders of Solutia Inc.:

We have audited the accompanying statements of consolidated financial position of Solutia Inc. and subsidiaries as of December 31, 2000 and 1999, and the related statements of consolidated income, comprehensive income (loss), cash flow, and shareholders' equity (deficit) for each of the three years in the period ended December 31, 2000. Our audits also included the financial statement schedule listed in the Index at Item 14. These financial statements and the financial statement schedule are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements and the financial statement schedule based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Solutia Inc. and subsidiaries as of December 31, 2000 and 1999, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2000, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly in all material respects the information set forth therein.



Deloitte & Touche LLP  
St. Louis, Missouri

February 28, 2001

**SOLUTIA INC.**  
**STATEMENT OF CONSOLIDATED INCOME**  
(Dollars in millions, except per share amounts)

|                                                                                                    | Year Ended December 31, |                |                |
|----------------------------------------------------------------------------------------------------|-------------------------|----------------|----------------|
|                                                                                                    | 2000                    | 1999           | 1998           |
| Net Sales .....                                                                                    | \$3,185                 | \$2,830        | \$2,835        |
| Cost of goods sold .....                                                                           | <u>2,699</u>            | <u>2,178</u>   | <u>2,085</u>   |
| <b>Gross Profit</b> .....                                                                          | <b>486</b>              | <b>652</b>     | <b>750</b>     |
| Marketing expenses .....                                                                           | 165                     | 153            | 145            |
| Administrative expenses .....                                                                      | 173                     | 122            | 136            |
| Technological expenses .....                                                                       | 91                      | 80             | 83             |
| Amortization expense .....                                                                         | <u>33</u>               | <u>3</u>       | <u>—</u>       |
| <b>Operating Income</b> .....                                                                      | <b>24</b>               | <b>294</b>     | <b>386</b>     |
| Equity earnings from affiliates .....                                                              | 35                      | 36             | 25             |
| Interest expense .....                                                                             | (83)                    | (40)           | (43)           |
| Gain on sale of Polymer Modifiers business .....                                                   | 73                      | —              | —              |
| Other income (expense)—net .....                                                                   | <u>(8)</u>              | <u>13</u>      | <u>7</u>       |
| <b>Income Before Income Taxes</b> .....                                                            | <b>41</b>               | <b>303</b>     | <b>375</b>     |
| Income taxes (benefit) .....                                                                       | <u>(8)</u>              | <u>97</u>      | <u>126</u>     |
| <b>Net Income</b> .....                                                                            | <b>\$ 49</b>            | <b>\$ 206</b>  | <b>\$ 249</b>  |
| <b>Basic Earnings per Share</b> .....                                                              | <b>\$ 0.46</b>          | <b>\$ 1.86</b> | <b>\$ 2.16</b> |
| <b>Diluted Earnings per Share</b> .....                                                            | <b>\$ 0.46</b>          | <b>\$ 1.80</b> | <b>\$ 2.03</b> |
| Weighted average equivalent shares (in millions):                                                  |                         |                |                |
| Basic .....                                                                                        | 105.9                   | 110.8          | 115.5          |
| Effect of dilutive securities:                                                                     |                         |                |                |
| Common share equivalents—common stock issuable upon exercise of<br>outstanding stock options ..... | <u>1.6</u>              | <u>3.8</u>     | <u>7.3</u>     |
| Diluted .....                                                                                      | <u>107.5</u>            | <u>114.6</u>   | <u>122.8</u>   |

**STATEMENT OF CONSOLIDATED COMPREHENSIVE INCOME (LOSS)**  
(Dollars in millions)

|                                                                                                         | Year Ended December 31, |              |              |
|---------------------------------------------------------------------------------------------------------|-------------------------|--------------|--------------|
|                                                                                                         | 2000                    | 1999         | 1998         |
| Net Income .....                                                                                        | \$ 49                   | \$206        | \$249        |
| <b>Other Comprehensive Income (Loss):</b>                                                               |                         |              |              |
| Currency translation adjustments .....                                                                  | (86)                    | (44)         | 10           |
| Minimum pension liability adjustments, net of tax of \$4 in 2000, \$2 in 1999, and \$2<br>in 1998 ..... | <u>7</u>                | <u>(4)</u>   | <u>(3)</u>   |
| <b>Comprehensive Income (Loss)</b> .....                                                                | <b>\$ (30)</b>          | <b>\$158</b> | <b>\$256</b> |

See accompanying Notes to Consolidated Financial Statements.

**SOLUTIA INC.**  
**STATEMENT OF CONSOLIDATED FINANCIAL POSITION**  
(Dollars in millions, except per share amounts)

|                                                                                                            | As of December 31, |                |
|------------------------------------------------------------------------------------------------------------|--------------------|----------------|
|                                                                                                            | 2000               | 1999           |
| <b>ASSETS</b>                                                                                              |                    |                |
| <b>Current Assets:</b>                                                                                     |                    |                |
| Cash and cash equivalents .....                                                                            | \$ 19              | \$ 28          |
| Trade receivables, net of allowances of \$12 in 2000 and \$12 in 1999 .....                                | 406                | 483            |
| Miscellaneous receivables and prepaid expenses .....                                                       | 126                | 131            |
| Deferred income tax benefit .....                                                                          | 107                | 101            |
| Inventories .....                                                                                          | 357                | 371            |
| <b>Total Current Assets .....</b>                                                                          | <b>1,015</b>       | <b>1,114</b>   |
| <b>Property, Plant and Equipment:</b>                                                                      |                    |                |
| Land .....                                                                                                 | 60                 | 68             |
| Buildings .....                                                                                            | 421                | 436            |
| Machinery and equipment .....                                                                              | 2,982              | 2,919          |
| Construction in progress .....                                                                             | 62                 | 272            |
| <b>Total property, plant and equipment .....</b>                                                           | <b>3,525</b>       | <b>3,695</b>   |
| <b>Less accumulated depreciation .....</b>                                                                 | <b>2,320</b>       | <b>2,379</b>   |
| <b>Net Property, Plant and Equipment .....</b>                                                             | <b>1,205</b>       | <b>1,316</b>   |
| <b>Investments in Affiliates .....</b>                                                                     | <b>351</b>         | <b>377</b>     |
| <b>Goodwill, net of accumulated amortization of \$24 in 2000 and \$2 in 1999 .....</b>                     | <b>421</b>         | <b>511</b>     |
| <b>Identified Intangible Assets, net of accumulated amortization of \$16 in 2000 and \$5 in 1999 .....</b> | <b>217</b>         | <b>33</b>      |
| <b>Long-Term Deferred Income Tax Benefit .....</b>                                                         | <b>190</b>         | <b>232</b>     |
| <b>Other Assets .....</b>                                                                                  | <b>182</b>         | <b>187</b>     |
| <b>Total Assets .....</b>                                                                                  | <b>\$3,581</b>     | <b>\$3,770</b> |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)</b>                                                      |                    |                |
| <b>Current Liabilities:</b>                                                                                |                    |                |
| Accounts payable .....                                                                                     | \$ 359             | \$ 312         |
| Wages and benefits .....                                                                                   | 45                 | 59             |
| Postretirement liabilities .....                                                                           | 78                 | 86             |
| Miscellaneous accruals .....                                                                               | 373                | 359            |
| Short-term debt .....                                                                                      | 494                | 511            |
| <b>Total Current Liabilities .....</b>                                                                     | <b>1,349</b>       | <b>1,327</b>   |
| <b>Long-Term Debt .....</b>                                                                                | <b>784</b>         | <b>802</b>     |
| <b>Postretirement Liabilities .....</b>                                                                    | <b>941</b>         | <b>998</b>     |
| <b>Other Liabilities .....</b>                                                                             | <b>541</b>         | <b>561</b>     |
| <b>Shareholders' Equity (Deficit):</b>                                                                     |                    |                |
| Common stock (authorized, 600,000,000 shares, par value \$0.01)                                            |                    |                |
| Issued: 118,400,635 shares in 2000 and 1999 .....                                                          | 1                  | 1              |
| Additional contributed capital .....                                                                       | (141)              | (137)          |
| Treasury stock, at cost (15,484,194 and 8,859,764 shares in 2000 and 1999, respectively) .....             | (296)              | (209)          |
| Unearned ESOP shares .....                                                                                 | (9)                | (18)           |
| Accumulated other comprehensive income (loss) .....                                                        | (108)              | (29)           |
| Reinvested earnings .....                                                                                  | 519                | 474            |
| <b>Total Shareholders' Equity (Deficit) .....</b>                                                          | <b>(34)</b>        | <b>82</b>      |
| <b>Total Liabilities and Shareholders' Equity (Deficit) .....</b>                                          | <b>\$3,581</b>     | <b>\$3,770</b> |

See accompanying Notes to Consolidated Financial Statements.

**SOLUTIA INC.**  
**STATEMENT OF CONSOLIDATED CASH FLOW**  
(Dollars in millions)

|                                                                | Year Ended December 31, |                |              |
|----------------------------------------------------------------|-------------------------|----------------|--------------|
|                                                                | 2000                    | 1999           | 1998         |
| <b>INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>        |                         |                |              |
| <b>OPERATING ACTIVITIES:</b>                                   |                         |                |              |
| Net income .....                                               | \$ 49                   | \$ 206         | \$ 249       |
| Adjustments to reconcile to Cash From Operations:              |                         |                |              |
| Items that did not use (provide) cash:                         |                         |                |              |
| Deferred income taxes .....                                    | 23                      | 23             | 32           |
| Depreciation and amortization .....                            | 191                     | 151            | 147          |
| Amortization of deferred credits .....                         | (12)                    | (10)           | (7)          |
| Restructuring expenses and other special charges—net.....      | 195                     | 63             | —            |
| Other .....                                                    | (15)                    | 15             | 17           |
| Working capital changes that provided (used) cash:             |                         |                |              |
| Trade receivables .....                                        | 69                      | (18)           | 68           |
| Inventories .....                                              | (18)                    | 42             | (6)          |
| Accounts payable and accrued liabilities .....                 | (64)                    | (114)          | 3            |
| Other .....                                                    | (1)                     | 6              | 15           |
| Net pretax gains from asset disposals .....                    | (79)                    | —              | —            |
| Other items .....                                              | (94)                    | —              | 19           |
| <b>Cash From Operations .....</b>                              | <b>244</b>              | <b>364</b>     | <b>537</b>   |
| <b>INVESTING ACTIVITIES:</b>                                   |                         |                |              |
| Property, plant and equipment purchases .....                  | (221)                   | (257)          | (158)        |
| Acquisition and investment payments, net of cash acquired..... | (110)                   | (835)          | (8)          |
| Property disposals and investment proceeds.....                | 220                     | 30             | 22           |
| <b>Cash Used in Investing Activities .....</b>                 | <b>(111)</b>            | <b>(1,062)</b> | <b>(144)</b> |
| <b>FINANCING ACTIVITIES:</b>                                   |                         |                |              |
| Net change in short-term debt obligations .....                | (23)                    | 511            | (190)        |
| Long-term debt proceeds .....                                  | —                       | 201            | —            |
| Long-term debt reductions .....                                | (13)                    | —              | —            |
| Treasury stock purchases.....                                  | (106)                   | (79)           | (161)        |
| Dividend payments .....                                        | (4)                     | (4)            | (5)          |
| Common stock issued under employee stock plans.....            | 4                       | 8              | 28           |
| <b>Cash (Used in) From Financing Activities .....</b>          | <b>(142)</b>            | <b>637</b>     | <b>(328)</b> |
| <b>INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS .....</b>  | <b>(9)</b>              | <b>(61)</b>    | <b>65</b>    |
| <b>CASH AND CASH EQUIVALENTS:</b>                              |                         |                |              |
| Beginning of year .....                                        | 28                      | 89             | 24           |
| End of year .....                                              | \$ 19                   | \$ 28          | \$ 89        |

See accompanying Notes to Consolidated Financial Statements.

The effect of exchange rate changes on cash and cash equivalents was not material. Cash payments for interest (net of amounts capitalized) were \$88 million in 2000, \$41 million in 1999 and \$44 million in 1998. Cash payments for income taxes were \$17 million in 2000, \$43 million in 1999 and \$94 million in 1998.

**SOLUTIA INC.**  
**STATEMENT OF CONSOLIDATED SHAREHOLDERS' EQUITY (DEFICIT)**  
(Dollars in millions)

|                                                                                                                                    | Year Ended December 31, |              |               |
|------------------------------------------------------------------------------------------------------------------------------------|-------------------------|--------------|---------------|
|                                                                                                                                    | 2000                    | 1999         | 1998          |
| <b>COMMON STOCK:</b>                                                                                                               |                         |              |               |
| Balance, January 1 .....                                                                                                           | \$ 1                    | \$ 1         | \$ 1          |
| Balance, December 31 .....                                                                                                         | \$ 1                    | \$ 1         | \$ 1          |
| <b>ADDITIONAL CONTRIBUTED CAPITAL:</b>                                                                                             |                         |              |               |
| Balance, January 1 .....                                                                                                           | \$(137)                 | \$(131)      | \$(119)       |
| Employee stock plans and ESOP .....                                                                                                | (4)                     | (6)          | (12)          |
| Balance, December 31 .....                                                                                                         | \$(141)                 | \$(137)      | \$(131)       |
| <b>TREASURY STOCK:</b>                                                                                                             |                         |              |               |
| Balance, January 1 .....                                                                                                           | \$(209)                 | \$(143)      | \$ (22)       |
| Shares purchased (7,717,300 shares in 2000, 3,781,700 shares in 1999,<br>6,246,300 shares in 1998) .....                           | (106)                   | (79)         | (161)         |
| Net shares issued under employee stock plans (1,092,870 shares in 2000,<br>551,613 shares in 1999, 1,609,451 shares in 1998) ..... | 19                      | 13           | 40            |
| Balance, December 31 .....                                                                                                         | \$(296)                 | \$(209)      | \$(143)       |
| <b>UNEARNED ESOP SHARES:</b>                                                                                                       |                         |              |               |
| Balance, January 1 .....                                                                                                           | \$ (18)                 | \$ (25)      | \$ (31)       |
| Amortization of ESOP balance .....                                                                                                 | 9                       | 7            | 6             |
| Balance, December 31 .....                                                                                                         | \$ (9)                  | \$ (18)      | \$ (25)       |
| <b>ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS):</b>                                                                              |                         |              |               |
| <b>ACCUMULATED CURRENCY ADJUSTMENT:</b>                                                                                            |                         |              |               |
| Balance, January 1 .....                                                                                                           | (15)                    | 29           | 19            |
| Currency translation adjustments .....                                                                                             | (86)                    | (44)         | 10            |
| Balance, December 31 .....                                                                                                         | (101)                   | (15)         | 29            |
| <b>MINIMUM PENSION LIABILITY:</b>                                                                                                  |                         |              |               |
| Balance, January 1 .....                                                                                                           | (14)                    | (10)         | (7)           |
| Minimum pension liability adjustments .....                                                                                        | 7                       | (4)          | (3)           |
| Balance, December 31 .....                                                                                                         | (7)                     | (14)         | (10)          |
| Balance, December 31 .....                                                                                                         | \$(108)                 | \$ (29)      | \$ 19         |
| <b>REINVESTED EARNINGS:</b>                                                                                                        |                         |              |               |
| Balance, January 1 .....                                                                                                           | \$ 474                  | \$ 272       | \$ 28         |
| Net income .....                                                                                                                   | 49                      | 206          | 249           |
| Dividends .....                                                                                                                    | (4)                     | (4)          | (5)           |
| Balance, December 31 .....                                                                                                         | \$ 519                  | \$ 474       | \$ 272        |
| <b>TOTAL SHAREHOLDERS' EQUITY (DEFICIT) .....</b>                                                                                  | <b>\$ (34)</b>          | <b>\$ 82</b> | <b>\$ (7)</b> |

See accompanying Notes to Consolidated Financial Statements.

## SOLUTIA INC.

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in millions, except per share amounts)

#### 1. Significant Accounting Policies

##### *Nature of Operations*

Solutia Inc. and its subsidiaries produce and market a variety of high-performance chemical-based materials. Solutia's strategic focus is built on key strengths, including complex manufacturing capabilities, process engineering expertise, technical service, customer problem solving, polymer chemistry and fiber technology. These world-class skills are applied to create solutions and products for customers in the consumer, household, automotive, industrial products and pharmaceutical industries. Solutia's products and services include SAFLEX® plastic interlayer; window and industrial films; GELVA® pressure-sensitive adhesives; liquid, powder and waterborne resins; VYDYNE® and ASCEND™ nylon polymers; process research, process development and scale-up services for the pharmaceutical industry; and nylon fibers.

Prior to September 1, 1997, Solutia was a wholly-owned subsidiary of the former Monsanto Company (now known as Pharmacia Corporation). On September 1, 1997, Monsanto distributed all of the outstanding shares of common stock of the company as a dividend to Monsanto stockholders (the spinoff). As a result of the spinoff, on September 1, 1997, Solutia became an independent publicly held company listed on the New York Stock Exchange and its operations ceased to be owned by Monsanto. Negative additional contributed capital arose upon the spinoff.

##### *Basis of Consolidation*

The consolidated financial statements include the accounts of Solutia and its majority-owned subsidiaries. Other companies in which Solutia has a significant interest (20 to 50 percent) are included in "Investments in Affiliates" in the Statement of Consolidated Financial Position. Solutia's share of these companies' net earnings or losses is reflected in "Equity Earnings from Affiliates" in the Statement of Consolidated Income.

##### *Use of Estimates*

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and that affect revenues and expenses during the period reported. Estimates are adjusted when necessary to reflect actual experience. Significant estimates were used to account for restructuring reserves, environmental reserves, self-insurance reserves, employee benefit plans, asset impairments and contingencies.

##### *Cash and Cash Equivalents*

Cash and cash equivalents consist of cash and temporary investments with maturities of three months or less when purchased.

##### *Inventory Valuation*

Inventories are stated at cost or market, whichever is less. Actual cost is used to value raw materials and supplies. Standard cost, which approximates actual cost, is used to value finished goods and goods in process. Standard cost includes direct labor and raw materials, and manufacturing overhead based on practical capacity. The cost of certain inventories (69 percent as of December 31, 2000) is determined by the last-in, first-out (LIFO) method, which generally reflects the effects of inflation or deflation on cost of goods sold sooner than other inventory cost methods. The cost of other inventories generally is determined by the first-in, first-out (FIFO) method.

## SOLUTIA INC.

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

#### *Property, Plant and Equipment*

Property, plant and equipment are recorded at cost. The cost of plant and equipment is depreciated over weighted average periods of 20 years for buildings and 12 years for machinery and equipment, by the straight-line method.

#### *Intangible Assets*

The cost of intangible assets is amortized on a straight-line basis over the estimated periods benefited, generally 20 years for goodwill and periods ranging from 5 to 20 years for identified intangible assets.

#### *Impairment of Long-Lived Assets*

Impairment tests of long-lived assets are made when conditions indicate a possible loss. Such impairment tests are based on a comparison of undiscounted cash flows to the recorded value of the asset. If an impairment is indicated, the asset value is written down to its fair value based upon market prices or, if not available, upon discounted cash value, at an appropriate discount rate.

#### *Environmental Remediation*

Costs for remediation of waste disposal sites are accrued in the accounting period in which the obligation is probable and when the cost is reasonably estimable. Postclosure costs for hazardous and other waste facilities at operating locations are accrued over the estimated life of the facility as part of its anticipated closure cost. Environmental liabilities are not discounted, and they have not been reduced for any claims for recoveries from insurance or third parties. In those cases where insurance carriers or third-party indemnitors have agreed to pay any amounts and management believes that collectability of such amounts is probable, the amounts are reflected as receivables in the consolidated financial statements.

#### *Revenue Recognition*

Revenues are recorded when products are shipped. In the case of the pharmaceutical services businesses, revenues are primarily recorded on a percentage of completion method.

#### *Derivative Financial Instruments*

Currency forward contracts are used to manage currency exposures for financial instruments denominated in currencies other than the entity's functional currency. Natural gas contracts are used to manage some of the exposure for the cost of natural gas. Gains and losses on contracts that are designated and effective as hedges are included in net income and offset the exchange gain or loss of the transaction being hedged.

Major currencies affecting the company's business are the U.S. dollar, the British pound sterling, the euro, the Canadian dollar and the Brazilian real. Currency restrictions are not expected to have a significant effect on Solutia's cash flow, liquidity or capital resources.

#### *Income Taxes*

Solutia accounts for income taxes using the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences of temporary differences between the carrying amounts and tax bases of assets and liabilities at enacted rates.

#### *Currency Translation*

The local currency has been used as the functional currency for nearly all worldwide locations. The financial statements for most of Solutia's ex-U.S. operations are translated into U.S. dollars at current exchange rates.

## SOLUTIA INC.

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Unrealized currency translation adjustments in the Statement of Consolidated Financial Position are accumulated in equity.

#### *Earnings per Share*

Solutia measures earnings per share under the guidance of Statement of Financial Accounting Standards (SFAS) No. 128, "Earnings per Share." Basic earnings per share is a measure of operating performance that assumes no dilution from securities or contracts to issue common stock. Diluted earnings per share is a measure of operating performance by giving effect to the dilution that would occur if securities or contracts to issue common stock were exercised or converted.

#### *New Accounting Pronouncements*

Effective January 1, 2001, Solutia adopted SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activity," which provides comprehensive and consistent standards for the recognition and measurement of derivative and hedging activities. The adoption of SFAS No. 133 did not have a material effect on Solutia's consolidated financial statements.

During the fourth quarter of 2000, Solutia adopted Staff Accounting Bulletin 101, "Revenue Recognition in Financial Statements" (SAB 101) which provides guidance related to revenue recognition. The adoption of SAB 101 did not have a material effect on Solutia's consolidated financial statements.

#### *Reclassifications*

Certain reclassifications to prior years' financial information have been made to conform to the 2000 presentation.

## **2. Acquisitions and Divestitures**

During the third quarter of 2000, Solutia completed the sale of its Polymer Modifiers business and related manufacturing facilities to Ferro Corporation for approximately \$130 million. As a result of this transaction, Solutia recognized a \$73 million pretax gain (\$46 million aftertax). Solutia's results of operations included net sales of approximately \$90 million in 2000, \$145 million in 1999 and \$147 million in 1998 and operating income of approximately \$16 million in 2000, \$36 million in 1999 and \$36 million in 1998, from the Polymer Modifiers business. During the second quarter of 2000, Solutia recognized a \$15 million pretax gain (\$9 million aftertax) on the sale of substantially all of its minority interest in P4 Production L.L.C., a phosphorus manufacturing venture. The results of operations from Solutia's minority interest in P4 Production L.L.C. were not material to Solutia's consolidated results of operations.

During the first quarter of 2000, Solutia completed two acquisitions in the Specialty Products segment, which provide custom process and technology services to the global pharmaceutical industry. In the first acquisition, which closed on February 10, Solutia acquired CarboGen Holdings AG. CarboGen is a leading process research and development firm. In the second acquisition, which closed on March 24, Solutia purchased AMCIS AG. AMCIS serves the global pharmaceutical industry by developing production processes and by manufacturing active ingredients for clinical trials and small-volume commercial drugs. The combined purchase price for these acquisitions was approximately \$118 million, which was financed with commercial paper and the assumption of debt.

Both of the acquisitions have been accounted for using the purchase method. The allocations of the purchase price to the assets and liabilities acquired resulted in current assets of \$17 million, non-current assets of \$27 million, goodwill of \$57 million, other intangible assets of \$41 million, current liabilities of \$21 million and non-current liabilities of \$3 million. Goodwill is being amortized over its estimated useful life of 20 years, and other intangible assets are being amortized over their estimated useful lives, which average 18 years.

## SOLUTIA INC.

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Results of operations for CarboGen and AMCIS were included in Solutia's results of operations from the acquisition dates. The results of operations for the acquired businesses were not material to Solutia's consolidated results of operations for 2000.

On December 22, 1999, Solutia acquired Vianova Resins from Morgan Grenfell Private Equity Ltd. for approximately 1.2 billion deutsche marks (approximately \$617 million), which was financed with commercial paper and the assumption of debt. Vianova Resins is a leading European producer of resins and additives for coatings and technical applications for the specialty, industrial and automotive sectors.

The acquisition has been accounted for using the purchase method. The allocation of the purchase price to the assets and liabilities acquired resulted in current assets of \$192 million, non-current assets of \$227 million, goodwill of \$321 million, other intangible assets of approximately \$163 million, current liabilities of \$99 million and non-current liabilities of \$187 million. Goodwill is being amortized over its estimated useful life of 20 years, and other intangible assets are being amortized over their estimated useful lives, which average 19 years.

On May 25, 1999, Solutia acquired CPFilms Inc. from Akzo Nobel N.V. for approximately \$200 million, which was financed with commercial paper. CPFilms is a leading manufacturer and marketer of window film and other high-technology film products for automotive and architectural after-markets and a variety of other specialty film applications. The acquisition has been accounted for using the purchase method. The allocation of the purchase price to the identifiable assets and liabilities acquired resulted in goodwill of approximately \$80 million. Goodwill and other intangible assets will be amortized over their estimated useful lives of 20 years. CPFilms' results of operations from May 25, 1999, through December 31, 1999, were included in Solutia's Statement of Consolidated Income for the year ended December 31, 1999.

The following unaudited pro forma condensed information for the years ended December 31, 1999 and 1998, give effect to the acquisitions of CPFilms and Vianova Resins, and the associated debt financing, as if the acquisitions and the financing had occurred as of the beginning of the periods presented.

|                                  | For the Year Ended<br>December 31 |         |
|----------------------------------|-----------------------------------|---------|
|                                  | 1999                              | 1998    |
| <i>(Unaudited)</i>               |                                   |         |
| Net sales .....                  | \$3,357                           | \$3,465 |
| Net income.....                  | 203                               | 241     |
| Basic earnings per share .....   | 1.83                              | 2.09    |
| Diluted earnings per share ..... | 1.77                              | 1.97    |

### 3. Restructuring and Business Combination Reserves

During the fourth quarter of 2000, Solutia recorded restructuring charges of \$53 million (\$33 million aftertax) to cost of goods sold for costs associated with work force reductions of approximately 700 people across all world areas of the company and the closure of certain non-strategic facilities. The restructuring actions are expected to be carried out by the end of 2001. Approximately 80 percent of the workforce reductions are planned for North American business and manufacturing operations, and approximately 20 percent are planned for European, Asian and Latin American operations and sales offices. Management and senior management positions represent approximately one-third of the workforce reductions. The closure of non-strategic facilities is not anticipated to have a significant impact on future operations.

# SOLUTIA INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table summarizes the 2000 restructuring charge and amounts utilized to carry out those plans:

|                                          | Employment<br>Reductions | Shutdown of<br>Facilities | Total              |
|------------------------------------------|--------------------------|---------------------------|--------------------|
| Balance at January 1, 2000 .....         | \$—                      | \$—                       | \$—                |
| Charges taken .....                      | 50                       | 3                         | 53                 |
| Amounts utilized .....                   | —                        | (3)                       | (3)                |
| <b>Balance at December 31, 2000.....</b> | <b><u>\$50</u></b>       | <b><u>\$—</u></b>         | <b><u>\$50</u></b> |

During the second quarter of 2000, Solutia completed plans to integrate Vianova Resins operations with Solutia's resins business and service organizations and recorded a liability of \$11 million to accrue for costs of integration, in accordance with Emerging Issues Task Force Issue 95-3, "Recognition of Liabilities in Connection with a Purchase Business Combination." The integration plans include employment reductions of approximately 130 people, primarily from Vianova Resin's service organizations located in more than 10 countries. In addition, the plans include amounts to shut down certain Vianova Resins sales offices. The integration actions are expected to be carried out by the end of the second quarter of 2001.

The following table summarizes the Vianova Resins integration costs and amounts utilized to carry out those plans:

|                                          | Employment<br>Reductions | Shutdown of<br>Facilities | Total              |
|------------------------------------------|--------------------------|---------------------------|--------------------|
| Balance at January 1, 2000 .....         | \$—                      | \$—                       | \$—                |
| Charges taken .....                      | 10                       | 1                         | 11                 |
| Amounts utilized .....                   | (2)                      | —                         | (2)                |
| <b>Balance at December 31, 2000.....</b> | <b><u>\$ 8</u></b>       | <b><u>\$ 1</u></b>        | <b><u>\$ 9</u></b> |

As part of the integration of Vianova Resins with Solutia's resins businesses, Solutia identified excess production capacity for certain Solutia resins products that will allow for the consolidation of production facilities. As a result, Solutia decided to exit operations at the Port Plastics site in Addyston, Ohio. An \$8 million (\$5 million aftertax) charge to cost of goods sold was recorded in the second quarter of 2000 to carry out the exit plan. The charge included \$2 million to write down plant assets to their fair value of approximately \$1 million, \$2 million of dismantling costs and \$4 million of estimated costs for which Solutia is contractually obligated under an operating agreement. Fair value was determined by discounting future cash flows using an appropriate discount rate. Under the operating agreement, Solutia is required to provide 24 months notice of intent to exit and to pay contractually obligated costs for an additional 18 months thereafter to a third-party operator. The contractually obligated costs represent direct manufacturing, overhead, utilities and severance. The financial impact will not be material to Solutia as production will be shifted to other production facilities.

The following table summarizes the 2000 restructuring charge and amounts utilized to carry out those plans:

|                                        | Shutdown of<br>Facilities | Asset Write-<br>downs | Other<br>Costs     | Total              |
|----------------------------------------|---------------------------|-----------------------|--------------------|--------------------|
| Balance at January 1, 2000 .....       | \$—                       | \$—                   | \$—                | \$—                |
| Charges taken .....                    | 2                         | 2                     | 4                  | 8                  |
| Amounts utilized .....                 | —                         | (2)                   | —                  | (2)                |
| <b>Balance at December 31, 2000...</b> | <b><u>\$ 2</u></b>        | <b><u>\$—</u></b>     | <b><u>\$ 4</u></b> | <b><u>\$ 6</u></b> |

# SOLUTIA INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In February 1999, Integrated Nylon's ammonia unit experienced the failure of certain equipment critical to the production process. Based on an analysis of the economics of purchased ammonia and the cost to repair the equipment, Solutia decided to exit the ammonia business. A \$28 million (\$18 million aftertax) special operations charge to cost of goods sold was recorded in the first quarter of 1999 to implement the exit plan. The charge included \$2 million to write down the assets to their fair value of approximately \$4 million, \$4 million of dismantling costs and \$22 million of costs for which Solutia is contractually obligated under an operating agreement. During the first quarter of 2000, Solutia entered into an agreement for the dismantling of those assets by a third-party and as a result, transferred the liability for dismantling to the third-party. During the third quarter of 2000, Solutia reached an agreement with the plant operator for the final settlement of the contractually obligated costs. As a result, Solutia transferred the liability for the contractually obligated costs to accrued liabilities. Net sales for the ammonia business were \$1 million for the year ended December 31, 1999, and \$20 million in 1998. Operating income for those periods was minimal.

The following table summarizes the 1999 restructuring charge and amounts utilized to carry out those plans:

|                                    | Shutdown of<br>Facilities | Asset Write-<br>downs | Other<br>Costs | Total |
|------------------------------------|---------------------------|-----------------------|----------------|-------|
| Balance at January 1, 1999.....    | \$—                       | \$—                   | \$—            | \$—   |
| Charges taken .....                | 4                         | 2                     | 22             | 28    |
| Amounts utilized .....             | —                         | (2)                   | (6)            | (8)   |
| Balance at December 31, 1999 ..... | \$ 4                      | \$—                   | \$ 16          | \$ 20 |
| Amounts utilized .....             | (4)                       | —                     | (16)           | (20)  |
| Balance at December 31, 2000 ..... | \$—                       | \$—                   | \$—            | \$—   |

In December 1996, Solutia recorded pretax restructuring charges of \$256 million (\$164 million aftertax) to cover costs associated with the closure or sale of certain facilities, asset write-offs and work force reductions of approximately 900 people across all world areas and functions of the company. The workforce reductions were required to reduce staffing for the spinoff and for the implementation of new business systems and methodologies. Approximately two-thirds of the workforce reductions were planned for North American business and manufacturing operations, and approximately one-third were planned for European, Asian and Latin American operations and sales offices. Of the North American reductions, approximately half of the reductions were management and senior management positions.

Activities completed during 1999 included the shutdowns of certain facilities and the final stage of headcount reductions totaling approximately 150 people. The 1999 headcount reductions occurred in Solutia's Asian, European and North American operations. Total headcount reductions under the 1996 restructuring were approximately 900 people. The headcount reductions occurred over a longer period of time than management estimated due to the efforts required to complete the separation from Monsanto and the transition to new business systems and methodologies. In the fourth quarter of 1999, Solutia reversed excess restructuring reserves due to the completion of the actions at a lower cost than contemplated in the 1996 plan. A reversal of \$1 million (\$1 million aftertax) was made to eliminate a reserve for headcount reductions after the final stage of headcount reductions was carried out. A second reversal of \$1 million (\$1 million aftertax) was made to eliminate a reserve recorded to shutdown a non-strategic facility after that shutdown was completed at a lower cost.

During 1998, actions taken under the 1996 restructuring plan included continuing the shutdowns of certain facilities and headcount reductions of approximately 50 people. The 50 people affected were in almost all areas of Solutia, but primarily in Solutia's shared service operations, and left the company by the end of 1998. During December 1998, Solutia also terminated approximately 100 individuals who left on various dates in the first half of 1999. During 1998, evaluations of the costs to complete Solutia's restructuring plans yielded lower cost estimates for certain of the restructuring actions. The second quarter 1998 review yielded lower cost estimates to complete the

# SOLUTIA INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

shutdown of certain facilities and resulted in the reversal of \$3 million (\$2 million aftertax) in that quarter. The third and fourth quarter 1998 reviews yielded downward revisions of the costs to implement the employment reduction plans due to higher than anticipated attrition that reduced employment levels without additional cost to the company. As a result, the company reversed restructuring reserves of \$3 million (\$2 million aftertax) in the third quarter 1998 and \$3 million (\$2 million aftertax) in the fourth quarter.

The following table summarizes the actions of the 1996 plan carried out during 1998 and 1999:

|                                    | Employee<br>Reductions | Shutdown of<br>Facilities | Total |
|------------------------------------|------------------------|---------------------------|-------|
| Balance at January 1, 1998 .....   | \$ 67                  | \$29                      | \$ 96 |
| Amounts utilized .....             | (24)                   | (8)                       | (32)  |
| Adjustments .....                  | (6)                    | (3)                       | (9)   |
| Balance at December 31, 1998 ..... | \$ 37                  | \$18                      | \$ 55 |
| Amounts utilized .....             | (36)                   | (17)                      | (53)  |
| Adjustments .....                  | (1)                    | (1)                       | (2)   |
| Balance at December 31, 1999 ..... | \$ —                   | \$ —                      | \$ —  |

For all of Solutia's restructuring charges, expenses were recorded based on estimates prepared at the time the restructuring actions were approved by the board of directors or management. Adjustments to these estimates, shown in the tables above, were credited to costs of goods sold in the respective year.

### 4. Asset Impairments

During the fourth quarter of 2000, Solutia recorded a \$76 million (\$47 million aftertax) impairment charge to cost of goods sold primarily for the write-off of certain non-performing and non-strategic fiber spinning, drawing and packaging equipment which supports several of Integrated Nylon's product lines. Solutia also recorded an impairment charge to cost of goods sold of \$15 million (\$10 million aftertax) for the write-off of chlorobenzenes' production equipment. The impairments were indicated by current period operating losses and projections of continued losses primarily because of the noncompetitive cost positions these businesses have and the competitive market conditions that they face. The carrying values of the assets were written off as determined by discounting expected future cash flows, using an appropriate discount rate. The assumptions used in the cash flow projections were not materially different from the market conditions experienced in 2000. These conditions are not expected to improve significantly in the foreseeable future. The cash flow assumptions included a declining demand and market share combined with decreased operating margins. Lower operating margins reflect the non-competitive cost position of these businesses and the impact of lower selling prices associated with an extremely competitive operating environment.

During the second quarter of 2000, Solutia recorded a \$6 million (\$4 million aftertax) impairment charge to administrative expenses for the write-down of capitalized software costs related to the formation of the Astaris joint venture. The software had previously been fully dedicated to Solutia's Phosphorus Derivatives business. Impairment was indicated by a significant change in the extent and manner in which Astaris was expected to utilize the asset under a transition services agreement. The carrying value of the asset was written down to its estimated fair value, as determined by discounting expected future cash flows, using an appropriate discount rate.

An impairment charge of \$6 million (\$4 million aftertax) was recorded in the first quarter of 1999 to cost of goods sold primarily to write down a bulk continuous filament spinning machine as a result of management's decision to shut down the equipment due to a noncompetitive cost position. The adjusted carrying value of the machine is \$0.5 million. The charge is due to a review under SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and Assets to Be Disposed Of," which indicated that the carrying amount of the assets exceeded the identifiable, undiscounted cash flows related to the assets. Fair value of the assets was determined based on estimates

# SOLUTIA INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

of market prices for the machinery. Operating income derived from the machinery was minimal in the years ended December 31, 1999 and 1998.

### 5. Investments in Affiliates

In April 2000, Astaris L.L.C., a joint venture between Solutia and FMC Corporation, started operations to manufacture and market phosphorus chemicals. Solutia contributed its Phosphorus Derivatives business to the joint venture in exchange for a 50 percent ownership share. Net assets contributed to the venture totaled approximately \$87 million. Solutia accounts for the joint venture using the equity method of accounting. During the third quarter of 2000, Solutia received \$85 million from Astaris representing a cash distribution and repayment of working capital loans.

At December 31, 2000, Solutia's investments in affiliates consisted principally of its 50 percent interests in the Flexsys, Advanced Elastomers Systems and Astaris joint ventures for which Solutia uses the equity method of accounting. Summarized combined financial information for 100 percent of the Flexsys, AES and Astaris joint ventures is as follows:

|                              | <u>2000</u> | <u>1999</u> | <u>1998</u> |
|------------------------------|-------------|-------------|-------------|
| Results of operations:       |             |             |             |
| Net sales .....              | \$1,247     | \$869       | \$838       |
| Gross profit .....           | 327         | 267         | 256         |
| Operating income .....       | 138         | 108         | 116         |
| Net income .....             | 95          | 85          | 94          |
| Financial position:          |             |             |             |
| Current assets .....         | \$ 552      | \$398       |             |
| Noncurrent assets .....      | 744         | 518         |             |
| Current liabilities .....    | 347         | 275         |             |
| Noncurrent liabilities ..... | 334         | 48          |             |

### 6. Inventory Valuation

The components of inventories were:

|                                     | <u>2000</u>   | <u>1999</u>   |
|-------------------------------------|---------------|---------------|
| Finished goods .....                | \$ 305        | \$ 260        |
| Goods in process .....              | 105           | 121           |
| Raw materials and supplies .....    | 108           | 109           |
| Inventories, at FIFO cost .....     | 518           | 490           |
| Excess of FIFO over LIFO cost ..... | (161)         | (119)         |
| Total .....                         | <u>\$ 357</u> | <u>\$ 371</u> |

Inventories at FIFO approximate current cost. The effects of LIFO inventory liquidations were not significant.

# SOLUTIA INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### 7. Income Taxes

The components of income before income taxes were:

|                             | <u>2000</u>         | <u>1999</u>         | <u>1998</u>         |
|-----------------------------|---------------------|---------------------|---------------------|
| United States .....         | <u>\$(23)</u>       | <u>\$224</u>        | <u>\$285</u>        |
| Outside United States ..... | <u>64</u>           | <u>79</u>           | <u>90</u>           |
| <b>Total .....</b>          | <b><u>\$ 41</u></b> | <b><u>\$303</u></b> | <b><u>\$375</u></b> |

The components of income tax expense (benefit) charged to operations were:

|                             | <u>2000</u>          | <u>1999</u>         | <u>1998</u>         |
|-----------------------------|----------------------|---------------------|---------------------|
| Current:                    |                      |                     |                     |
| U.S. federal .....          | <u>\$(63)</u>        | <u>\$ 48</u>        | <u>\$ 66</u>        |
| U.S. state .....            | <u>(2)</u>           | <u>6</u>            | <u>3</u>            |
| Outside United States ..... | <u>34</u>            | <u>20</u>           | <u>25</u>           |
|                             | <u>(31)</u>          | <u>74</u>           | <u>94</u>           |
| Deferred:                   |                      |                     |                     |
| U.S. federal .....          | <u>46</u>            | <u>18</u>           | <u>21</u>           |
| U.S. state .....            | <u>(7)</u>           | <u>—</u>            | <u>6</u>            |
| Outside United States ..... | <u>(16)</u>          | <u>5</u>            | <u>5</u>            |
|                             | <u>23</u>            | <u>23</u>           | <u>32</u>           |
| <b>Total .....</b>          | <b><u>\$ (8)</u></b> | <b><u>\$ 97</u></b> | <b><u>\$126</u></b> |

During 2000, Germany reduced its corporate tax rate effective January 1, 2001. In accordance with SFAS No. 109, "Accounting for Income Taxes," Solutia recognized \$7 million of income to record the net effect of the change on deferred income tax assets and liabilities. This adjustment is included as part of the deferred tax provision above.

Factors causing Solutia's effective tax rate to differ from the U.S. federal statutory rate were:

|                                                         | <u>2000</u>         | <u>1999</u>       | <u>1998</u>       |
|---------------------------------------------------------|---------------------|-------------------|-------------------|
| U.S. federal statutory rate .....                       | <u>35%</u>          | <u>35%</u>        | <u>35%</u>        |
| U.S. state income taxes .....                           | <u>(15)</u>         | <u>2</u>          | <u>2</u>          |
| Tax benefit of foreign sales corporation .....          | <u>(13)</u>         | <u>(2)</u>        | <u>(2)</u>        |
| Taxes related to foreign income, net of credits .....   | <u>(17)</u>         | <u>(1)</u>        | <u>—</u>          |
| Valuation allowances .....                              | <u>32</u>           | <u>—</u>          | <u>—</u>          |
| Income from equity affiliates recorded net of tax ..... | <u>(37)</u>         | <u>(4)</u>        | <u>(2)</u>        |
| Other .....                                             | <u>(6)</u>          | <u>2</u>          | <u>1</u>          |
| <b>Effective income tax rate .....</b>                  | <b><u>(21)%</u></b> | <b><u>32%</u></b> | <b><u>34%</u></b> |

# SOLUTIA INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Deferred income tax balances were related to:

|                                | <u>2000</u>    | <u>1999</u>    |
|--------------------------------|----------------|----------------|
| Property.....                  | <u>\$(173)</u> | <u>\$(197)</u> |
| Postretirement benefits.....   | <u>377</u>     | <u>399</u>     |
| Restructuring reserves.....    | <u>29</u>      | <u>7</u>       |
| Environmental liabilities..... | <u>64</u>      | <u>76</u>      |
| Intangible assets.....         | <u>(66)</u>    | <u>—</u>       |
| Inventory.....                 | <u>—</u>       | <u>(3)</u>     |
| Valuation allowances.....      | <u>(13)</u>    | <u>—</u>       |
| Other.....                     | <u>(21)</u>    | <u>17</u>      |
| Net deferred tax assets.....   | <u>\$ 197</u>  | <u>\$ 299</u>  |

At December 31, 2000, foreign tax credit carryforwards available to reduce possible future U.S. income taxes amounted to approximately \$13 million, all of which expire in 2005. Valuation allowances have been provided for the foreign tax credit carryforwards that are not likely to be utilized. Income taxes and remittance taxes have not been recorded on \$77 million in undistributed earnings of subsidiaries, either because any taxes on dividends would be offset substantially by foreign tax credits or because Solutia intends to reinvest those earnings indefinitely. It is not practicable to estimate the tax effect of remitting these earnings to the United States.

### 8. Debt Obligations

Solutia's debt obligations include commercial paper, notes and debentures. The weighted average interest rate on total debt outstanding at December 31, 2000, was 6.7 percent and was 6.8 percent at December 31, 1999.

#### *Debt Maturing in One Year*

Debt maturing in one year consisted of commercial paper balances of \$485 million at December 31, 2000, and \$511 million at December 31, 1999. Weighted average interest rates on commercial paper balances were 6.6 percent during 2000, 5.5 percent in 1999 and 5.7 percent during 1998.

At December 31, 1999, \$201 million of outstanding commercial paper was reclassified from short-term debt to long-term debt based on Solutia's intention to refinance that amount through the issuance of €200 million of notes, due February 2005.

Solutia's commercial paper program is principally supported by an \$800 million, five-year revolving credit facility (\$800 million facility) with a syndicate of commercial banks. The \$800 million facility is also available for working capital and other general corporate purposes. This agreement was amended during November 1999, principally to allow the issuance of commercial paper in euros, as well as U.S. dollars.

During November 2000, Solutia put in place a \$250 million, 364-day multi-currency revolving credit agreement (\$250 million facility) with a syndicate of commercial banks. The \$250 million facility has terms that are generally consistent with the terms of the \$800 million facility. The \$250 million facility supports Solutia's commercial paper program and is available for working capital and other general corporate purposes.

Both the \$800 million facility and the \$250 million facility contain various covenants that, among other things, restrict Solutia's ability to merge with another entity and require Solutia to meet certain leverage and interest coverage ratios. Solutia does not anticipate that future borrowings will be limited by the terms of these agreements. Interest on amounts borrowed under these credit facilities is expected to approximate money market rates.

# SOLUTIA INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

### Long-Term Debt

Long-term debt consisted of the following:

|                                 | <u>2000</u>         | <u>1999</u>         |
|---------------------------------|---------------------|---------------------|
| Commercial paper.....           | \$ —                | \$201               |
| 6.5% notes due 2002.....        | 150                 | 150                 |
| 7.375% debentures due 2027..... | 300                 | 300                 |
| 6.72% debentures due 2037.....  | 150                 | 150                 |
| 6.25% euro notes due 2005.....  | 186                 | —                   |
| Other.....                      | 1                   | 4                   |
| Unamortized debt discount.....  | (3)                 | (3)                 |
| <b>Total</b> .....              | <u><b>\$784</b></u> | <u><b>\$802</b></u> |

Other notes of \$1 million at December 31, 2000, and \$4 million at December 31, 1999, were assumed in the acquisition of Vianova Resins.

The notes and debentures are unsecured obligations. Interest is payable semiannually, on April 15 and October 15 of each year. The holders of the 2037 debentures have the right to require repayment on October 15, 2004. The notes and debentures contain provisions that, among other things, restrict Solutia's ability to create liens against assets and its ability to enter into sale and leaseback transactions.

### 9. Fair Values of Financial Instruments

The estimated fair value of Solutia's long-term debt was \$685 million as of December 31, 2000, and \$761 million as of December 31, 1999. These estimates compare with the recorded amount of \$784 million in 2000 and \$802 million in 1999.

The recorded amounts of cash, trade receivables, third-party guarantees, accounts payable and short-term debt approximate their fair values at both December 31, 2000, and December 31, 1999. The estimated fair value of the company's foreign currency forward contracts and natural gas contracts was not material. Notional amounts for purchase contracts were \$286 million at December 31, 2000, and \$44 million at December 31, 1999, and for sell contracts the notional amounts were \$265 million at December 31, 2000, and \$44 million at December 31, 1999.

Fair values are estimated by the use of quoted market prices, estimates obtained from brokers and other appropriate valuation techniques and are based upon information available as of December 31, 2000, and December 31, 1999. The fair-value estimates do not necessarily reflect the values Solutia could realize in the current market.

### 10. Postretirement Benefits

Pension benefits are based on the employee's age, years of service and/or compensation level. The qualified pension plan is funded in accordance with Solutia's long-range projections of the plan's financial conditions. These projections take into account benefits earned and expected to be earned, anticipated returns on pension plan assets and income tax and other regulations. Prior to the spinoff, the majority of Solutia's employees participated in Monsanto's noncontributory pension plans. In conjunction with the spinoff, Monsanto assumed pension liabilities and received related assets from those plans for its applicable active employees and for certain former employees who left Monsanto in earlier years.

The majority of Solutia's employees also participate in benefit programs that provide certain health care and life insurance benefits for retired employees. Substantially all regular, full-time U.S. employees and certain employees in other countries may become eligible for these benefits if they reach retirement age while employed by Solutia and have the required years of service. These postretirement benefits are unfunded and are generally based on the

# SOLUTIA INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

employee's age, years of service and/or compensation level. The costs of postretirement benefits are accrued by the date the employees become eligible for the benefits. In connection with the spinoff, Solutia assumed retiree medical liabilities for its applicable active employees and for approximately two-thirds of the retired U.S. employees of Monsanto.

During the second quarter of 1998, Solutia amended certain of its postretirement health care plans, primarily to adjust cost-sharing provisions. The amendment resulted in a \$161 million reduction in the company's accumulated postretirement benefit obligation, which is being amortized over the average remaining service life of plan participants of approximately 12 years.

For 2000, 1999 and 1998, Solutia's pension and healthcare and other benefit costs were as follows:

|                                          | Pension Benefits |              |              | Healthcare and Other Benefits |             |             |
|------------------------------------------|------------------|--------------|--------------|-------------------------------|-------------|-------------|
|                                          | 2000             | 1999         | 1998         | 2000                          | 1999        | 1998        |
| Service costs for benefits earned.....   | \$ 32            | \$ 38        | \$ 33        | \$10                          | \$11        | \$11        |
| Interest cost on benefit obligation..... | 131              | 132          | 130          | 53                            | 49          | 54          |
| Assumed return on plan assets.....       | (144)            | (153)        | (147)        | —                             | —           | —           |
| Prior service costs.....                 | 21               | 21           | 19           | (18)                          | (18)        | (12)        |
| Transition asset.....                    | (10)             | (10)         | (10)         | —                             | —           | —           |
| Unrecognized net (gain)/loss.....        | 4                | (3)          | (3)          | 7                             | 6           | 1           |
| Settlement.....                          | (23)             | —            | —            | —                             | —           | —           |
| <b>Total .....</b>                       | <b>\$ 11</b>     | <b>\$ 25</b> | <b>\$ 22</b> | <b>\$52</b>                   | <b>\$48</b> | <b>\$54</b> |

Components of the changes in fair value of plan assets, changes in the benefit obligation and the funding status of Solutia's postretirement plans are as follows:

|                                                      | Pension Benefits |                | Healthcare and Other Benefits |              |
|------------------------------------------------------|------------------|----------------|-------------------------------|--------------|
|                                                      | 2000             | 1999           | 2000                          | 1999         |
| <b>Changes in Fair Value of Plan Assets</b>          |                  |                |                               |              |
| Fair value of plan assets at January 1.....          | \$1,973          | \$1,910        | \$ —                          | \$ —         |
| Actual return on plan assets.....                    | 92               | 349            | —                             | —            |
| Acquisitions.....                                    | —                | 2              | —                             | —            |
| Settlements.....                                     | (37)             | —              | —                             | —            |
| Benefits paid.....                                   | (304)            | (288)          | —                             | —            |
| <b>Fair value of plan assets at December 31.....</b> | <b>\$1,724</b>   | <b>\$1,973</b> | <b>\$ —</b>                   | <b>\$ —</b>  |
| <b>Changes in Benefit Obligation</b>                 |                  |                |                               |              |
| Benefit obligation at January 1.....                 | \$1,833          | \$1,983        | \$720                         | \$726        |
| Service costs.....                                   | 32               | 38             | 10                            | 11           |
| Interest cost.....                                   | 131              | 132            | 53                            | 49           |
| Participant contributions.....                       | —                | —              | 7                             | 2            |
| Actuarial gains and losses.....                      | 111              | (54)           | 51                            | 12           |
| Acquisitions.....                                    | —                | 21             | —                             | —            |
| Settlements.....                                     | (37)             | —              | (17)                          | —            |
| Benefits paid.....                                   | (326)            | (300)          | (92)                          | (80)         |
| Plan amendments.....                                 | 2                | 13             | —                             | —            |
| <b>Benefit obligation at December 31.....</b>        | <b>\$1,746</b>   | <b>\$1,833</b> | <b>\$732</b>                  | <b>\$720</b> |

# SOLUTIA INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Plan assets consist principally of common stocks and U.S. government and corporate obligations. Contributions to the pension benefit plans were neither required nor made in 2000 and 1999 because Solutia's principal pension plan is adequately funded, using assumed returns.

The funded status of Solutia's postretirement benefit plans at December 31, 2000, and 1999 was as follows:

|                                                   | Pension Benefits      |                       | Healthcare and Other Benefits |                       |
|---------------------------------------------------|-----------------------|-----------------------|-------------------------------|-----------------------|
|                                                   | 2000                  | 1999                  | 2000                          | 1999                  |
| <b>Funded Status</b> .....                        | <b>\$ (22)</b>        | <b>\$ 140</b>         | <b>\$(732)</b>                | <b>\$(720)</b>        |
| Unrecognized actuarial (gain)/loss .....          | (294)                 | (464)                 | 65                            | 18                    |
| Unrecognized prior service costs .....            | 135                   | 149                   | (141)                         | (159)                 |
| Additional liability .....                        | (13)                  | (25)                  | —                             | —                     |
| Unrecognized transition (gain)/loss .....         | (5)                   | (13)                  | —                             | —                     |
| <b>Accrued net liability at December 31</b> ..... | <b><u>\$(199)</u></b> | <b><u>\$(213)</u></b> | <b><u>\$(808)</u></b>         | <b><u>\$(861)</u></b> |

The accrued net liability was included in:

|                                            | Pension Benefits      |                       | Healthcare and Other Benefits |                       |
|--------------------------------------------|-----------------------|-----------------------|-------------------------------|-----------------------|
|                                            | 2000                  | 1999                  | 2000                          | 1999                  |
| Current postretirement liabilities .....   | \$ —                  | \$ —                  | \$ ( 78)                      | \$ ( 86)              |
| Long-term postretirement liabilities ..... | (211)                 | (223)                 | (730)                         | (775)                 |
| Less: Other assets .....                   | 12                    | 10                    | —                             | —                     |
| <b>Accrued net liability</b> .....         | <b><u>\$(199)</u></b> | <b><u>\$(213)</u></b> | <b><u>\$(808)</u></b>         | <b><u>\$(861)</u></b> |

Certain of Solutia's pension benefit plans are unfunded and therefore have accumulated benefit obligations in excess of plan assets. Information regarding these unfunded plans is as follows:

|                                      | 2000 | 1999 |
|--------------------------------------|------|------|
| Projected benefit obligation .....   | \$25 | \$30 |
| Accumulated benefit obligation ..... | 23   | 24   |
| Fair value of plan assets .....      | —    | —    |

The significant actuarial assumptions used to estimate the projected benefit obligation for the company's principal pension, healthcare and other benefit plans were as follows:

|                                                                                                  | Pension Benefits |       | Healthcare and Other Benefits |       |
|--------------------------------------------------------------------------------------------------|------------------|-------|-------------------------------|-------|
|                                                                                                  | 2000             | 1999  | 2000                          | 1999  |
| Discount rate .....                                                                              | 7.25%            | 7.50% | 7.25%                         | 7.50% |
| Assumed long-term rate of return on plan assets .....                                            | 9.50%            | 9.50% | —                             | —     |
| Annual rates of salary increase (for plans that base benefits on final compensation level) ..... | 4.25%            | 4.50% | —                             | —     |
| Assumed trend rate for healthcare costs .....                                                    | —                | —     | 5.00%                         | 5.25% |
| Ultimate trend rate for healthcare costs .....                                                   | —                | —     | 5.00%                         | 5.25% |

# SOLUTIA INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

A 1 percent change in the assumed health care cost trend rates would have the following effect as of December 31, 2000:

|                                                            | 1-Percentage-<br>Point Increase | 1-Percentage-<br>Point Decrease |
|------------------------------------------------------------|---------------------------------|---------------------------------|
| Effect on total service and interest cost components ..... | \$ 1                            | \$ (1)                          |
| Effect on postretirement benefit obligation....            | 12                              | (13)                            |

### 11. Employee Savings Plans

In connection with the spinoff, Monsanto common stock held by the Monsanto Employee Stock Ownership Plan (ESOP) and related Monsanto ESOP borrowings were allocated between Solutia and Monsanto. As a result of this allocation, Solutia received 2.4 million shares of Monsanto common stock and assumed \$29 million of ESOP debt to third parties. Simultaneously, Solutia created its own ESOP, established a trust to hold the Monsanto shares, and issued a \$29 million loan to the trust. The trust used the proceeds of the loan to repay the assumed third-party debt. Subsequent to the spinoff, the ESOP trust was required by government regulations to divest its holdings of Monsanto common stock and to use the proceeds to acquire Solutia common stock. The divestiture of Monsanto common stock and the purchase of Solutia common stock were completed in early 1998. At inception, the trust held 10,737,097 shares of Solutia common stock. As of December 31, 2000, there have been 9,143,358 shares allocated to participants.

Substantially all U.S. employees of Solutia are eligible to participate in the Solutia Inc. Savings and Investment Plan, a 401(k) plan. Shares held in the ESOP are used to make Solutia's matching contribution to eligible participants' accounts under this plan. The number of shares released is computed on each pay date based on a formula that considers the participant contribution, the Solutia matching rate and Solutia's closing stock price. Shares allocated to participant accounts totaled 1,314,341 shares in 2000, 979,439 shares in 1999 and 622,598 shares in 1998, leaving 1,593,739 unallocated shares as of December 31, 2000. The value of these contributions was \$17 million in 2000, \$18 million in 1999, and \$16 million in 1998. Compensation expense is equal to the cost of the shares allocated to participants, less dividends paid on the shares held by the ESOP. Information regarding the ESOP follows:

|                                              | 2000 | 1999 | 1998 |
|----------------------------------------------|------|------|------|
| Total ESOP expense .....                     | \$10 | \$ 8 | \$6  |
| Interest portion of total ESOP expense ..... | 1    | 2    | 2    |
| Cash contributions .....                     | 10   | 10   | 7    |

### 12. Stock Option Plans

Solutia has two stock-based incentive plans under which awards are being granted to officers and employees, the Solutia Inc. 2000 Stock-Based Incentive Plan and the Solutia Inc. 1997 Stock-Based Incentive Plan. The 2000 plan authorizes up to 5,400,000, and the 1997 plan up to 7,800,000, shares of Solutia common stock for grants of non-qualified and incentive stock options, stock appreciation rights, restricted stock awards and bonus stock awards. The shares used may be newly issued shares, treasury shares or a combination. Under both plans, the exercise price of a stock option must be no less than the fair market value of Solutia's common stock on the option grant date. Additionally, the plans provide that the term of any stock option granted may not exceed 10 years. At December 31, 2000, approximately 4,191,380 shares from the 2000 plan and 356,374 shares from the 1997 plan remained available for grants.

During 2000, non-qualified options to purchase 456,000 shares of Solutia common stock were granted under the plans to current executive officers and other senior executives as a group, and non-qualified stock options to purchase 1,430,876 shares were granted to other employees at an average exercise price of \$13.98 per share. Total shares covered by options granted under the plans to current executive officers and other senior executives as a group totaled 2,099,000 and other employees totaled 6,631,268, through December 31, 2000. The options granted to Solutia's

# SOLUTIA INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

executive officers and other senior executives are performance options that become exercisable upon the earlier of achievement of specified share price targets or the ninth anniversary of the option grant. The options granted to the other management employees are time-based. They generally become exercisable in thirds, one-third on each of the first three anniversaries of the option grant date.

The Solutia Inc. Non-Employee Director Compensation Plan provides incentives to non-employee members of Solutia's board of directors. This plan authorizes up to 400,000 shares for grants of non-qualified stock options and for grants of deferred shares in payment of all or a portion of the annual retainer for the non-employee directors. Only treasury shares may be used. Under this plan, the exercise price of a stock option must be no less than the fair market value of Solutia's common stock on the grant date and the term of any stock option granted under the plan may not exceed 10 years. At December 31, 2000, 257,717 shares of Solutia's common stock remained available for grants under the plan. Shares covered by options granted, and deferred shares credited to non-employee directors' accounts totaled 25,167 in 2000, 34,333 in 1999 and 16,000 in 1998.

As permitted by SFAS No. 123, "Accounting for Stock-Based Compensation," Solutia has elected to continue following the guidance of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," for measurement and recognition of stock-based transactions with employees. Accordingly, no compensation cost has been recognized for Solutia's option plans. Had the determination of compensation cost for these plans been based on the fair value at the grant dates for awards under these plans, consistent with the method of SFAS No. 123, Solutia's net income would have been reduced to the pro forma amounts indicated below:

|                                    | <u>2000</u> | <u>1999</u> | <u>1998</u> |
|------------------------------------|-------------|-------------|-------------|
| <b>Net income:</b>                 |             |             |             |
| As reported.....                   | \$ 49       | \$ 206      | \$ 249      |
| Pro forma .....                    | 42          | 187         | 224         |
| <b>Diluted earnings per share:</b> |             |             |             |
| As reported.....                   | \$0.46      | \$1.80      | \$2.03      |
| Pro forma .....                    | 0.39        | 1.63        | 1.82        |

Compensation expense resulting from the fair value method of SFAS No. 123 may not be representative of compensation expense to be incurred on a pro forma basis in future years. The fair value of each option grant is estimated on the date of grant by use of the Black-Scholes option-pricing model.

The following weighted-average assumptions were used for grants of Solutia options in 2000, 1999 and 1998:

|                                    | <u>2000</u> | <u>1999</u> | <u>1998</u> |
|------------------------------------|-------------|-------------|-------------|
| Expected dividend yield.....       | 0.2%        | 0.2%        | 0.2%        |
| Expected volatility.....           | 34.0%       | 34.0%       | 28.0%       |
| Risk-free interest rates.....      | 5.8%        | 6.0%        | 5.1%        |
| Expected option lives (years)..... | 5.0         | 5.0         | 5.0         |

The weighted-average fair values of options granted were \$5.30 in 2000, \$8.05 in 1999 and \$9.33 in 1998.

# SOLUTIA INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

A summary of the status of Solutia's stock option plans for years ended December 31, 2000, 1999 and 1998 follows:

|                         | Exercisable<br>Shares | Outstanding       |                                    |
|-------------------------|-----------------------|-------------------|------------------------------------|
|                         |                       | Shares            | Weighted-Average<br>Exercise Price |
| December 31, 1997       | <u>9,517,858</u>      | <u>27,892,400</u> | <u>\$14.53</u>                     |
| Granted.....            |                       | 273,567           | \$27.12                            |
| Exercised .....         |                       | (1,833,225)       | 12.19                              |
| Expired .....           |                       | (475,637)         | 16.22                              |
| December 31, 1998 ..... | <u>17,116,842</u>     | <u>25,857,105</u> | <u>\$14.79</u>                     |
| Granted.....            |                       | 2,054,658         | \$20.61                            |
| Exercised .....         |                       | (678,710)         | 10.93                              |
| Expired .....           |                       | (495,232)         | 18.43                              |
| December 31, 1999 ..... | <u>18,852,246</u>     | <u>26,737,821</u> | <u>\$15.27</u>                     |
| Granted.....            |                       | 1,912,043         | \$13.98                            |
| Exercised .....         |                       | (379,687)         | 6.74                               |
| Expired .....           |                       | (1,279,514)       | 17.21                              |
| December 31, 2000 ..... | <u>23,590,921</u>     | <u>26,990,663</u> | <u>\$15.21</u>                     |

The following table summarizes information about stock options outstanding at December 31, 2000:

### Options Outstanding:

| Range of<br>Exercise<br>Prices | Shares            | Weighted-Average<br>Remaining<br>Contractual Life | Weighted-Average<br>Exercise Price |
|--------------------------------|-------------------|---------------------------------------------------|------------------------------------|
| \$ 3 to 7 .....                | 4,353,760         | 2.4                                               | \$ 5.90                            |
| 8 to 11 .....                  | 50,029            | 7.0                                               | 10.58                              |
| 12 to 15 .....                 | 3,081,363         | 7.8                                               | 13.42                              |
| 16 to 18 .....                 | 13,206,730        | 6.0                                               | 16.44                              |
| 19 to 22 .....                 | 6,061,700         | 7.3                                               | 19.69                              |
| 23 to 29 .....                 | 237,081           | 7.4                                               | 27.65                              |
| \$ 3 to 29 .....               | <u>26,990,663</u> | <u>5.9</u>                                        | <u>\$15.21</u>                     |

### Options Exercisable:

| Range of<br>Exercise Prices | Shares            | Weighted-Average<br>Exercise Price |
|-----------------------------|-------------------|------------------------------------|
| \$ 3 to 7 .....             | 4,353,760         | \$ 5.90                            |
| 8 to 11 .....               | 28,862            | 9.74                               |
| 12 to 15 .....              | 1,261,713         | 12.56                              |
| 16 to 18 .....              | 13,206,730        | 16.44                              |
| 19 to 22 .....              | 4,619,940         | 19.43                              |
| 23 to 29 .....              | 119,916           | 27.49                              |
| \$ 3 to 29 .....            | <u>23,590,921</u> | <u>\$14.92</u>                     |

## SOLUTIA INC.

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

#### 13. Capital Stock

Solutia's board of directors declared a dividend of one preferred stock purchase right for each share of Solutia's common stock issued in the distribution of shares by Monsanto to its shareholders on the effective date of the spinoff and authorized the issuance of one right for each share of common stock issued after the effective date of the spinoff until the earlier of the date the rights become exercisable and the termination date of the rights plan. If a person or group acquires beneficial ownership of 20 percent or more, or announces a tender offer that would result in beneficial ownership of 20 percent or more, of Solutia's outstanding common stock, the rights become exercisable. Then, for every right held, the owner will be entitled to purchase one one-hundredth of a share of a series of preferred stock for \$125. If Solutia is acquired in a business combination transaction while the rights are outstanding, for every right held, the holder will be entitled to purchase, for \$125, common shares of the acquiring company having a market value of \$250. In addition, if a person or group acquires beneficial ownership of 20 percent or more of Solutia's outstanding common stock, for every right held, the holder (other than such person or members of such group) will be entitled to purchase, for \$125, a number of shares of Solutia's common stock having a market value of \$250. Furthermore, at any time after a person or group acquires beneficial ownership of 20 percent or more (but less than 50 percent) of Solutia's outstanding common stock, Solutia's board of directors may, at its option, exchange part or all of the rights (other than rights held by the acquiring person or group) for shares of Solutia's common stock on a one-share-for-every-one-right basis. At any time prior to the acquisition of such a 20 percent position, Solutia can redeem each right for \$0.01. The board of directors is also authorized to reduce the aforementioned 20 percent thresholds to not less than 10 percent. The rights expire in the year 2007.

The company has 10 million shares of preferred stock, par value \$0.01 per share, authorized. As of December 31, 2000, there were no preferred shares issued or outstanding.

#### 14. Commitments and Contingencies

Commitments, principally in connection with uncompleted additions to property, were approximately \$7 million at December 31, 2000. Solutia was contingently liable as a guarantor principally in connection with bank loans totaling approximately \$16 million at December 31, 2000. In addition, as of December 31, 2000, the company was contingently liable under letters of credit, primarily related to environmental remediation, totaling \$37 million. Solutia's future minimum payments under noncancelable operating leases and unconditional purchase obligations are \$30 million for 2001, \$25 million for 2002, \$58 million for 2003, \$18 million for 2004, \$17 million for 2005 and \$87 million thereafter.

Solutia has entered into agreements with customers to supply a guaranteed quantity of certain products annually at prices specified in the agreements. In return, the customers have advanced funds to Solutia to cover the costs of expanding capacity to provide the guaranteed supply. Solutia has recorded the advances as deferred credits and amortizes the amounts to income as the customers purchase the products. The unamortized deferred credits were approximately \$171 million at December 31, 2000, and approximately \$183 million at December 31, 1999.

In connection with the finalization of the external financing agreement for Astaris during the third quarter of 2000, Solutia and FMC Corporation have independently contractually agreed to provide Astaris with funding in the event the joint venture fails to meet certain financial benchmarks. Subsequent to December 31, 2000, Solutia received notification that such a contribution will be required in 2001. Solutia believes that this obligation is not likely to have a significant impact on its consolidated financial position, liquidity or profitability.

## SOLUTIA INC.

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The more significant concentrations in Solutia's trade receivables at year-end were:

|                                 | <u>2000</u> | <u>1999</u> |
|---------------------------------|-------------|-------------|
| U.S. chemical industry.....     | \$ 51       | \$ 51       |
| U.S. carpet industry.....       | 42          | 41          |
| European glass industry.....    | 38          | 50          |
| European chemical industry..... | 101         | 28          |

Management does not anticipate losses on its trade receivables in excess of established allowances.

Solutia's Statement of Consolidated Financial Position included accrued liabilities of \$181 million at December 31, 2000, and \$201 million at December 31, 1999, for the remediation of identified waste disposal sites. Expenditures related to remediation activities were \$29 million in 2000, \$22 million in 1999 and \$22 million in 1998.

Uncertainties related to all of Solutia's environmental liabilities include evolving government policy and regulations, the method and extent of remediation and future changes in technology. Because of these uncertainties, Solutia estimates that potential future expenses associated with these liabilities could be an additional \$20 million to \$30 million. Although the ultimate costs and results of remediation of contaminated sites cannot be predicted with certainty, they are not expected to have a material adverse effect on Solutia's consolidated financial position, liquidity or profitability in any one year.

On October 12, 2000, the printing ink resins unit and a small phenolics production unit at Wiesbaden, Germany were severely damaged by an explosion and fire. No fatalities, serious injuries or environmental damage resulted from the incident. Solutia has determined that all probable losses will be recovered from insurance proceeds and has not recorded a loss from the incident. Solutia anticipates that the insurance recoveries will exceed the net book value of the plant assets and associated losses resulting in a gain. The results of operations from these production units were not material to Solutia's consolidated results of operations.

During the first quarter of 1999, Solutia recorded a \$29 million (\$18 million aftertax) charge to cost of goods sold to increase reserves related to the anticipated settlement of two lawsuits brought against Monsanto, for which Solutia assumed responsibility in the 1997 spinoff from Monsanto, relating to the alleged discharge of polychlorinated biphenyls ("PCBs") from the Anniston, Alabama plant site, and to environmental remediation of the allegedly affected areas. During the third quarter of 2000, Solutia paid approximately \$23 million for the settlement of these actions. The remainder of the reserve will cover costs associated with environmental remediation of the allegedly affected areas.

Because of the size and nature of its business, Solutia is a party to numerous legal proceedings. Most of these proceedings have arisen in the ordinary course of business and involve claims for money damages. In addition, at the time of the spinoff, Solutia assumed from Monsanto, under the Distribution Agreement, liabilities related to specified legal proceedings. As a result, although Monsanto remains the named defendant, Solutia is required to manage the litigation and indemnify Monsanto for costs, expenses and judgments arising from the litigation. Such matters arise out of the normal course of business and relate to product liability; government regulation, including environmental issues; employee relations and other issues. Certain of the lawsuits and claims seek damages in very large amounts. Although the results of litigation cannot be predicted with certainty, management's belief is that the final outcome of such litigation, except as noted below, will not have a material adverse effect on Solutia's consolidated financial position, liquidity or profitability in any one year.

Monsanto manufactured PCBs at the Anniston, Alabama plant from 1935 to 1971. Solutia is defending a number of actions in state and federal court in Alabama relating to the alleged emission of PCBs and other allegedly hazardous materials from that plant. Plaintiffs claim to suffer from various personal injuries and are allegedly fearful of future illness. Some claim property damage. These cases are being vigorously defended. Management does not believe that the ultimate resolution of these cases will have a material adverse impact on its consolidated financial

# SOLUTIA INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

position or liquidity. However, it is possible that a resolution of these cases may have a material adverse impact on Solutia's net income in a given year, although it is impossible at this time to estimate the range or amount of any such liability.

### 15. Supplemental Data

Supplemental income statement data were:

|                                                     | 2000    | 1999  | 1998  |
|-----------------------------------------------------|---------|-------|-------|
| Raw material and energy costs .....                 | \$1,300 | \$984 | \$994 |
| Employee compensation and benefits.....             | 824     | 728   | 757   |
| Current income and other taxes .....                | 82      | 166   | 176   |
| Rent expense.....                                   | 38      | 26    | 26    |
| Technological expenses:                             |         |       |       |
| Research and development.....                       | 67      | 58    | 60    |
| Engineering, commercial development and patent..... | 24      | 22    | 23    |
| Total technological expenses .....                  | 91      | 80    | 83    |
| Interest expense:                                   |         |       |       |
| Total interest cost .....                           | 101     | 53    | 49    |
| Less capitalized interest .....                     | 18      | 13    | 6     |
| Net interest expense .....                          | 83      | 40    | 43    |

### 16. Segment and Geographic Data

Solutia's management is organized around four strategic business platforms: Performance Films, Resins and Additives, Specialties and Integrated Nylon. Resins and Additives and Specialties have been aggregated into the Specialty Products reportable segment because of their similar economic characteristics, as well as their similar products and services, production processes, types of customers and methods of distribution. Solutia's reportable segments and their major products are as follows:

| Performance Films                                                                                                                | Specialty Products                                                                                                         | Integrated Nylon                                                                            |
|----------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------|
| SAFLEX® plastic interlayer                                                                                                       | Resins and additives, including                                                                                            | Intermediate "building block" chemicals                                                     |
| KEEPSAFE®, SAFLEX INSIDE® (in Europe only) and KEEPSAFE MAXIMUM® glass for residential security and hurricane protection windows | ALFTALAT® polyester resins, RESIMENE® and MAPRENAL® crosslinkers and SYNTHACRYL® acrylic resins                            |                                                                                             |
| LLUMAR®, VISTA® and GILA® professional and after-market window films                                                             | THERMINOL® heat transfer fluids                                                                                            | Merchant polymer and nylon extrusion polymers, including VYDYNE® and ASCEND™                |
| Conductive and anti-reflective coated films and deep-dyed films                                                                  | DEQUEST® water treatment chemicals                                                                                         | Carpet fibers, including the WEAR-DATED® and ULTRON VIP® brands                             |
| GELVA® pressure-sensitive adhesives                                                                                              | SKYDROL® hydraulic fluids and SKYKLEEN® cleaning fluids for aviation                                                       | Industrial nylon fibers                                                                     |
|                                                                                                                                  | Process research, process development, scale-up capabilities and small scale manufacturing for the pharmaceutical industry | ACRILAN® acrylic fibers for apparel, upholstery fabrics, craft yarns and other applications |

# SOLUTIA INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Accounting policies of the segments are the same as those described in the summary of significant accounting policies in Note 1. However, segment profit reflects only operating expenses that are directly attributable to the segment. Unallocated service costs are managed centrally and primarily include costs of technology, engineering and manufacturing services that are provided to the segments. These amounts also include corporate administration costs. The company accounts for intersegment sales at agreed upon transfer prices. Intersegment sales are eliminated in consolidation. Segment assets consist primarily of customer receivables, finished goods inventories and fixed assets directly associated with the production processes of the segment (direct fixed assets). Segment depreciation and amortization is based upon direct fixed assets. Unallocated assets consist primarily of goodwill, identified intangible assets, deferred taxes, certain investments in equity affiliates and indirect fixed assets.

Solutia's 2000, 1999 and 1998 segment information follows:

|                                                            | Year Ended December 31, |                     |              |                |                     |               |                |                     |               |
|------------------------------------------------------------|-------------------------|---------------------|--------------|----------------|---------------------|---------------|----------------|---------------------|---------------|
|                                                            | 2000                    |                     |              | 1999           |                     |               | 1998           |                     |               |
|                                                            | Net Sales               | Inter-segment Sales | Profit       | Net Sales      | Inter-segment Sales | Profit        | Net Sales      | Inter-segment Sales | Profit        |
| <b>Segment:</b>                                            |                         |                     |              |                |                     |               |                |                     |               |
| Performance Films .....                                    | \$ 731                  | \$—                 | \$ 185       | \$ 713         | \$—                 | \$ 189        | \$ 614         | \$—                 | \$ 168        |
| Specialty Products .....                                   | 866                     | —                   | 182          | 615            | 2                   | 159           | 613            | 3                   | 152           |
| Integrated Nylon .....                                     | 1,580                   | 1                   | 160          | 1,508          | 4                   | 289           | 1,613          | 4                   | 376           |
| <b>Segment totals.....</b>                                 | <b>3,177</b>            | <b>1</b>            | <b>527</b>   | <b>2,836</b>   | <b>6</b>            | <b>637</b>    | <b>2,840</b>   | <b>7</b>            | <b>696</b>    |
| <b>Reconciliation to consolidated totals:</b>              |                         |                     |              |                |                     |               |                |                     |               |
| Sales eliminations .....                                   | (1)                     | (1)                 |              | (6)            | (6)                 |               | (7)            | (7)                 |               |
| Other revenues .....                                       | 9                       |                     |              | —              |                     |               | 2              |                     |               |
| Less unallocated service costs:                            |                         |                     |              |                |                     |               |                |                     |               |
| Cost of goods sold .....                                   |                         |                     | (207)        |                |                     | (124)         |                |                     | (70)          |
| Marketing, administrative and technological expenses ..... |                         |                     | (263)        |                |                     | (216)         |                |                     | (240)         |
| Amortization expense .....                                 |                         |                     | (33)         |                |                     | (3)           |                |                     | —             |
| Equity earnings from affiliates .....                      |                         |                     | 35           |                |                     | 36            |                |                     | 25            |
| Interest expense .....                                     |                         |                     | (83)         |                |                     | (40)          |                |                     | (43)          |
| Gain on sale of Polymer Modifiers business .....           |                         |                     | 73           |                |                     | —             |                |                     | —             |
| Other income (expense)—net .....                           |                         |                     | (8)          |                |                     | 13            |                |                     | 7             |
| <b>Consolidated totals:</b>                                |                         |                     |              |                |                     |               |                |                     |               |
| Net sales .....                                            | <u>\$3,185</u>          | <u>\$—</u>          |              | <u>\$2,830</u> | <u>\$—</u>          |               | <u>\$2,835</u> | <u>\$—</u>          |               |
| Income before income taxes .....                           |                         |                     | <u>\$ 41</u> |                |                     | <u>\$ 303</u> |                |                     | <u>\$ 375</u> |

|                                               | Year Ended December 31, |                      |                               |                       |                      |                               |                       |                      |                               |
|-----------------------------------------------|-------------------------|----------------------|-------------------------------|-----------------------|----------------------|-------------------------------|-----------------------|----------------------|-------------------------------|
|                                               | 2000                    |                      |                               | 1999                  |                      |                               | 1998                  |                      |                               |
|                                               | Assets                  | Capital Expenditures | Depreciation and Amortization | Assets                | Capital Expenditures | Depreciation and Amortization | Assets                | Capital Expenditures | Depreciation and Amortization |
| <b>Segment:</b>                               |                         |                      |                               |                       |                      |                               |                       |                      |                               |
| Performance Films .....                       | \$ 411                  | \$ 26                | \$ 28                         | \$ 484                | \$ 21                | \$ 30                         | \$ 371                | \$ 24                | \$ 27                         |
| Specialty Products .....                      | 508                     | 29                   | 27                            | 677                   | 8                    | 18                            | 324                   | 20                   | 19                            |
| Integrated Nylon .....                        | 1,041                   | 137                  | 58                            | 985                   | 189                  | 57                            | 887                   | 81                   | 56                            |
| <b>Segment totals.....</b>                    | <b>\$1,960</b>          | <b>\$192</b>         | <b>113</b>                    | <b>\$2,146</b>        | <b>218</b>           | <b>105</b>                    | <b>\$1,582</b>        | <b>125</b>           | <b>102</b>                    |
| <b>Reconciliation to consolidated totals:</b> |                         |                      |                               |                       |                      |                               |                       |                      |                               |
| Unallocated amounts .....                     | 1,621                   | 29                   | 78                            | 1,624                 | 39                   | 46                            | 1,183                 | 33                   | 45                            |
| <b>Consolidated totals.....</b>               | <b><u>\$3,581</u></b>   | <b><u>\$221</u></b>  | <b><u>\$191</u></b>           | <b><u>\$3,770</u></b> | <b><u>\$257</u></b>  | <b><u>\$151</u></b>           | <b><u>\$2,765</u></b> | <b><u>\$158</u></b>  | <b><u>\$147</u></b>           |

# SOLUTIA INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Solutia's geographic information for 2000, 1999 and 1998 follows:

|                                 | Net Sales      |                |                | Long-Lived Assets |                |
|---------------------------------|----------------|----------------|----------------|-------------------|----------------|
|                                 | 2000           | 1999           | 1998           | 2000              | 1999           |
| U.S.....                        | \$1,939        | \$1,992        | \$2,009        | \$ 899            | \$1,001        |
| Other countries.....            | 1,246          | 838            | 826            | 306               | 315            |
| <b>Consolidated totals.....</b> | <b>\$3,185</b> | <b>\$2,830</b> | <b>\$2,835</b> | <b>\$1,205</b>    | <b>\$1,316</b> |

### 17. Quarterly Data—Unaudited

|                                 |      | First<br>Quarter | Second<br>Quarter | Third<br>Quarter | Fourth<br>Quarter | Total<br>Year |
|---------------------------------|------|------------------|-------------------|------------------|-------------------|---------------|
| Net Sales.....                  | 2000 | \$ 846           | \$ 834            | \$ 774           | \$ 731            | \$3,185       |
|                                 | 1999 | 652              | 711               | 731              | 736               | 2,830         |
| Gross Profit.....               | 2000 | 199              | 158               | 143              | (14)              | 486           |
|                                 | 1999 | 105              | 193               | 183              | 171               | 652           |
| Operating Income.....           | 2000 | 79               | 37                | 35               | (127)             | 24            |
|                                 | 1999 | 26               | 102               | 94               | 72                | 294           |
| Net Income.....                 | 2000 | 51               | 4                 | 78               | (84)              | 49            |
|                                 | 1999 | 23               | 71                | 61               | 51                | 206           |
| Basic Earnings per Share.....   | 2000 | 0.47             | 0.04              | 0.75             | (0.82)            | 0.46          |
|                                 | 1999 | 0.21             | 0.64              | 0.55             | 0.46              | 1.86          |
| Diluted Earnings per Share..... | 2000 | 0.46             | 0.04              | 0.74             | (0.81)            | 0.46          |
|                                 | 1999 | 0.20             | 0.61              | 0.53             | 0.46              | 1.80          |
| Common Stock Price:             |      |                  |                   |                  |                   |               |
| 2000.....                       | High | 17.19            | 15.56             | 15.69            | 13.00             | 17.19         |
|                                 | Low  | 11.63            | 11.25             | 10.38            | 10.88             | 10.38         |
| 1999.....                       | High | 24.38            | 26.31             | 22.94            | 18.88             | 26.31         |
|                                 | Low  | 15.88            | 16.06             | 16.13            | 13.50             | 13.50         |

Net income in the second quarter of 2000 includes special net aftertax charges of \$31 million principally associated with the formation and start-up of the Astaris joint venture and Solutia's share of restructuring and asset impairment charges recorded by the Flexsys joint venture. Net income in the third quarter of 2000 includes a \$46 million aftertax gain on sale of the Polymer Modifiers business and income of \$7 million recorded in income taxes related to changes in German income tax laws. Net income in the fourth quarter of 2000 includes restructuring and asset impairment charges of \$96 million aftertax.

Net income in the first quarter of 1999 includes aftertax charges of \$18 million related to exiting Integrated Nylon's ammonia business, \$4 million related to the write down of an Integrated Nylon bulk continuous filament spinning machine to fair value and \$18 million related to the anticipated settlement of certain property claims litigation involving the Anniston, Alabama plant site.

Under SFAS No. 128, "Earnings per Share," the quarterly and total year calculations of basic and diluted earnings per share are based on weighted average shares outstanding for that quarterly or total year period, respectively. As a result, the sum of diluted earnings per share for the quarterly periods may not equal total year earnings per share.

**Item 9. CHANGES IN AND DISAGREEMENTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.**

None.

**PART III****Item 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT.**

Information about directors and executive officers appearing under "Election of Directors" on pages 5 through 7 of Solutia's Notice of Annual Meeting and Proxy Statement dated March 15, 2001, is incorporated by reference. The following information about Solutia's executive officers on March 1, 2001, is included pursuant to Instruction 3 of Item 401(b) of Regulation S-K:

| Name-Age               | Present Position with Registrant                                     | Year First Became an Executive Officer | Other Business Experience since January 1, 1996                                                                                                                                                                                                              |
|------------------------|----------------------------------------------------------------------|----------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| John C. Hunter III, 54 | Chairman, President, Chief Executive Officer and Director            | 1997                                   | President, Chief Operating Officer and Director, 1997-1999. President, Fibers Business Unit, Monsanto, 1995-1997.                                                                                                                                            |
| Karl R. Barnickol, 59  | Senior Vice President, General Counsel and Secretary                 | 1997                                   | Associate General Counsel and Assistant Secretary of Monsanto, 1985-1997.                                                                                                                                                                                    |
| Russell J. Belle, 58   | Vice President and General Manager, Industrial Products              | 2001                                   | Vice President and General Manager, Specialty Chemicals, 2000-2001. Vice President and General Manager, Intermediates, 1998-1999. Vice President and General Manager, Specialty Resins, 1997-1998. Business Director, Specialty Resins, Monsanto, 1995-1997. |
| Robert A. Clausen, 56  | Senior Vice President and Chief Financial Officer; Advisory Director | 1997                                   | President, Monsanto Business Services, 1994-1997.                                                                                                                                                                                                            |
| Sheila B. Feldman, 46  | Vice President, Human Resources and Public Affairs                   | 1997                                   | Vice President, Human Resources, 1997-1999. Director, Human Resources, Monsanto Business Services and Stewardship, 1995-1997.                                                                                                                                |
| John J. Ferguson, 48   | Senior Vice President, Integrated Nylon                              | 1998                                   | Senior Vice President, Shared Services and Supply Chain, 1998-1999. Vice President and General Manager, SAFLEX® Plastic Interlayer, 1997-1998. President, SAFLEX® Plastic Interlayer, Monsanto, 1994-1997.                                                   |
| Victoria M. Holt, 43   | Vice President and General Manager, Performance Films                | 1999                                   | Vice President and General Manager, Saflex, 1999-2001. Vice President and General Manager, Acrilan Business Unit, 1997-1998. Business Director, Acrilan Business Unit, Monsanto, 1996-1997. Assistant to Monsanto's Chief Executive Officer, 1995-1996.      |

| Name-Age              | Present Position with Registrant                         | Year First Became an Executive Officer | Other Business Experience since January 1, 1996                                                                                                                                                                                                                                            |
|-----------------------|----------------------------------------------------------|----------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Todd B. Imhoff, 36    | Vice President, Corporate Services                       | 2001                                   | Vice President, Supply Chain, 2000-2001. Director, Strategic Procurement, 1999-2000. Manager, Supply Chain Strategy, 1997-1999. National Accounts Manager (Operations), Americas Division of Monsanto, 1996-1997. Manager, U.S. Package Distribution, Americas Division of Monsanto, 1996. |
| Michael E. Miller, 59 | Vice Chairman and Director                               | 1997                                   | Vice Chairman and Chief Operating Officer and Director, 1999-2001. Vice Chairman and Advisory Director, 1998-1999. Senior Vice President, Chief Administrative Officer, and Advisory Director, 1997-1998. President, Specialty Products Business Unit, Monsanto, 1995-1997.                |
| Robert B. Toth, 40    | Vice President and General Manager, Resins and Additives | 1999                                   | Vice President and General Manager, Polymer Modifiers and Resins, 1998-1999. Vice President and General Manager, Polymer Modifiers, 1997-1998. Director, Global Strategy for Crop Business Unit of Monsanto, 1996-1997.                                                                    |

The above listed individuals are elected to the offices set opposite their names to hold office until their successors are duly elected and have qualified, or until their earlier death, resignation or removal.

**Item 11. EXECUTIVE COMPENSATION.**

Information appearing under "Compensation of Directors" on page 9 and under "Summary Compensation Table," "Option Grants in 2000," "Aggregated Option Exercises in 2000 and Year-End Option Values," "Long-Term Incentive Plan—Awards in Last Fiscal Year," "Pension Plans," and "Agreements with Named Executive Officers" on pages 15 through 19 of Solutia's 2001 Proxy Statement is incorporated here by reference.

**Item 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT.**

Information appearing under "Ownership of Company Common Stock" on pages 10 and 11 of Solutia's 2001 Proxy Statement is incorporated here by reference.

**Item 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.**

Information appearing under "Relationships and Transactions" on page 21 of Solutia's 2001 Proxy Statement is incorporated here by reference.

#### PART IV

##### Item 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULE, AND REPORTS ON FORM 8-K.

(a) Documents filed as part of this report:

1. Financial Statements—See the Index to Consolidated Financial Statements and Financial Statement Schedule at page 25 of this report.
2. The following supplemental schedule for the years ended December 31, 2000, 1999 and 1998:

II—Valuation and Qualifying Accounts

All other supplemental schedules are omitted because of the absence of the conditions under which they are required.

3. Exhibits—See the Exhibit Index beginning at page 57 of this report. For a listing of all management contracts and compensatory plans or arrangements required to be filed as Exhibits to this report, see the exhibits listed under Exhibit Nos. 10(a), 10(b), 10(d), 10(e), 10(f), 10(h), 10(i), 10(j), 10(k), 10(l) and 10(o) on pages 57 and 58 of the Exhibit Index. The following exhibits listed in the Exhibit Index are filed with this report:

- 10(m) U.S. \$250,000,000 364-Day Multicurrency Credit Agreement, dated as of November 21, 2000, among Solutia, the lenders named therein, Bank of America, N.A., as Syndication Agent and Citibank, N.A., as Administrative Agent
- 10(p) Amendment No. 1, dated as of November 21, 2000, to U.S. \$800,000,000 Amended and Restated Five-Year Credit Agreement, dated as of November 23, 1999, among Solutia, the initial lenders named therein, Bank of America, N.A., as Syndication Agent and Citibank, N.A., as Administrative Agent
- 21 Subsidiaries of the Registrant (see page 59)
- 23 Consent of Independent Auditors (see page 60)
- 24(a) Powers of Attorney submitted by John C. Hunter III, Robert A. Clausen, James M. Sullivan, Michael E. Miller, Robert T. Blakely, Paul H. Hatfield, Robert H. Jenkins, Frank A. Metz, Jr., J. Patrick Mulcahy, Sally G. Narodick, William D. Ruckelshaus and John B. Slaughter
- 24(b) Certified copy of Board resolution authorizing Form 10-K filing using powers of attorney
- 99 Computation of the Ratio of Earnings to Fixed Charges (see page 62)

(b) Reports on Form 8-K during the quarter ended December 31, 2000:

None.

## SIGNATURES

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

### SOLUTIA INC.

By: /s/ JAMES M. SULLIVAN  
James M. Sullivan  
Vice President and Controller  
(Principal Accounting Officer)

Date: March 8, 2001

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

| <u>Signature</u>                                  | <u>Title</u>                                                                            | <u>Date</u>   |
|---------------------------------------------------|-----------------------------------------------------------------------------------------|---------------|
| <u>*</u><br>John C. Hunter III                    | Chairman, President, Chief Executive Officer and Director (Principal Executive Officer) | March 8, 2001 |
| <u>*</u><br>Robert A. Clausen                     | Senior Vice President and Chief Financial Officer (Principal Financial Officer)         | March 8, 2001 |
| <u>/s/ JAMES M. SULLIVAN</u><br>James M. Sullivan | Vice President and Controller (Principal Accounting Officer)                            | March 8, 2001 |
| <u>*</u><br>Michael E. Miller                     | Vice Chairman and Director                                                              | March 8, 2001 |
| <u>*</u><br>Robert T. Blakely                     | Director                                                                                | March 8, 2001 |
| <u>*</u><br>Paul H. Hatfield                      | Director                                                                                | March 8, 2001 |
| <u>*</u><br>Robert H. Jenkins                     | Director                                                                                | March 8, 2001 |

| <u>Signature</u>                     | <u>Title</u> | <u>Date</u>   |
|--------------------------------------|--------------|---------------|
| *<br>_____<br>Frank A. Metz, Jr.     | Director     | March 8, 2001 |
| *<br>_____<br>J. Patrick Mulcahy     | Director     | March 8, 2001 |
| *<br>_____<br>Sally G. Narodick      | Director     | March 8, 2001 |
| *<br>_____<br>William D. Ruckelshaus | Director     | March 8, 2001 |
| *<br>_____<br>John B. Slaughter      | Director     | March 8, 2001 |

\*Karl R. Barnickol, by signing his name hereto, does sign this document on behalf of the above noted individuals, pursuant to powers of attorney duly executed by such individuals which have been filed as an Exhibit to this Form 10-K.

\_\_\_\_\_  
/s/ KARL R. BARNICKOL  
Karl R. Barnickol  
Attorney-in-Fact

## EXHIBIT INDEX

These exhibits are numbered in accordance with the Exhibit Table of Item 601 of Regulation S-K.

| Exhibit No. | Description                                                                                                                                                                                                                          |
|-------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 2(a)        | Distribution Agreement (incorporated by reference to Exhibit 2 of Solutia's Registration Statement on Form S-1 (333-36355) filed September 25, 1997)                                                                                 |
| 2(b)        | Joint Venture Agreement between Solutia Inc. and FMC Corporation* (incorporated by reference to Exhibit 2(i) of Solutia's Form 8-K filed on April 27, 2000)                                                                          |
| 2(c)        | First Amendment to Joint Venture Agreement between Solutia Inc. and FMC Corporation (incorporated by reference to Exhibit 2(ii) of Solutia's Form 8-K filed on April 27, 2000)                                                       |
| 2(d)        | Second Amendment to Joint Venture Agreement between Solutia Inc. and FMC Corporation (incorporated by reference to Exhibit 2(iii) of Solutia's Form 8-K filed on April 27, 2000)                                                     |
| 2(e)        | Third Amendment to Joint Venture Agreement between Solutia Inc. and FMC Corporation* (incorporated by reference to Exhibit 2(iv) of Solutia's Form 8-K filed on April 27, 2000)                                                      |
| 3(a)        | Restated Certificate of Incorporation of Solutia (incorporated by reference to Exhibit 3(a) of Solutia's Registration Statement on Form S-1 (333-36355) filed September 25, 1997)                                                    |
| 3(b)        | By-Laws of Solutia Inc., as amended April 28, 1999 (incorporated by reference to Exhibit 3(ii) of Solutia's Form 10-Q for the quarter ended March 31, 1999)                                                                          |
| 4(a)        | Rights Agreement (incorporated by reference to Exhibit 4 of Solutia's Registration Statement on Form 10 filed on August 7, 1997)                                                                                                     |
| 4(b)        | Indenture dated as of October 1, 1997, between Solutia Inc. and The Chase Manhattan Bank, as Trustee (incorporated by reference to Exhibit 4.1 of Solutia's Form 10-Q for the quarter ended September 30, 1997)                      |
| 4(c)        | 6.5% Notes due 2002 in the principal amount of \$150,000,000 (incorporated by reference to Exhibit 4.2 of Solutia's Form 10-Q for the quarter ended September 30, 1997)                                                              |
| 4(d)        | 7.375% Debentures due 2027 in the principal amount of \$200,000,000 (incorporated by reference to Exhibit 4.3 of Solutia's Form 10-Q for the quarter ended September 30, 1997)                                                       |
| 4(e)        | 7.375% Debentures due 2027 in the principal amount of \$100,000,000 (incorporated by reference to Exhibit 4.4 of Solutia's Form 10-Q for the quarter ended September 30, 1997)                                                       |
| 4(f)        | 6.72% Debentures due 2037 in the principal amount of \$150,000,000 (incorporated by reference to Exhibit 4.5 of Solutia's Form 10-Q for the quarter ended September 30, 1997)                                                        |
| 4(g)        | Registrant agrees to furnish to the Securities and Exchange Commission upon request copies of instruments defining the rights of holders of certain unregistered long-term debt of the registrant and its consolidated subsidiaries. |
| 9           | Omitted—Inapplicable                                                                                                                                                                                                                 |
| 10(a)       | Financial Planning and Tax Preparation Services Program for the Executive Leadership Team (incorporated by reference to Exhibit 10(a) of Solutia's Form 10-K for the year ended December 31, 1997)                                   |
| 10(b)       | Employee Benefits Allocation Agreement (incorporated by reference to Exhibit 10(a) of Solutia's Registration Statement on Form S-1 (333-36355) filed September 25, 1997)                                                             |
| 10(c)       | Tax Sharing and Indemnification Agreement (incorporated by reference to Exhibit 10(b) of Solutia's Registration Statement on Form S-1 (333-36355) filed September 25, 1997)                                                          |
| 10(d)       | Solutia Inc. Management Incentive Replacement Plan as amended on April 28, 1999 (incorporated by reference to Exhibit 10(2) of Solutia's Form 10-Q for the quarter ended June 30, 1999)                                              |

\*Confidential treatment has been granted for a portion of this exhibit.

# EXHIBIT INDEX (Continued)

| <u>Exhibit No.</u> | <u>Description</u>                                                                                                                                                                                                                                                                                                                                                                                                                    |
|--------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 10(e)              | Solutia Inc. 1997 Stock-Based Incentive Plan as amended on April 28, 1999 and April 26, 2000 (incorporated by reference to Exhibit 10(1) of Solutia's Form 10-Q for the quarter ended June 30, 2000)                                                                                                                                                                                                                                  |
| 10(f)              | Solutia Inc. Non-Employee Director Compensation Plan, as amended February 24, 1999 and January 26, 2000 (incorporated by reference to Exhibit 10 of Solutia's Form 10-Q for the quarter ended March 31, 2000)                                                                                                                                                                                                                         |
| 10(g)              | U.S. \$800,000,000 Amended and Restated Five Year Credit Agreement, dated as of November 23, 1999, among Solutia, the initial lenders named therein, Bank of America, N.A., as Syndication Agent and Citibank, N.A., as Administrative Agent (incorporated by reference to Exhibit 10(g) of Solutia's Form 10-K for the year ended December 31, 1999)                                                                                 |
| 10(h)              | Form of Employment Agreement with certain Named Executive Officers (incorporated by reference to Exhibit 10(1) of Solutia's Form 10-Q for the quarter ended March 31, 1998)                                                                                                                                                                                                                                                           |
| 10(i)              | Form of Employment Agreement with other executive officers (incorporated by reference to Exhibit 10(2) of Solutia's Form 10-Q for the quarter ended March 31, 1998)                                                                                                                                                                                                                                                                   |
| 10(j)              | Solutia Inc. Annual Incentive Plan (incorporated by reference to Appendix B of the Solutia Inc. Notice of Annual Meeting and Proxy Statement dated March 9, 2000)                                                                                                                                                                                                                                                                     |
| 10(k)              | Solutia Inc. Long-Term Incentive Plan (incorporated by reference to Appendix C of the Solutia Inc. Notice of Annual Meeting and Proxy Statement dated March 9, 2000)                                                                                                                                                                                                                                                                  |
| 10(l)              | Solutia Inc. Deferred Compensation Plan (incorporated by reference to Exhibit 10 of Solutia's Form 10-Q for the quarter ended September 30, 1998)                                                                                                                                                                                                                                                                                     |
| 10(m)              | U.S. \$250,000,000 364-Day Multicurrency Credit Agreement, dated as of November 21, 2000, among Solutia, the lenders named therein, Bank of America, N.A., as Syndication Agent and Citibank, N.A., as Administrative Agent                                                                                                                                                                                                           |
| 10(n)              | Agreement, dated 10th November, 1999, for the sale and purchase of class A shares, preference shares and loan stock and the cancellation of warrants in Viking Resins Group Holdings B.V. between (a) Solutia Inc., as purchaser, (b) the holders of the A shares, preference shares and loan stock as sellers, and (c) the warrant holders (incorporated by reference to Exhibit 2.1 of Solutia's Form 8-K filed on January 4, 2000) |
| 10(o)              | Solutia Inc. 2000 Stock-Based Incentive Plan (incorporated by reference to Appendix A of the Solutia Inc. Notice of Annual Meeting and Proxy Statement dated March 9, 2000)                                                                                                                                                                                                                                                           |
| 10(p)              | Amendment No. 1, dated as of November 21, 2000, to U.S. \$800,000,000 Amended and Restated Five-Year Credit Agreement, dated as of November 23, 1999, among Solutia, the initial lenders named therein, Bank of America, N.A., as Syndication Agent and Citibank, N.A., as Administrative Agent                                                                                                                                       |
| 11                 | Omitted—Inapplicable; see "Statement of Consolidated Income" on page 27                                                                                                                                                                                                                                                                                                                                                               |
| 16                 | Omitted—Inapplicable                                                                                                                                                                                                                                                                                                                                                                                                                  |
| 18                 | Omitted—Inapplicable                                                                                                                                                                                                                                                                                                                                                                                                                  |
| 21                 | Subsidiaries of the Registrant (see page 59)                                                                                                                                                                                                                                                                                                                                                                                          |
| 22                 | Omitted—Inapplicable                                                                                                                                                                                                                                                                                                                                                                                                                  |
| 23                 | Consent of Independent Auditors (see page 60)                                                                                                                                                                                                                                                                                                                                                                                         |
| 24(a)              | Powers of Attorney submitted by John C. Hunter III, Robert A. Clausen, James M. Sullivan, Michael E. Miller, Robert T. Blakely, Paul H. Hatfield, Robert H. Jenkins, Frank A. Metz, Jr., J. Patrick Mulcahy, Sally G. Narodick, William D. Ruckelshaus and John B. Slaughter                                                                                                                                                          |
| 24(b)              | Certified copy of Board resolution authorizing Form 10-K filing utilizing powers of attorney                                                                                                                                                                                                                                                                                                                                          |
| 99                 | Computation of the Ratio of Earnings to Fixed Charges (see page 62)                                                                                                                                                                                                                                                                                                                                                                   |

Only Exhibits Nos. 21, 23, and 99 have been included in the printed copy of this report.

**EXHIBIT 21**

**SUBSIDIARIES OF THE REGISTRANT**

The following is a list of Solutia's subsidiaries as of December 31, 2000, except for unnamed subsidiaries which, considered in the aggregate as a single subsidiary, would not constitute a significant subsidiary.

|                                                                         | Percentage of<br>Voting Power<br>Owned by<br>Solutia |
|-------------------------------------------------------------------------|------------------------------------------------------|
| CPFilms Inc.....                                                        | 100%                                                 |
| Erste Viking Resins Germany 1 GmbH.....                                 | 100%                                                 |
| Monchem, Inc.....                                                       | 100%                                                 |
| Monchem International, Inc.....                                         | 100%                                                 |
| Solutia Deutschland Holding GmbH.....                                   | 100%                                                 |
| Solutia Europe S.A./N.V. ....                                           | 100%                                                 |
| Solutia International Sales, Inc.....                                   | 99%                                                  |
| Solutia Investments, LLC.....                                           | 100%                                                 |
| Solutia Netherlands Holdings B.V. (formerly Alhadar Holdings B.V.)..... | 100%                                                 |
| Solutia Netherlands International B.V.....                              | 100%                                                 |
| Solutia Systems, Inc.....                                               | 100%                                                 |
| Solutia U.K. Holdings Limited .....                                     | 100%                                                 |
| Solutia U.K. Ltd.....                                                   | 100%                                                 |
| Vianova Resins Aktiengesellschaft .....                                 | 100%                                                 |
| Vianova Resins GmbH & Co. KG.....                                       | 100%                                                 |

**CONSENT OF INDEPENDENT AUDITORS**

We consent to the incorporation by reference in Solutia's Registration Statements on Form S-8 (Nos. 333-34561, 333-34587, 333-34589, 333-34591, 333-34593, 333-34683, 333-35689, 333-47911, 333-51081, 333-74463, 333-74465, 333-32112 and 333-39972) and Solutia's Registration Statement on Form S-3 (No. 333-46070) of our opinion dated February 28, 2001, appearing in this annual report on Form 10-K of Solutia Inc. for the year ended December 31, 2000.

/s/ DELOITTE & TOUCHE LLP

DELOITTE & TOUCHE LLP

Saint Louis, Missouri  
March 8, 2001

**SCHEDULE II**

**SOLUTIA INC.**

**VALUATION AND QUALIFYING ACCOUNTS  
FOR THE YEARS ENDED DECEMBER 31, 2000, 1999 AND 1998**

**(Dollars in Millions)**

| <u>COLUMN A</u>                             | <u>COLUMN B</u>                             | <u>COLUMN C</u>                                      |                                                  | <u>COLUMN D</u>   | <u>COLUMN E</u>                         |
|---------------------------------------------|---------------------------------------------|------------------------------------------------------|--------------------------------------------------|-------------------|-----------------------------------------|
| <u>Description</u>                          | <u>Balance at<br/>beginning<br/>of year</u> | <u>Additions</u>                                     |                                                  | <u>Deductions</u> | <u>Balance at<br/>end<br/>of period</u> |
|                                             |                                             | <u>(1)<br/>Charged to<br/>costs and<br/>expenses</u> | <u>(2)<br/>Charged<br/>to other<br/>accounts</u> |                   |                                         |
| <b>Year Ended December 31, 2000</b>         |                                             |                                                      |                                                  |                   |                                         |
| Valuation accounts for doubtful receivables | \$ 12                                       | \$11                                                 | \$—                                              | \$11              | \$12                                    |
| Restructuring reserves .....                | 20                                          | 61                                                   | 11                                               | 27                | 65                                      |
| <b>Year Ended December 31, 1999</b>         |                                             |                                                      |                                                  |                   |                                         |
| Valuation accounts for doubtful receivables | \$ 8                                        | \$—                                                  | \$ 7                                             | \$ 3              | \$12                                    |
| Restructuring reserves .....                | 55                                          | 28                                                   | —                                                | 63                | 20                                      |
| <b>Year Ended December 31, 1998</b>         |                                             |                                                      |                                                  |                   |                                         |
| Valuation accounts for doubtful receivables | \$ 7                                        | \$ 2                                                 | \$—                                              | \$ 1              | \$ 8                                    |
| Restructuring reserves .....                | 104                                         | —                                                    | —                                                | 49                | 55                                      |

## SOLUTIA INC.

## CALCULATION OF THE RATIO OF EARNINGS TO FIXED CHARGES

(Dollars in Millions)

|                                                                                                                    | Four Months<br>Ended<br>December 31, 1999 <sup>(1)</sup> | 1998          | 1999          | 2000          |
|--------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------|---------------|---------------|---------------|
| Income from continuing operations, before income taxes<br>and equity earnings from affiliates <sup>(2)</sup> ..... | \$ 37                                                    | \$ 350        | \$ 267        | \$ 6          |
| Add:                                                                                                               |                                                          |               |               |               |
| Fixed charges.....                                                                                                 | 22                                                       | 58            | 62            | 114           |
| Amortization of capitalized interest.....                                                                          | 2                                                        | 7             | 7             | 7             |
| Dividends from affiliated companies.....                                                                           | 14                                                       | 37            | 60            | 45            |
| Less:                                                                                                              |                                                          |               |               |               |
| Interest capitalized.....                                                                                          | (4)                                                      | (6)           | (13)          | (18)          |
| Income as adjusted.....                                                                                            | <u>\$ 71</u>                                             | <u>\$ 446</u> | <u>\$ 383</u> | <u>\$ 154</u> |
| Fixed charges:                                                                                                     |                                                          |               |               |               |
| Interest expensed and capitalized.....                                                                             | 19                                                       | 49            | 53            | 101           |
| Amortization of debt premium.....                                                                                  | —                                                        | —             | —             | —             |
| Estimate of interest within rental expense.....                                                                    | 3                                                        | 9             | 9             | 13            |
| Fixed charges.....                                                                                                 | <u>\$ 22</u>                                             | <u>\$ 58</u>  | <u>\$ 62</u>  | <u>\$ 114</u> |
| Ratio of Earnings to Fixed Charges.....                                                                            | 3.23                                                     | 7.69          | 6.18          | 1.35          |

(1) We have not calculated the ratio of earnings to fixed charges for the periods before September 1, 1997. Historical computation of earnings to fixed charges is not considered meaningful before that date because we were not an independent company and Monsanto Company did not allocate debt to us.

(2) Includes restructuring and other unusual items of \$122 million for the year ended December 31, 2000, \$63 million for the year ended December 31, 1999, and \$72 million for the four months ended December 31, 1997.

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