

SCOTTS MIRACLE-GRO CO
Form 10-Q
August 10, 2011
Table of Contents

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

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE QUARTERLY PERIOD ENDED JULY 2, 2011

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE TRANSITION PERIOD FROM TO
COMMISSION FILE NUMBER: 001-11593

THE SCOTTS MIRACLE-GRO COMPANY

(Exact name of registrant as specified in its charter)

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

OHIO
(State or other jurisdiction of
incorporation or organization)

31-1414921
(I.R.S. Employer
Identification No.)

14111 SCOTTSLAWN ROAD,

MARYSVILLE, OHIO
(Address of principal executive offices)

43041
(Zip Code)

(937) 644-0011

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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

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

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

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

Class	Outstanding at August 4, 2011
Common Shares, \$0.01 stated value, no par value	62,855,438 common shares

Table of Contents

THE SCOTTS MIRACLE-GRO COMPANY

INDEX

	PAGE NO.
<u>PART I. FINANCIAL INFORMATION:</u>	
Item 1. <u>Financial Statements</u>	
<u>Condensed, Consolidated Statements of Operations Three and nine months ended July 2, 2011 and July 3, 2010</u>	3
<u>Condensed, Consolidated Statements of Cash Flows Nine months ended July 2, 2011 and July 3, 2010</u>	4
<u>Condensed, Consolidated Balance Sheets July 2, 2011, July 3, 2010 and September 30, 2010</u>	5
<u>Notes to Condensed, Consolidated Financial Statements</u>	6
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	31
Item 3. <u>Quantitative and Qualitative Disclosures about Market Risk</u>	40
Item 4. <u>Controls and Procedures</u>	40
<u>PART II. OTHER INFORMATION:</u>	
Item 1. <u>Legal Proceedings</u>	40
Item 1A. <u>Risk Factors</u>	41
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	41
Item 6. <u>Exhibits</u>	42
<u>Signatures</u>	43
<u>Index to Exhibits</u>	44

Table of Contents

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

THE SCOTTS MIRACLE-GRO COMPANY

CONDENSED, CONSOLIDATED STATEMENTS OF OPERATIONS

(IN MILLIONS, EXCEPT PER SHARE DATA)

(UNAUDITED)

	September 30, THREE MONTHS ENDED		September 30, NINE MONTHS ENDED	
	JULY 2, 2011	JULY 3, 2010	JULY 2, 2011	JULY 3, 2010
Net sales	\$ 1,058.7	\$ 1,172.6	\$ 2,418.5	\$ 2,475.7
Cost of sales	657.5	690.8	1,503.4	1,524.6
Cost of sales product registration and recall matters	1.1		3.2	1.5
Gross profit	400.1	481.8	911.9	949.6
Operating expenses:				
Selling, general and administrative	192.4	201.3	551.8	544.3
Product registration and recall matters	5.7	1.5	7.8	4.3
Impairment, restructuring and other charges	13.8		13.8	
Other income, net	(4.2)	(1.1)	(5.0)	(6.8)
Income from operations	192.4	280.1	343.5	407.8
Costs related to refinancing	1.2		1.2	
Interest expense	14.0	11.2	37.3	35.0
Income from continuing operations before income taxes	177.2	268.9	305.0	372.8
Income tax expense from continuing operations	65.5	99.4	111.4	139.2
Income from continuing operations	111.7	169.5	193.6	233.6
Income (loss) from discontinued operations, net of tax	(0.1)	6.4	27.7	3.1
Net income	\$ 111.6	\$ 175.9	\$ 221.3	\$ 236.7
BASIC INCOME PER COMMON SHARE:				
Income from continuing operations	\$ 1.73	\$ 2.55	\$ 2.95	\$ 3.53
Income from discontinued operations		0.10	0.42	0.05
Basic net income per common share	\$ 1.73	\$ 2.65	\$ 3.37	\$ 3.58
Weighted-average common shares outstanding during the period	64.5	66.5	65.6	66.2
DILUTED INCOME PER COMMON SHARE:				
Income from continuing operations	\$ 1.69	\$ 2.50	\$ 2.89	\$ 3.46

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

Income from discontinued operations			0.09		0.41		0.05
Diluted net income per common share	\$	1.69	\$	2.59	\$	3.30	\$ 3.51
Weighted-average common shares outstanding during the period plus dilutive potential common shares		66.2		67.9		67.1	67.4
Dividends declared per common share	\$	0.250	\$	0.125	\$	0.750	\$ 0.375

See notes to condensed, consolidated financial statements

Table of Contents

THE SCOTTS MIRACLE-GRO COMPANY

CONDENSED, CONSOLIDATED STATEMENTS OF CASH FLOWS

(IN MILLIONS)

(UNAUDITED)

	September 30, NINE MONTHS ENDED	September 30, JULY 3,
	JULY 2, 2011	2010
OPERATING ACTIVITIES		
Net income	\$ 221.3	\$ 236.7
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Impairment, restructuring and other charges, excluding share-based compensation expense	12.4	
Costs related to refinancing	1.2	
Share-based compensation expense	14.3	12.5
Depreciation	37.3	36.3
Amortization	8.7	8.3
Gain on sale of long-lived assets	(0.1)	(21.5)
Gain on sale of business	(93.0)	
Changes in assets and liabilities, net of acquired businesses:		
Accounts receivable	(352.9)	(311.3)
Inventories	(87.8)	(13.9)
Prepaid and other assets	(8.0)	(8.4)
Accounts payable	113.9	44.9
Other current liabilities	121.8	163.5
Restructuring reserves	(0.3)	
Other non-current items	(2.7)	18.4
Other, net	0.4	(9.3)
Net cash (used in) provided by operating activities	(13.5)	156.2
INVESTING ACTIVITIES		
Proceeds from sale of long-lived assets	0.2	23.6
Proceeds from sale of business, net of transaction costs	253.9	
Investments in property, plant and equipment	(53.3)	(46.9)
Payment of contingent consideration and related	(20.0)	
Investment in acquired business, net of cash acquired	(0.8)	
Net cash provided by (used in) investing activities	180.0	(23.3)
FINANCING ACTIVITIES		
Borrowings under revolving and bank lines of credit and term loans	1,419.2	927.8
Repayments under revolving and bank lines of credit and term loans	(1,459.2)	(1,234.8)
Proceeds from issuance of Senior Notes, net of discount	200.0	198.5
Financing and issuance fees	(18.5)	(5.5)
Dividends paid	(49.4)	(25.9)
Purchase of treasury shares	(218.7)	
Payments on seller notes		(0.2)
Excess tax benefits from share-based payment arrangements	5.4	3.9
Cash received from the exercise of stock options	29.4	14.8

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

Net cash used in financing activities		(91.8)		(121.4)
Effect of exchange rate changes on cash		1.5		(4.4)
Net increase in cash and cash equivalents		76.2		7.1
Cash and cash equivalents at beginning of period		88.1		70.6
Cash and cash equivalents at end of period	\$	164.3	\$	77.7
Supplemental cash flow information				
Interest paid, net of interest capitalized	\$	(33.6)	\$	(29.2)
Income taxes paid		(63.1)		(39.0)
	See notes to condensed, consolidated financial statements			

Table of Contents

THE SCOTTS MIRACLE-GRO COMPANY
CONDENSED, CONSOLIDATED BALANCE SHEETS

(IN MILLIONS, EXCEPT PER SHARE DATA)

	September 30, JULY 2, 2011 UNAUDITED	September 30, JULY 3, 2010	September 30, SEPTEMBER 30, 2010 (SEE NOTE 1)
ASSETS			
Current assets:			
Cash and cash equivalents	\$ 164.3	\$ 77.7	\$ 88.1
Accounts receivable, less allowances of \$13.6, \$7.3 and \$7.7, respectively	693.9	603.2	350.9
Accounts receivable pledged		23.3	
Inventories, net	442.2	405.9	352.9
Assets held for sale		206.0	193.1
Prepaid and other assets	137.3	161.2	133.1
Total current assets	1,437.7	1,477.3	1,118.1
Property, plant and equipment, net of accumulated depreciation of \$496.8, \$448.2 and \$461.1, respectively	394.3	359.4	381.3
Goodwill	306.5	305.8	305.8
Intangible assets, net	343.2	347.1	330.2
Other assets	45.5	33.6	28.6
Total assets	\$ 2,527.2	\$ 2,523.2	\$ 2,164.0
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities:			
Current portion of debt	\$ 2.1	\$ 200.0	\$ 195.0
Accounts payable	258.8	213.3	141.7
Liabilities held for sale		44.4	45.3
Other current liabilities	490.2	536.4	354.8
Total current liabilities	751.1	994.1	736.8
Long-term debt	782.1	490.2	436.7
Other liabilities	225.7	204.1	226.0
Total liabilities	1,758.9	1,688.4	1,399.5
Commitments and contingencies (notes 3 and 12)			
Shareholders' equity:			
Common shares and capital in excess of \$.01 stated value per share, 63.7, 66.9 and 66.8 shares issued and outstanding, respectively	426.7	439.3	434.0
Retained earnings	671.3	548.8	499.6
Treasury shares, at cost: 4.6, 1.6, and 1.8 shares, respectively	(252.6)	(86.5)	(92.0)
Accumulated other comprehensive loss	(77.1)	(66.8)	(77.1)
Total shareholders' equity	768.3	834.8	764.5

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

Total liabilities and shareholders equity	\$	2,527.2	\$	2,523.2	\$	2,164.0
---	----	---------	----	---------	----	---------

See notes to condensed, consolidated financial statements

Table of Contents

NOTES TO CONDENSED, CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

NATURE OF OPERATIONS

The Scotts Miracle-Gro Company (Scotts Miracle-Gro) and its subsidiaries (collectively, together with Scotts Miracle-Gro, the Company) are engaged in the manufacturing, marketing and sale of branded products for consumer lawn and garden care. The Company s primary customers include home centers, mass merchandisers, warehouse clubs, large hardware chains, independent hardware stores, nurseries, garden centers and food and drug stores. The Company s products are sold primarily in North America and the European Union. The Company also operates the Scotts LawnService® business, which provides residential and commercial lawn care, tree and shrub care and limited pest control services in the United States.

On February 28, 2011, the Company completed the sale of a significant majority of the assets of its Global Professional business (excluding the non-European professional seed business, Global Pro) to Israel Chemicals Ltd. (ICL). Effective in the Company s first quarter of fiscal 2011, the Company classified Global Pro as discontinued operations. See NOTE 2. DISCONTINUED OPERATIONS.

Due to the nature of the consumer lawn and garden business, the majority of sales to customers occur in the Company s second and third fiscal quarters. On a combined basis, net sales for the second and third fiscal quarters represent approximately 75% of annual net sales.

ORGANIZATION AND BASIS OF PRESENTATION

The Company s condensed, consolidated financial statements are unaudited; however, in the opinion of management, these financial statements are presented in accordance with accounting principles generally accepted in the United States of America (GAAP). The condensed, consolidated financial statements include the accounts of Scotts Miracle-Gro and its subsidiaries. All intercompany transactions and accounts have been eliminated in consolidation. The Company s consolidation criteria are based on majority ownership (as evidenced by a majority voting interest in the entity) and an objective evaluation and determination of effective management control. Interim results reflect all normal and recurring adjustments and are not necessarily indicative of results for a full year.

Certain information and disclosures normally included in financial statements prepared in accordance with GAAP have been omitted or condensed pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). The information in this report should be read in conjunction with Scotts Miracle-Gro s Annual Report on Form 10-K for the fiscal year ended September 30, 2010, which includes a complete set of disclosures, including the Company s significant accounting policies.

The Company s Condensed, Consolidated Balance Sheet at September 30, 2010 has been derived from the Company s audited Consolidated Balance Sheet at that date, but does not include all of the information and disclosures required by GAAP for complete financial statements.

USE OF ESTIMATES

The preparation of condensed, consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported and related disclosures. Although these estimates are based on management s best knowledge of current events and actions the Company may undertake in the future, actual results ultimately may differ from the estimates.

RECENT ACCOUNTING PRONOUNCEMENTS

Variable Interest Entities

In June 2009, the Financial Accounting Standards Board (FASB) issued new accounting guidance requiring an enterprise to perform an analysis to determine whether the enterprise s variable interest or interests give it a controlling financial interest in a variable interest entity. The new guidance also requires enhanced disclosures that will provide users of financial statements with more transparent information about an enterprise s involvement in a variable interest entity. The Company adopted the new guidance on October 1, 2010 and the adoption did not impact the Company s financial statements and related disclosures.

Table of Contents

Revenue Recognition Multiple-Element Arrangements

In October 2009, the FASB issued new accounting guidance addressing the accounting for multiple-deliverable arrangements to enable entities to account for products or services (deliverables) separately rather than as a combined unit. The provisions establish the accounting and reporting guidance for arrangements under which the entity will perform multiple revenue-generating activities. Specifically, this guidance addresses how to separate deliverables and how to measure and allocate arrangement consideration to one or more units of accounting. The Company adopted the new guidance on October 1, 2010 and the adoption did not impact the Company's financial statements and related disclosures.

Fair Value Measurement

In May 2011, the FASB issued amended accounting guidance to improve comparability of fair value measures between GAAP and the International Financial Reporting Standards. The amended guidance clarifies how to apply the existing fair value measurement and disclosure requirements. The provisions will be effective for the Company's financial statements beginning with the Company's second quarter of fiscal 2012. The Company is in the process of evaluating the impact that the amended guidance may have on its financial statements and related disclosures.

Comprehensive Income

In June 2011, the FASB issued amended accounting guidance on the presentation of comprehensive income. The amended guidance requires that all non-owner changes in stockholders' equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The provisions will be effective for the Company's financial statements for the fiscal year beginning October 1, 2012. The Company is in the process of evaluating the impact that the amended guidance may have on its financial statements and related disclosures.

NOTE 2. DISCONTINUED OPERATIONS

Global Pro

On February 28, 2011, the Company completed the sale of Global Pro to ICL for \$270 million, pursuant to the terms of the definitive share and business sale agreement (the "SBSA") between Scotts Miracle-Gro, The Scotts Company LLC ("Scotts"), a wholly-owned subsidiary of Scotts Miracle-Gro, and ICL. After agreed upon adjustments (including post-closing adjustments), the Company received \$270.9 million net proceeds. Results from discontinued operations for the first nine months of fiscal 2011 include an after-tax gain on the sale of Global Pro of \$21.2 million, which includes transaction costs.

The Company's decision to exit the professional ornamental horticulture, turf and specialty agriculture markets and sell Global Pro was another step in its strategy to evolve its business portfolio to better leverage growth opportunities within its core Global Consumer business segment. The Company applied a portion of the net proceeds of the sale toward debt retirement and intends to apply the remaining portion toward capital investments.

In conjunction with the transaction, Scotts and ICL entered into several product supply agreements which are generally up to five years in duration, as well as various trademark and technology licensing agreements with varying durations. The purpose of these agreements is to allow each party to continue leveraging existing production capabilities and intellectual property to meet customer demand for their respective products. Furthermore, certain transitional services are being provided by Scotts to ICL, the majority of which extend for a period of six to 12 months from the date of sale. Scotts estimates that it will supply ICL with approximately \$35 million of product, as well as purchase approximately \$15 million of materials from ICL, each on an annualized basis.

The Company's continuing cash inflows and outflows related to these agreements are not considered to be significant in relation to the overall cash flows of Global Pro. Furthermore, none of these agreements permit the Company to influence the operating or financial policies of Global Pro under the ownership of ICL. Therefore, Global Pro met the criteria for presentation as discontinued operations. As such, effective in the first quarter of fiscal 2011, the Company classified Global Pro as discontinued operations for all periods presented.

The Global Pro results from discontinued operations include an allocation of interest expense relating to the amount of our senior secured credit facilities that was required to be repaid from the sale proceeds. The amount of interest expense allocated to and included in discontinued operations was \$0.7 million for the three-month period ended July 3, 2010, and \$1.7 million and \$2.7 million for the nine-month periods ended July 2, 2011 and July 3, 2010, respectively.

Smith & Hawken Ltd.

In July 2009, Scotts Miracle-Gro announced that its wholly-owned subsidiary, Smith & Hawken, Ltd., had adopted a plan to close the Smith & Hawken⁺ business. During the Company's first quarter of fiscal 2010, all Smith & Hawken stores were closed and substantially all operational activities of Smith & Hawken were discontinued. As a result, effective in its first quarter of fiscal 2010, the Company classified Smith & Hawken as discontinued operations.

- + Smith & Hawken[®] is a registered trademark of Target Brands, Inc. The Company sold the Smith & Hawken brand and certain intellectual property rights related thereto on December 30, 2009, and subsequently changed the name of the subsidiary entity formerly known as Smith & Hawken, Ltd. to Teak 2, Ltd. References in this Quarterly Report on Form 10-Q to Smith & Hawken refer to Scotts Miracle-Gro's subsidiary entity, not the brand itself.

Table of Contents

In the first nine months of fiscal 2010, the Company incurred charges related to the liquidation of the Smith & Hawken business primarily associated with the termination of retail site lease obligations, third-party agency fees and severance and benefit commitments. These charges were partially offset by a gain of approximately \$18 million from the sale of the Smith & Hawken intellectual property on December 30, 2009.

The following table summarizes the results of Global Pro and Smith & Hawken as discontinued operations (in millions):

	September 30, THREE MONTHS ENDED		September 30, NINE MONTHS ENDED	
	JULY 2, 2011	JULY 3, 2010	JULY 2, 2011	JULY 3, 2010
Net sales	\$	\$ 66.3	\$ 88.7	\$ 203.3
Operating costs		56.2	78.1	190.9
Impairment, restructuring and other charges		0.4		19.3
Gain on sale of Global Pro business	(2.4)		(93.0)	
Global Pro sale related transaction costs	2.2		17.0	
Other income, net	(0.3)	(0.6)	(0.2)	(19.1)
Interest expense		0.7	1.7	2.7
Income from discontinued operations before income taxes	0.5	9.6	85.1	9.5
Income tax expense from discontinued operations	0.6	3.2	57.4	6.4
Income (loss) from discontinued operations	\$ (0.1)	\$ 6.4	\$ 27.7	\$ 3.1

The major classes of assets and liabilities of Global Pro were as follows (in millions):

	September 30, JULY 3, 2010	September 30, SEPTEMBER 30, 2010
Cash and cash equivalents	\$ 1.0	\$ 1.0
Accounts receivable, net	70.6	57.5
Inventories, net	55.7	50.7
Prepaid and other assets	2.4	3.4
Property, plant and equipment, net	13.2	13.5
Goodwill	63.1	67.0
Assets held for sale	\$ 206.0	\$ 193.1
Accounts payable	\$ 16.2	\$ 11.4
Other current liabilities	17.6	18.7
Other liabilities	10.6	15.2
Liabilities held for sale	\$ 44.4	\$ 45.3

The major classes of assets and liabilities of Smith & Hawken were as follows (in millions):

September 30, JULY 3, 2010	September 30, SEPTEMBER 30, 2010
----------------------------------	--

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

Assets of discontinued operations in other current assets	\$	5.2	\$	1.3
Accounts payable	\$	0.2	\$	
Other current liabilities		4.3		0.9
Liabilities of discontinued operations	\$	4.5	\$	0.9

NOTE 3. PRODUCT REGISTRATION AND RECALL MATTERS

In April 2008, the Company became aware that a former associate apparently deliberately circumvented the Company's policies and U.S. Environmental Protection Agency (U.S. EPA) regulations under the Federal Insecticide, Fungicide, and Rodenticide Act of 1947, as amended (FIFRA), by failing to obtain valid registrations for certain products and/or causing certain invalid product registration forms to be submitted to regulators. Since that time, the Company has been cooperating with both the U.S. EPA and the U.S. Department of Justice (the U.S. DOJ) in related civil and criminal investigations into the pesticide product registration issues as well as a state civil investigation into related allegations arising under state pesticide registration laws and regulations.

Table of Contents

In late April 2008, in connection with the U.S. EPA's investigation, the Company conducted a consumer-level recall of certain consumer lawn and garden products and a Scotts LawnService® product. Subsequently, the Company and the U.S. EPA agreed upon a Compliance Review Plan for conducting a comprehensive, independent review of the Company's product registration records. Pursuant to the Compliance Review Plan, an independent third-party firm, Quality Associates Incorporated (QAI), reviewed substantially all of the Company's U.S. pesticide product registrations and associated advertisements, some of which were historical in nature and no longer related to sales of the Company's products. The U.S. EPA investigation and the QAI review process resulted in the temporary suspension of sales and shipments of certain products. In addition, as the QAI review process or the Company's internal review identified potential FIFRA registration issues (some of which appear unrelated to the actions of the former associate), the Company endeavored to stop selling or distributing the affected products until the issues could be resolved. QAI's review of the Company's U.S. pesticide product registrations and associated advertisements is now substantially complete. The results of the QAI review process did not materially affect the Company's fiscal 2010 or year-to-date fiscal 2011 sales and are not expected to materially affect the Company's sales during the remainder of fiscal 2011.

Settlement discussions relating to potential fines and/or penalties are a frequent outgrowth of governmental investigations. In that regard, on or about June 30, 2011, the Company received a Notice of Intent to File Administrative Complaint (Notice) from the U.S. EPA Region 5 with respect to the alleged FIFRA violations. The Notice, which does not set forth a proposed penalty amount, offers the Company an opportunity to present any information that it believes the U.S. EPA should consider prior to filing the complaint and indicates that the U.S. EPA is prepared to meet with the Company to discuss the alleged violations. The Company made a timely response to the Notice and communications between the Company and the U.S. EPA are underway. In addition, the Company recently began settlement discussions with the U.S. DOJ regarding its criminal investigation.

Based on the facts and circumstances known to the Company at this time (including settlement discussions that have taken place to date), the Company has established what it believes to be an appropriate reserve. The U.S. EPA and U.S. DOJ investigations continue, however, and may result in future state, federal or private rights of action including fines and/or penalties with respect to known or potential additional product registration issues. Until these investigations are completed, the Company cannot reasonably estimate the total scope or magnitude of all possible liabilities. It is possible that any such fines and/or penalties, as well as any judgments, litigation costs or other liabilities relating to such known or potential product registration issues, could exceed the amount of the reserve, possibly materially, and could have an adverse effect on the Company's financial condition, results of operations or cash flows.

In June 2008, the California Department of Pesticide Regulation (CDPR) issued a request for information to the Company relating to products that had been the subject of the April 2008 recall. The Company cooperated with that inquiry and reached agreement with CDPR that CDPR would place its investigation on hold pending the completion of the Company's internal audit. In furtherance of that agreement, in May 2010, the Company and CDPR executed a tolling agreement that extended CDPR's rights through April 2012. In July 2010, CDPR notified the Company that CDPR planned to proceed with its investigation independent of the U.S. EPA and U.S. DOJ, and in March 2011, the Company received a letter from CDPR offering to settle the matter without the need for an enforcement proceeding for \$245,631. On July 25, 2011, the Company paid the requested civil penalty and entered into a Settlement Agreement pursuant to which CDPR agreed not to take further civil or criminal action with regard to the affected products.

As a result of these registration and recall matters, the Company has recorded charges for affected inventory and other registration and recall-related costs. The effects of these adjustments, including the reserve noted above, were pre-tax charges of \$6.8 million and \$1.5 million for the three-month periods, and \$11.0 million and \$5.8 million for the nine-month periods ended July 2, 2011 and July 3, 2010, respectively. The Company expects that future charges will include costs associated with the rework of certain finished goods inventories, the potential disposal of certain products and ongoing third-party professional services related to the U.S. EPA, U.S. DOJ and state investigations. It may also be appropriate to establish additional reserves as settlement discussions continue.

The following tables summarize the impact of the product registration and recall matters on the Company's results of operations during the three and nine months ended July 2, 2011 and July 3, 2010, and on accrued liabilities and inventory reserves as of July 2, 2011 (in millions):

	September 30, THREE MONTHS ENDED JULY 2, 2011	September 30, THREE MONTHS ENDED JULY 3, 2010	September 30, NINE MONTHS ENDED JULY 2, 2011	September 30, NINE MONTHS ENDED JULY 3, 2010
Cost of sales other charges	\$ 1.1	\$	\$ 3.2	\$ 1.5
Gross profit	(1.1)		(3.2)	(1.5)
Selling, general and administrative	5.7	1.5	7.8	4.3

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

Loss from operations	(6.8)	(1.5)	(11.0)	(5.8)
Income tax benefit	0.8	0.5	2.2	2.0
Net loss	\$ (6.0)	\$ (1.0)	\$ (8.8)	\$ (3.8)

Table of Contents

	September 30, RESERVES AT SEPTEMBER 30, 2010	September 30, ADDITIONAL COSTS AND CHANGES IN ESTIMATE	September 30, RESERVES USED	September 30, RESERVES AT JULY 2, 2011
Inventory reserves	\$ 3.0	\$ 1.6	\$ (0.6)	\$ 4.0
Other incremental costs of sales	0.5	1.6	(1.0)	1.1
Other general and administrative costs	0.5	7.8	(3.4)	4.9
Accrued liabilities and inventory reserves	\$ 4.0	\$ 11.0	\$ (5.0)	\$ 10.4

NOTE 4. IMPAIRMENT, RESTRUCTURING AND OTHER CHARGES

During the three month period ended July 2, 2011, the Company recorded \$13.8 million of impairment, restructuring and other charges relating to payments to the former owners of Turf-Seed, Inc. and severance related costs. On May 26, 2011, the Company and the former owners of Turf-Seed, Inc. agreed to an early settlement of the contingent consideration associated with Company's fiscal 2006 acquisition of Turf-Seed, Inc. Concurrently, several other contracts and agreements between the Company and the former owners of Turf-Seed, Inc. were terminated or amended. The Company agreed to pay a total of \$21.3 million to resolve these matters, resulting in a net charge of \$10.3 million after consideration of previously recorded liabilities and other aspects of the agreements.

On August 8, 2011, the Company announced a restructuring plan designed to streamline management decision making, continue the regionalization of the Company's operating structure and provide additional resources to invest in innovation and growth initiatives. During the three-month period ended July 2, 2011, the Company incurred \$3.5 million in restructuring costs. The Company anticipates incurring total restructuring charges of \$15-\$20 million in fiscal 2011, primarily related to severance activities, to complete this restructuring initiative.

NOTE 5. DETAIL OF INVENTORIES, NET

Inventories, net of reserves for slow moving and obsolete inventories of \$24.0 million, \$28.2 million and \$27.0 million as of July 2, 2011, July 3, 2010 and September 30, 2010, respectively, consisted of:

	September 30, JULY 2, 2011	September 30, JULY 3, 2010	September 30, SEPTEMBER 30, 2010
Finished goods	\$ 258.7	\$ 231.6	\$ 144.8
Work-in-process	27.7	21.8	27.2
Raw materials	155.8	152.5	180.9
	\$ 442.2	\$ 405.9	\$ 352.9

NOTE 6. MARKETING AGREEMENT

The Company is Monsanto's exclusive agent for the marketing and distribution of consumer Roundup® herbicide products (with additional rights to new products containing glyphosate or other similar non-selective herbicides) in the consumer lawn and garden market within the United States and other specified countries, including Australia, Austria, Belgium, Canada, France, Germany, the Netherlands and the United Kingdom. Under the terms of the Marketing Agreement, the Company is entitled to receive an annual commission from Monsanto as consideration for the performance of the Company's duties as agent. The annual gross commission under the Marketing Agreement is calculated as a percentage of the actual earnings before interest and income taxes (EBIT) of the consumer Roundup® business in the markets covered by the Marketing Agreement and is based on the achievement of two earnings thresholds, as defined in the Marketing Agreement. The Marketing Agreement also requires the Company to make annual payments to Monsanto as a contribution against the overall expenses of the consumer Roundup® business. The annual contribution payment is defined in the Marketing Agreement as \$20 million.

In consideration for the rights granted to the Company under the Marketing Agreement for North America, the Company was required to pay a marketing fee of \$32 million to Monsanto. The Company has deferred this amount on the basis that the payment will provide a future benefit

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

through commissions that will be earned under the Marketing Agreement. Based on management's current assessment of the likely term of the Marketing Agreement, the useful life over which the marketing fee is being amortized is 20 years.

* Roundup® is a registered trademark of Monsanto Technology LLC, a company affiliated with Monsanto Company (Monsanto).

Table of Contents

Under the terms of the Marketing Agreement, the Company performs certain functions, primarily manufacturing conversion, distribution and logistics, and selling and marketing support, on behalf of Monsanto in the conduct of the consumer Roundup® business. The actual costs incurred for these activities are charged to and reimbursed by Monsanto. The Company records costs incurred under the Marketing Agreement for which the Company is the primary obligor on a gross basis, recognizing such costs in Cost of sales and the reimbursement of these costs in Net sales, with no effect on gross profit or net income. The related net sales and cost of sales were \$17.7 million and \$18.9 million for the three-month periods, and \$51.8 million and \$54.0 million for the nine-month periods ended July 2, 2011 and July 3, 2010, respectively.

The elements of the net commission earned under the Marketing Agreement and included in Net sales are as follows (in millions):

	September 30, THREE MONTHS ENDED		September 30, NINE MONTHS ENDED	
	JULY 2, 2011	JULY 3, 2010	JULY 2, 2011	JULY 3, 2010
Gross commission	\$ 32.9	\$ 46.7	\$ 65.9	\$ 76.6
Contribution expenses	(5.0)	(5.0)	(15.0)	(15.0)
Amortization of marketing fee	(0.2)	(0.2)	(0.6)	(0.6)
Net commission income	27.7	41.5	50.3	61.0
Reimbursements associated with Marketing Agreement	17.7	18.9	51.8	54.0
Total net sales associated with Marketing Agreement	\$ 45.4	\$ 60.4	\$ 102.1	\$ 115.0

The Marketing Agreement has no definite term except as it relates to the European Union countries (the EU term). The EU term extends through September 30, 2011, with up to two additional automatic renewal periods of two years each, subject to non-renewal only upon the occurrence of certain performance defaults. Thereafter, the Marketing Agreement provides that the parties may agree to renew the EU term for an additional three years.

The Marketing Agreement provides Monsanto with the right to terminate the Marketing Agreement upon an event of default (as defined in the Marketing Agreement) by the Company, a change in control of Monsanto or the sale of the consumer Roundup® business. The Marketing Agreement provides the Company with the right to terminate the Marketing Agreement in certain circumstances, including an event of default by Monsanto or the sale of the consumer Roundup® business. Unless Monsanto terminates the Marketing Agreement due to an event of default by the Company, Monsanto is required to pay a termination fee to the Company that varies by program year. The termination fee is calculated as a percentage of the value of the Roundup® business exceeding a certain threshold, but in no event will the termination fee be less than \$16 million. If Monsanto were to terminate the Marketing Agreement due to an event of default by the Company, however, the Company would not be entitled to any termination fee, and the Company would lose all, or a substantial portion, of the significant source of earnings and overhead expense absorption the Marketing Agreement provides. Monsanto may also be able to terminate the Marketing Agreement within a given region, including North America, without paying a termination fee if unit volume sales to consumers in that region decline: (1) over a cumulative three-fiscal-year period; or (2) by more than 5% for each of two consecutive years.

Under the Marketing Agreement, Monsanto must provide the Company with notice of any proposed sale of the consumer Roundup® business, allow the Company to participate in the sale process and negotiate in good faith with the Company with respect to any such proposed sale. In the event the Company acquires the consumer Roundup® business in such a sale, the Company would receive as a credit against the purchase price the amount of the termination fee that would have been paid to the Company if Monsanto had exercised its right to terminate the Marketing Agreement in connection with a sale to another party. If Monsanto decides to sell the consumer Roundup® business to another party, the Company must let Monsanto know whether the Company intends to terminate the Marketing Agreement and forfeit any right to a termination fee or whether it will agree to continue to perform under the Marketing Agreement on behalf of the purchaser.

NOTE 7. DEBT

The components of long-term debt are as follows (in millions):

September 30, September 30, September 30,

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

	JULY 2, 2011	JULY 3, 2010	SEPTEMBER 30, 2010
Credit Facilities:			
Revolving loans	\$ 377.0	\$ 108.8	\$ 111.7
Term loans		344.4	302.4
Senior Notes 7.25%	200.0	200.0	200.0
Senior Notes 6.625%	200.0		
Master Accounts Receivable Purchase Agreement		15.0	
Contingent consideration (see note 4)		11.3	10.9
Other	7.2	10.7	6.7
	784.2	690.2	631.7
Less current portions	2.1	200.0	195.0
	\$ 782.1	\$ 490.2	\$ 436.7

Table of Contents

On June 30, 2011, Scotts Miracle-Gro and certain of its subsidiaries entered into a second amended and restated senior secured credit facility, providing for revolving loans in the aggregate principal amount of up to \$1.7 billion over a five-year term. Borrowings may be made in various currencies including U.S. dollars, Euros, British pounds, Australian dollars and Canadian dollars. Under this amended and restated facility, the Company may request up to an additional \$450 million in revolving and/or term commitments, subject to certain specified conditions, including approval from the Company's lenders. The amended and restated facility replaces the Company's previous senior secured credit facilities, which were comprised of: (a) a senior secured revolving loan facility in the aggregate principal of up to \$1.59 billion and (b) a senior secured term loan facility totaling \$560 million. The previous senior secured credit facilities were scheduled to expire in February 2012.

As of July 2, 2011, there was \$1.3 billion of availability under the Company's credit facility, including letters of credit. Under the facility, the Company has the ability to issue letter of credit commitments up to \$75 million. At July 2, 2011, the Company had letters of credit in the aggregate face amount of \$26.3 million outstanding.

On January 14, 2010, Scotts Miracle-Gro issued \$200 million aggregate principal amount of 7.25% Senior Notes due 2018 (the 7.25% Senior Notes). The net proceeds of the offering were used to reduce outstanding borrowings under the Company's then existing senior secured credit facilities. The 7.25% Senior Notes represent general unsecured senior obligations of Scotts Miracle-Gro, and were sold to the public at 99.254% of the principal amount thereof, to yield 7.375% to maturity. The 7.25% Senior Notes have interest payment dates of January 15 and July 15 of each year, which began on July 15, 2010, and may be redeemed prior to maturity at applicable redemption premiums. The 7.25% Senior Notes contain usual and customary incurrence-based covenants, which include, but are not limited to, restrictions on the incurrence of additional indebtedness, the incurrence of liens and the issuance of certain preferred shares, and the making of certain distributions, investments and other restricted payments, as well as other usual and customary covenants, which include, but are not limited to, restrictions on sale and leaseback transactions, restrictions on purchases or redemptions of Scotts Miracle-Gro stock and prepayments of subordinated debt, limitations on asset sales and restrictions on transactions with affiliates. The 7.25% Senior Notes mature on January 15, 2018.

On December 16, 2010, Scotts Miracle-Gro issued \$200 million aggregate principal amount of 6.625% Senior Notes due 2020 (the 6.625% Senior Notes) in a private placement exempt from the registration requirements under the Securities Act of 1933, as amended. The net proceeds of the offering were used to repay outstanding borrowings under the Company's then existing senior secured credit facilities and for general corporate purposes. The 6.625% Senior Notes represent general unsecured senior obligations of Scotts Miracle-Gro and rank equal in right of payment with the Company's existing and future unsecured senior debt, including, without limitation, the 7.25% Senior Notes. The 6.625% Senior Notes have interest payment dates of June 15 and December 15 of each year, commencing June 15, 2011, and may be redeemed prior to maturity at applicable redemption premiums. The 6.625% Senior Notes contain usual and customary incurrence-based covenants, as well as other usual and customary covenants, substantially similar to those contained in the 7.25% Senior Notes. The 6.625% Senior Notes mature on December 15, 2020.

Certain of Scotts Miracle-Gro's domestic subsidiaries serve as guarantors of both the 7.25% and the 6.625% Senior Notes. Refer to NOTE 16. FINANCIAL INFORMATION FOR SUBSIDIARY GUARANTORS AND NON-GUARANTORS for more information regarding the guarantor entities.

The Company was in compliance with the terms of all borrowing agreements at July 2, 2011.

At July 2, 2011, the Company had outstanding interest rate swap agreements with major financial institutions that effectively convert a portion of variable-rate debt denominated in U.S. dollars to a fixed rate. The swap agreements had a total U.S. dollar notional amount of \$900 million at July 2, 2011. Interest payments made between the effective date and expiration date are hedged by the swap agreements, except as noted below. The notional amount, effective date, expiration date and rate of these swap agreements are shown in the table below.

NOTIONAL AMOUNT (IN MILLIONS)	September 30, EFFECTIVE DATE (a)	September 30, EXPIRATION DATE	September 30, FIXED RATE
\$ 200	2/14/2007	2/14/2012	5.20%
50	2/14/2012	2/14/2016	3.78%
150 ^(b)	11/16/2009	5/16/2016	3.26%
50 ^(c)	2/16/2010	5/16/2016	3.05%
150 ^(b)	12/20/2011	6/20/2016	2.61%
150 ^(c)	2/7/2012	5/7/2016	2.42%

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

100 ^(c)	2/21/2012	5/23/2016	2.40%
50 ^(d)	12/6/2012	9/6/2017	2.96%

Table of Contents

- (a) The effective date refers to the date on which interest payments are first hedged by the applicable swap agreement.
- (b) Interest payments made during the six-month period of each year that begins with the month and day of the effective date are hedged by the swap agreement.
- (c) Interest payments made during the three-month period of each year that begins with the month and day of the effective date are hedged by the swap agreement.
- (d) Interest payments made during the nine-month period of each year that begins with the month and day of the effective date are hedged by the swap agreement.

Master Accounts Receivable Purchase Agreement

On May 1, 2009, the Company entered into a Master Accounts Receivable Purchase Agreement (the 2009 MARP Agreement), with an initial stated termination date of May 1, 2010, or such later date as may be mutually agreed by the Company and its lender. The 2009 MARP Agreement provided for the discounted sale, on an uncommitted, revolving basis, of accounts receivable generated by a specified account debtor, with aggregate limits not to exceed \$80 million. The 2009 MARP Agreement provided an interest rate that approximated the 7-day LIBOR rate plus 225 basis points.

On May 13, 2010, the Company and its lender entered into a First Amendment to the 2009 MARP Agreement (the First Amendment). The First Amendment, which was effective May 1, 2010, extended the stated termination date of the 2009 MARP Agreement through May 12, 2011, or such later date as may be mutually agreed by the Company and its lender. On May 10, 2011, the Company and its lender entered into a Second Amendment to the 2009 MARP Agreement which further extended the stated termination date through September 30, 2011, or such later date as may be mutually agreed by the Company and its lender.

The 2009 MARP Agreement, as amended by the First Amendment, provides an interest rate that approximates the 7-day LIBOR rate plus 125 basis points; the amendments did not otherwise modify any substantive provisions of the 2009 MARP Agreement.

The Company accounts for the sale of receivables under the 2009 MARP Agreement, as amended, as short-term debt and continues to carry the receivables on its Condensed, Consolidated Balance Sheet, primarily as a result of the Company's right to repurchase receivables sold. The caption Accounts receivable pledged on the accompanying Condensed, Consolidated Balance Sheets in the amount of \$23.3 million as of July 3, 2010 represents the pool of receivables that were designated as sold under the 2009 MARP Agreement, as amended, and served as collateral for short-term debt thereunder in the amount of \$15.0 million as of July 3, 2010. There were no short-term borrowings under the amended 2009 MARP Agreement as of July 2, 2011 and September 30, 2010.

Estimated Fair Values

A description of the methods and assumptions used to estimate the fair values of the Company's debt instruments is as follows:

Credit Facilities

The interest rate currently available to the Company fluctuates with the applicable LIBOR rate, prime rate or Federal Funds Effective Rate, and thus the carrying value is a reasonable estimate of fair value.

7.25% Senior Notes

The fair value of the 7.25% Senior Notes can be determined based on the trading of the 7.25% Senior Notes in the open market. The difference between the carrying value and the fair value of the 7.25% Senior Notes represents the premium or discount on that date. Based on the trading value on or around July 2, 2011, the fair value of the 7.25% Senior Notes was approximately \$218.0 million.

6.625% Senior Notes

Table of Contents

The fair value of the 6.625% Senior Notes can be determined based on the trading of the 6.625% Senior Notes. The difference between the carrying value and the fair value of the 6.625% Senior Notes represents the premium or discount on that date. Based on the trading value on or around July 2, 2011, the fair value of the 6.625% Senior Notes was approximately \$204.0 million.

Accounts Receivable Pledged

The interest rate on the short-term debt associated with accounts receivable pledged under the 2009 MARP Agreement fluctuates with the one-week LIBOR rate, and thus the carrying value is a reasonable estimate of fair value.

NOTE 8. COMPREHENSIVE INCOME

The components of other comprehensive income (expense) and total comprehensive income were as follows (in millions):

	September 30, THREE MONTHS ENDED		September 30, NINE MONTHS ENDED	
	JULY 2, 2011	JULY 3, 2010	JULY 2, 2011	JULY 3, 2010
Net income	\$ 111.6	\$ 175.9	\$ 221.3	\$ 236.7
Other comprehensive income (expense):				
Change in valuation of derivative instruments	(3.5)	(3.8)	4.6	5.1
Pension and other postretirement related items	1.0	(3.9)	7.9	1.4
Foreign currency translation adjustments	(3.2)	(5.3)	(12.5)	(0.4)
Comprehensive income	\$ 105.9	\$ 162.9	\$ 221.3	\$ 242.8

NOTE 9. RETIREMENT AND RETIREE MEDICAL PLANS COST INFORMATION

The following summarizes the net periodic benefit cost from continuing operations for the various retirement and retiree medical plans sponsored by the Company (in millions):

	September 30, JULY 2, 2011		September 30, THREE MONTHS ENDED		September 30, JULY 3, 2010	
	U.S. Pension	International Pension	U.S. Medical	U.S. Pension	International Pension	U.S. Medical
Components of net periodic benefit cost						
Service cost	\$	\$ 0.4	\$ 0.1	\$	\$ 0.5	\$ 0.1
Interest cost	1.2	2.6	0.4	1.3	2.2	0.4
Expected return on plan assets	(1.3)	(2.4)		(1.2)	(1.9)	
Net amortization	1.2	0.3		1.1	0.5	
Net periodic benefit cost	\$ 1.1	\$ 0.9	\$ 0.5	\$ 1.2	\$ 1.3	\$ 0.5

	September 30, JULY 2, 2011	September 30, NINE MONTHS ENDED	September 30, JULY 3, 2010
--	-------------------------------	------------------------------------	-------------------------------

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

	U.S. Pension	International Pension	U.S. Medical	U.S. Pension	International Pension	U.S. Medical
Components of net periodic benefit cost						
Service cost	\$	\$	\$	\$	\$	\$
Interest cost	3.6	8.0	1.2	3.9	6.8	1.2
Expected return on plan assets	(3.9)	(7.6)		(3.8)	(5.9)	
Net amortization	3.7	1.1		3.3	1.5	
Net periodic benefit cost	\$ 3.4	\$ 2.7	\$ 1.5	\$ 3.4	\$ 3.9	\$ 1.6

NOTE 10. SHARE-BASED COMPENSATION AWARDS

Share-Based Awards

The following is a summary of the share-based compensation awards granted during the periods indicated:

	September 30, NINE MONTHS ENDED JULY 2, 2011	September 30, NINE MONTHS ENDED JULY 3, 2010
Options	429,700	367,600
Restricted stock units (including deferred stock units)	95,570	287,508
Performance shares		4,200
Performance units	53,874	
Total share-based awards	579,144	659,308
Aggregate fair value at grant dates (in millions)	\$ 13.8	\$ 16.9

Table of Contents

Total share-based compensation recognized was as follows for the periods indicated (in millions):

	September 30, THREE MONTHS ENDED JULY 2, 2011	September 30, THREE MONTHS ENDED JULY 3, 2010	September 30, NINE MONTHS ENDED JULY 2, 2011	September 30, NINE MONTHS ENDED JULY 3, 2010
Share-based compensation	\$ 3.4	\$ 4.3	\$ 14.3	\$ 12.5

NOTE 11. INCOME TAXES

The effective tax rate related to continuing operations for the nine months ended July 2, 2011 was 36.5%, compared to 37.3% for the nine months ended July 3, 2010. The effective tax rate used for interim reporting purposes is based on management's best estimate of factors impacting the effective tax rate for the full fiscal year. An allocation of the income tax expense has been separately determined to report the discontinued operations net of tax. There can be no assurance that the effective tax rate estimated for interim financial reporting purposes will approximate the effective tax rate determined at fiscal year end.

Scotts Miracle-Gro or one or more of its subsidiaries files income tax returns in the U.S. federal jurisdiction and various state, local and foreign jurisdictions. With few exceptions, the Company is no longer subject to examinations by these tax authorities for fiscal years prior to 2008. The Company is currently under examination by the Internal Revenue Service (the IRS) and certain foreign and U.S. state and local tax authorities. The IRS is reviewing the fiscal 2008 tax period only. In regards to a local German audit, the tax periods under investigation are limited to fiscal years 2004 through 2008. In regards to U.S. state and local audits, the tax periods under investigation are limited to fiscal years 1997 through 2008. In addition to these audits, certain other tax deficiency notices and refund claims for previous years remain unresolved.

The Company anticipates that few of its open and active audits will be resolved within the next 12 months. The Company is unable to make a reasonably reliable estimate as to when or if cash settlements with taxing authorities may occur. Although audit outcomes and the timing of audit payments are subject to significant uncertainty, the Company does not anticipate that the resolution of these tax matters or any events related thereto will result in a material change to its consolidated financial position, results of operations or cash flows.

NOTE 12. CONTINGENCIES

Management regularly evaluates the Company's contingencies, including various lawsuits and claims which arise in the normal course of business, product and general liabilities, workers' compensation, property losses and other fiduciary liabilities for which the Company is self-insured or retains a high exposure limit. Self-insurance reserves are established based on actuarial loss estimates for specific individual claims plus actuarially estimated amounts for incurred but not reported claims and adverse development factors applied to existing claims. Legal costs incurred in connection with the resolution of claims, lawsuits and other contingencies are expensed as incurred. In the opinion of management, its assessment of contingencies is reasonable and related reserves, in the aggregate, are adequate; however, there can be no assurance that final resolution of these matters will not have a material adverse effect on the Company's financial condition, results of operations or cash flows. The following are the more significant of the Company's identified contingencies:

FIFRA Compliance and the Corresponding Governmental Investigations

For a description of the Company's ongoing FIFRA compliance efforts and the corresponding governmental investigations, see NOTE 3. PRODUCT REGISTRATION AND RECALL MATTERS.

Other Regulatory Matters

At July 2, 2011, \$2.7 million was accrued for other regulatory matters in the Other liabilities line in the Condensed, Consolidated Balance Sheet. The amounts accrued are believed to be adequate to cover such known regulatory exposures based on current facts and estimates of likely outcomes. However, if facts and circumstances change significantly, they could result in a material adverse effect on the Company's financial condition, results of operations or cash flows.

Table of Contents**Other**

The Company has been named as a defendant in a number of cases alleging injuries that the lawsuits claim resulted from exposure to asbestos-containing products, apparently based on the Company's historic use of vermiculite in certain of its products. The complaints in these cases are not specific about the plaintiffs' contacts with the Company or its products. The Company in each case is one of numerous defendants and none of the claims seek damages from the Company alone. The Company believes that the claims against it are without merit and is vigorously defending against them. It is not currently possible to reasonably estimate a probable loss, if any, associated with these cases and, accordingly, no accrual or reserves have been recorded in the Company's condensed, consolidated financial statements. The Company is reviewing agreements and policies that may provide insurance coverage or indemnity as to these claims and is pursuing coverage under some of these agreements and policies, although there can be no assurance of the results of these efforts. There can be no assurance that these cases, whether as a result of adverse outcomes or as a result of significant defense costs, will not have a material adverse effect on the Company's financial condition, results of operations or cash flows.

The Company is involved in other lawsuits and claims which arise in the normal course of business. These claims individually and in the aggregate are not expected to result in a material adverse effect on the Company's financial condition, results of operations or cash flows.

NOTE 13. DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES**Derivatives and Hedging**

The Company is exposed to market risks, such as changes in interest rates, currency exchange rates and commodity prices. To manage a portion of the volatility related to these exposures, the Company enters into various financial transactions. The utilization of these financial transactions is governed by policies covering acceptable counterparty exposure, instrument types and other hedging practices. The Company does not hold or issue derivative financial instruments for speculative trading purposes.

The Company formally designates and documents qualifying instruments as hedges of underlying exposures at inception. The Company formally assesses, both at inception and at least quarterly, whether the financial instruments used in hedging transactions are effective at offsetting changes in cash flows of the related underlying exposure. Fluctuations in the value of these instruments generally are offset by changes in the cash flows of the underlying exposures being hedged. This offset is driven by the high degree of effectiveness between the exposure being hedged and the hedging instrument. GAAP requires all derivative instruments to be recognized as either assets or liabilities at fair value in the Condensed, Consolidated Balance Sheets. The Company designates commodity hedges as cash flow hedges of forecasted purchases of commodities and interest rate swap agreements as cash flow hedges of interest payments on variable rate borrowings. Any ineffective portion of a change in the fair value of a qualifying instrument is immediately recognized in earnings. The amounts recorded in earnings related to ineffectiveness of derivative hedges for the three- and nine-month periods ended July 2, 2011 and July 3, 2010 were not significant.

Foreign Currency Swap Contracts

The Company periodically uses foreign currency swap contracts to manage the exchange rate risk associated with intercompany loans with foreign subsidiaries that are denominated in local currencies. At July 2, 2011 and July 3, 2010, the notional amount of outstanding foreign currency swap contracts was \$382.4 million and \$211.4 million, respectively, with a fair value of \$0.8 million and a negative fair value of \$5.6 million, respectively. The fair value of foreign currency swap contracts is determined based on changes in spot rates. The unrealized loss on the foreign currency swap contracts approximates the unrealized gain on the intercompany loans recognized by the Company's lending subsidiaries.

Interest Rate Swap Agreements

The Company enters into interest rate swap agreements as a means to hedge its variable interest rate exposure on debt instruments. The fair values are reflected in the Company's Condensed, Consolidated Balance Sheets. Net amounts to be received or paid under the swap agreements are reflected as adjustments to interest expense. Since the interest rate swap agreements have been designated as hedging instruments, unrealized gains or losses resulting from adjusting these swaps to fair value are recorded as elements of accumulated other comprehensive loss (AOCI) within the Condensed, Consolidated Balance Sheets. The fair value of the swap agreements is determined based on the present value of the estimated future net cash flows using implied rates in the applicable yield curve as of the valuation date.

At July 2, 2011 and July 3, 2010, the Company had outstanding interest rate swap agreements with major financial institutions that effectively converted a portion of the Company's variable-rate debt to a fixed rate. The swap agreements had a total U.S. dollar equivalent notional amount of \$900 million and \$450 million at July 2, 2011 and July 3, 2010, respectively. Refer to NOTE 7. DEBT for the terms of the swap agreements

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

outstanding at July 2, 2011. Included in the AOCI balance at July 2, 2011 was a pre-tax loss of \$11.7 million related to interest rate swap agreements that is expected to be reclassified to earnings during the next 12 months, consistent with the timing of the underlying hedged transactions.

Table of Contents**Commodity Hedges**

The Company had outstanding hedging arrangements at July 2, 2011 designed to fix the price of a portion of its projected future urea requirements. The contracts are designated as hedges of the Company's exposure to future cash flow fluctuations associated with the cost of urea. The objective of the hedges is to mitigate the earnings and cash flow volatility attributable to the risk of changing prices. Unrealized gains or losses in the fair value of these contracts are recorded to the AOCI component of shareholders' equity. Realized gains or losses remain as a component of AOCI until the related inventory is sold. Upon sale of the underlying inventory, the gain or loss is reclassified to cost of sales. Included in the AOCI balance at July 2, 2011 was a pre-tax gain of \$1.4 million related to urea derivatives that is expected to be reclassified to earnings during the next 12 months, consistent with the timing of the underlying hedged transactions.

The Company enters into fuel derivatives for its Scotts LawnService® business that qualify for hedge accounting treatment. Unrealized gains or losses in the fair value of these contracts are recorded in other comprehensive income (expense), except for any ineffective portion of the change in fair value, which is immediately recorded in earnings. For the effective portion of the change in fair value, realized gains or losses remain as a component of AOCI until the related fuel is consumed by the Scotts LawnService® service vehicles. Upon consumption of the fuel, the gain or loss is reclassified to cost of sales. Included in the AOCI balance at July 2, 2011 was a pre-tax gain of \$0.1 million related to fuel derivatives that is expected to be reclassified to earnings during the next 12 months, consistent with the timing of the underlying hedged transactions.

Periodically, the Company also uses fuel derivatives to partially mitigate the effect of fluctuating diesel and gasoline costs on operating results. Fuel derivatives used by the Company that do not qualify for hedge accounting treatment in accordance with GAAP are recorded at fair value, with unrealized gains and losses on open contracts and realized gains or losses on settled contracts recorded as an element of cost of sales.

As of July 2, 2011, the Company had the following outstanding commodity contracts that were entered into to hedge forecasted purchases:

Commodity	September 30, Volume
Urea	7,500 tons
Diesel	1,344,000 gallons

Fair Values of Derivative Instruments

The fair values of the Company's derivative instruments were as follows (in millions):

	BALANCE SHEET LOCATION	ASSETS / (LIABILITIES)		
		JULY 2, 2011	JULY 3, 2010	SEPTEMBER 30, 2010
DERIVATIVES DESIGNATED AS HEDGING INSTRUMENTS			FAIR VALUE	
Interest rate swap agreements	Other assets	\$ 0.8	\$	\$
	Other current liabilities	(13.0)		(12.1)
	Other liabilities	(4.6)	(20.8)	(12.5)
Commodity hedging instruments	Prepaid and other assets	0.6		1.9
	Other current liabilities		(0.2)	
Total derivatives designated as hedging instruments		\$ (16.2)	\$ (21.0)	\$ (22.7)
<u>DERIVATIVES NOT DESIGNATED AS HEDGING INSTRUMENTS ⁽¹⁾</u>				
Foreign currency swap contracts	Prepaid and other assets	\$ 3.1	\$	\$
	Other current liabilities	(2.3)	(5.6)	(6.6)
Commodity hedging instruments		0.3		

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

Prepaid and other
assets

Other current liabilities (0.5)

Total derivatives not designated as hedging instruments ⁽¹⁾	\$ 1.1	\$ (6.1)	\$ (6.6)
Total derivatives	\$ (15.1)	\$ (27.1)	\$ (29.3)

Table of Contents

(1) See discussion above for additional information regarding the Company's purpose for entering into derivatives not designated as hedging instruments and its overall risk management strategy.

Refer to NOTE 14. FAIR VALUE MEASUREMENTS for the Company's fair value measurements of derivative instruments as they relate to the valuation hierarchy.

The effect of derivative instruments on AOCI and the Condensed, Consolidated Statements of Operations for the three- and nine-month periods ended July 2, 2011 and July 3, 2010 was as follows:

	September 30,			
	AMOUNT OF GAIN / (LOSS) RECOGNIZED IN AOCI			
	(IN MILLIONS)			
	THREE MONTHS ENDED		NINE MONTHS ENDED	
	JULY 2, 2011	JULY 3, 2010	JULY 2, 2011	JULY 3, 2010
DERIVATIVES IN CASH FLOW HEDGING RELATIONSHIPS				
Interest rate swap agreements	\$ (6.4)	\$ (6.2)	\$ (5.1)	\$ (12.8)
Commodity hedging instruments	0.3	(0.6)	1.7	1.5
Total	\$ (6.1)	\$ (6.8)	\$ (3.4)	\$ (11.3)

	September 30, LOCATION OF GAIN / (LOSS) RECLASSIFIED FROM AOCI INTO EARNINGS	September 30,			
		AMOUNT OF GAIN / (LOSS) RECLASSIFIED FROM AOCI INTO EARNINGS (IN MILLIONS)			
		THREE MONTHS ENDED		NINE MONTHS ENDED	
		JULY 2, 2011	JULY 3, 2010	JULY 2, 2011	JULY 3, 2010
DERIVATIVES IN CASH FLOW HEDGING RELATIONSHIPS					
Interest rate swap agreements	Interest expense	\$ (3.3)	\$ (3.2)	\$ (10.1)	\$ (14.7)
Commodity hedging instruments	Cost of sales	0.7	0.3	2.1	(2.5)
Total		\$ (2.6)	\$ (2.9)	\$ (8.0)	\$ (17.2)

	September 30, LOCATION OF GAIN / (LOSS) RECOGNIZED IN EARNINGS	September 30,			
		AMOUNT OF GAIN / (LOSS) RECOGNIZED IN EARNINGS (IN MILLIONS)			
		THREE MONTHS ENDED		NINE MONTHS ENDED	
		JULY 2, 2011	JULY 3, 2010	JULY 2, 2011	JULY 3, 2010
DERIVATIVES NOT DESIGNATED AS HEDGING INSTRUMENTS					
Foreign currency swap contracts	Interest expense	\$ 0.3	\$ (5.6)	\$ 5.9	\$ (4.9)
Commodity hedging instruments	Cost of sales	(0.3)	(0.8)	2.0	(0.9)
Total		\$ (6.4)	\$ 7.9	\$ (5.8)	

NOTE 14. FAIR VALUE MEASUREMENTS

GAAP defines fair value, establishes a framework for measuring fair value, and prescribes disclosures about fair value measurements. It defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or the most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. GAAP establishes a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. The hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair value are as follows:

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. This includes pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

The following describes the valuation methodologies used for financial assets and liabilities measured at fair value on a recurring basis, as well as the general classification within the valuation hierarchy.

Table of Contents**Derivatives**

Derivatives consist of foreign currency, interest rate and commodity derivative instruments. For further information on the Company's derivative instruments, refer to NOTE 13. DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES.

Other

Other financial assets consist of investment securities in non-qualified retirement plan assets. These securities are valued using observable market prices in active markets.

The following table presents the Company's financial assets and liabilities measured at fair value on a recurring basis at July 2, 2011 (in millions):

	September 30, Quoted Prices in Active Markets for Identical Assets (Level 1)	September 30, Significant Other Observable Inputs (Level 2)	September 30, Unobservable Inputs (Level 3)	September 30, Total
Assets				
Derivatives				
Interest rate swap agreements	\$	\$ 0.8	\$	\$ 0.8
Foreign currency swap contracts		3.1		3.1
Commodity hedging instruments		0.9		0.9
Other	7.5			7.5
Total	\$ 7.5	\$ 4.8	\$	\$ 12.3
Liabilities				
Derivatives				
Interest rate swap agreements	\$	\$ (17.6)	\$	\$ (17.6)
Foreign currency swap contracts		(2.3)		(2.3)
Total	\$	\$ (19.9)	\$	\$ (19.9)

The following table presents the Company's financial assets and liabilities measured at fair value on a recurring basis at July 3, 2010 (in millions):

	September 30, Quoted Prices in Active Markets for Identical Assets (Level 1)	September 30, Significant Other Observable Inputs (Level 2)	September 30, Unobservable Inputs (Level 3)	September 30, Total
Assets				
Other	\$ 5.9	\$	\$	\$ 5.9
Total	\$ 5.9	\$	\$	\$ 5.9
Liabilities				
Derivatives				

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

Interest rate swap agreements	\$	\$	(20.8)	\$	\$	(20.8)
Foreign currency swap contracts			(5.6)			(5.6)
Commodity hedging instruments			(0.7)			(0.7)
Total	\$	\$	(27.1)	\$	\$	(27.1)

The following table presents the Company's financial assets and liabilities measured at fair value on a recurring basis at September 30, 2010 (in millions):

Table of Contents

	September 30, Quoted Prices in Active Markets for Identical Assets (Level 1)	September 30, Significant Other Observable Inputs (Level 2)	September 30, Unobservable Inputs (Level 3)	September 30, Total
Assets				
Derivatives				
Commodity hedging instruments	\$	\$ 1.9	\$	\$ 1.9
Other	6.5			6.5
Total	\$ 6.5	\$ 1.9	\$	\$ 8.4
Liabilities				
Derivatives				
Interest rate swap agreements	\$	\$ (24.6)	\$	\$ (24.6)
Foreign currency swap contracts		(6.6)		(6.6)
Total	\$	\$ (31.2)	\$	\$ (31.2)

NOTE 15. SEGMENT INFORMATION

The Company divides its business into the following segments: Global Consumer and Scotts LawnService®. This division of reportable segments is consistent with how the segments report to and are managed by senior management of the Company. Reclassifications have been made to prior period segment amounts to reflect changes in the allocation of certain shared expenses among the segments, which in management's judgment better align those expenses with the associated drivers and benefits. Furthermore, the Company's reportable segments have been revised to reflect the sale of a significant majority of its previously reported Global Professional business segment, which is now reported in discontinued operations. For additional information regarding the sale, refer to NOTE 2. DISCONTINUED OPERATIONS.

The Global Consumer segment consists of the U.S. Consumer and International Consumer business groups. The business groups comprising this segment manufacture, market and sell dry, granular slow-release lawn fertilizers, combination lawn fertilizer and control products, grass seed, spreaders, water-soluble, liquid and continuous release garden and indoor plant foods, plant care products, potting, garden and lawn soils, mulches and other growing media products, wild bird food, pesticide and rodenticide products. Products are marketed to mass merchandisers, home centers, large hardware chains, warehouse clubs, distributors, garden centers and grocers in the United States, Canada, Europe, Latin America and Australia.

The Scotts LawnService® segment provides lawn fertilization, disease and insect control and other related services such as core aeration, tree and shrub fertilization and limited pest control services primarily to residential consumers through Company-owned branches and franchises in the United States.

Segment performance is evaluated based on several factors, including income from continuing operations before amortization, product registration and recall costs, and impairment, restructuring and other charges, which is not a GAAP measure. Senior management of the Company uses this measure of operating profit to gauge segment performance because the Company believes this measure is the most indicative of performance trends and the overall earnings potential of each segment.

Corporate & Other consists of the Company's non-European professional seed business and revenues and expenses associated with the Company's supply agreements with ICL, as well as corporate and administrative expenses.

The following tables present segment financial information (in millions):

	September 30,	September 30,	September 30,	September 30,
--	---------------	---------------	---------------	---------------

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

	THREE MONTHS ENDED		NINE MONTHS ENDED	
	JULY 2, 2011	JULY 3, 2010	JULY 2, 2011	JULY 3, 2010
Net sales:				
Global Consumer	\$ 951.6	\$ 1,085.9	\$ 2,225.2	\$ 2,314.6
Scotts LawnService®	82.4	81.3	152.2	144.9
Segment total	1,034.0	1,167.2	2,377.4	2,459.5
Corporate & Other	24.9	5.6	41.7	16.8
Roundup® amortization	(0.2)	(0.2)	(0.6)	(0.6)
Consolidated	\$ 1,058.7	\$ 1,172.6	\$ 2,418.5	\$ 2,475.7
Income from continuing operations before income taxes:				
Global Consumer	\$ 209.9	\$ 289.5	\$ 453.8	\$ 499.8
Scotts LawnService®	22.4	21.9	2.7	(0.7)
Segment total	232.3	311.4	456.5	499.1

Table of Contents

	September 30,	September 30,	September 30,	September 30,
Corporate & Other	(16.0)	(27.3)	(79.5)	(77.4)
Roundup® amortization	(0.2)	(0.2)	(0.6)	(0.6)
Other amortization	(3.1)	(2.3)	(8.1)	(7.5)
Product registration and recall matters	(6.8)	(1.5)	(11.0)	(5.8)
Impairment, restructuring and other charges	(13.8)		(13.8)	
Costs related to refinancing	(1.2)		(1.2)	
Interest expense	(14.0)	(11.2)	(37.3)	(35.0)
Consolidated	\$ 177.2	\$ 268.9	\$ 305.0	\$ 372.8

	September 30, JULY 2, 2011	September 30, JULY 3, 2010	September 30, SEPTEMBER 30, 2010
Total assets:			
Global Consumer	\$ 2,037.9	\$ 1,793.4	\$ 1,458.4
Scotts LawnService®	180.2	177.5	177.7
Corporate & Other	309.1	346.3	334.8
Assets held for sale		206.0	193.1
Consolidated	\$ 2,527.2	\$ 2,523.2	\$ 2,164.0

Total assets reported for the Company's operating segments include the intangible assets associated with the acquired businesses within those segments. Corporate & Other assets primarily include deferred financing and debt issuance costs, corporate intangible assets and deferred tax assets, and Smith & Hawken assets.

NOTE 16. FINANCIAL INFORMATION FOR SUBSIDIARY GUARANTORS AND NON-GUARANTORS

The 7.25% and 6.625% Senior Notes (collectively, the Senior Notes) issued by Scotts Miracle-Gro on January 14, 2010 and December 16, 2010, respectively, are guaranteed by certain of its domestic subsidiaries and, therefore, the Company has disclosed condensed, consolidating financial information in accordance with SEC Regulation S-X Rule 3-10, *Financial Statements of Guarantors and Issuers of Guaranteed Securities Registered or Being Registered*. The following 100% directly or indirectly owned subsidiaries fully and unconditionally guarantee the Senior Notes on a joint and several basis: EG Systems, Inc., dba Scotts LawnService®; Gutwein & Co., Inc.; Hyponex Corporation; Miracle-Gro Lawn Products, Inc.; OMS Investments, Inc.; Rod McLellan Company; Sanford Scientific, Inc.; Scotts Temecula Operations, LLC; Scotts Manufacturing Company; Scotts Products Co.; Scotts Professional Products Co.; Scotts-Sierra Investments, Inc.; SMG Growing Media, Inc.; Swiss Farms Products, Inc.; and The Scotts Company LLC (collectively, the Guarantors).

The following information presents condensed, consolidating Statements of Operations for the three- and nine-month periods ended July 2, 2011 and July 3, 2010, condensed, consolidating Statements of Cash Flows for the nine-month periods ended July 2, 2011 and July 3, 2010, and condensed, consolidating Balance Sheets as of July 2, 2011, July 3, 2010 and September 30, 2010. The condensed, consolidating financial information presents, in separate columns, financial information for: Scotts Miracle-Gro on a Parent-only basis, carrying its investment in subsidiaries under the equity method; Guarantors on a combined basis, carrying their investments in subsidiaries which do not guarantee the debt (collectively, the Non-Guarantors) under the equity method; Non-Guarantors on a combined basis; and eliminating entries. The eliminating entries primarily reflect intercompany transactions, such as interest expense, accounts receivable and payable, short and long-term debt, and the elimination of equity investments and income in subsidiaries. Because Scotts Miracle-Gro, as the Parent, is obligated to pay the unpaid principal amount and interest on all amounts borrowed by the Guarantors or Non-Guarantors under the senior secured five-year revolving loan facility, the borrowings and related interest expense for the revolving loans outstanding of the Guarantors and Non-Guarantors are also presented in the accompanying Parent-only financial information, and are then eliminated.

Table of Contents

The Scotts Miracle-Gro Company
Condensed, Consolidating Statement of Operations
for the three months ended July 2, 2011

(in millions)

	Parent	Subsidiary Guarantors	Non- Guarantors	Eliminations	Consolidated
Net sales	\$	\$ 852.9	\$ 205.8	\$	\$ 1,058.7
Cost of sales		528.8	128.7		657.5
Cost of sales product registration and recall matters		1.1			1.1
Gross profit		323.0	77.1		400.1
Operating expenses:					
Selling, general and administrative		134.4	58.0		192.4
Product registration and recall matters		5.7			5.7
Impairment, restructuring and other charges		13.8			13.8
Other income, net		(4.2)			(4.2)
Income from operations		173.3	19.1		192.4
Equity income in subsidiaries	(120.3)	(4.6)		124.9	
Other non-operating income	(5.4)			5.4	
Costs related to refinancing		1.2			1.2
Interest expense	13.1	5.3	1.0	(5.4)	14.0
Income from continuing operations before income taxes	111.4	172.6	18.1	(124.9)	177.2
Income tax (benefit) expense from continuing operations	(0.2)	59.1	6.6		65.5
Income from continuing operations	111.6	113.5	11.5	(124.9)	111.7
Income (loss) from discontinued operations, net of tax		6.7	(6.8)		(0.1)
Net income	\$ 111.6	\$ 120.2	\$ 4.7	\$ (124.9)	\$ 111.6

Table of Contents

The Scotts Miracle-Gro Company
Condensed, Consolidating Statement of Operations
for the nine months ended July 2, 2011

(in millions)

	Parent	Subsidiary Guarantors	Non- Guarantors	Eliminations	Consolidated
Net sales	\$	\$ 1,961.1	\$ 457.4	\$	\$ 2,418.5
Cost of sales		1,208.5	294.9		1,503.4
Cost of sales product registration and recall matters		3.2			3.2
Gross profit		749.4	162.5		911.9
Operating expenses:					
Selling, general and administrative		421.1	130.7		551.8
Product registration and recall matters		7.8			7.8
Impairment, restructuring and other charges		13.8			13.8
Other income, net		(3.9)	(1.1)		(5.0)
Income from operations		310.6	32.9		343.5
Equity income in subsidiaries	(242.5)	(5.2)		247.7	
Other non-operating income	(15.0)			15.0	
Costs related to refinancing	1.2				1.2
Interest expense	35.6	14.4	2.3	(15.0)	37.3
Income from continuing operations before income taxes	220.7	301.4	30.6	(247.7)	305.0
Income tax (benefit) expense from continuing operations	(0.6)	100.8	11.2		111.4
Income from continuing operations	221.3	200.6	19.4	(247.7)	193.6
Income (loss) from discontinued operations, net of tax		41.8	(14.1)		27.7
Net income	\$ 221.3	\$ 242.4	\$ 5.3	\$ (247.7)	\$ 221.3

Table of Contents

The Scotts Miracle-Gro Company
Condensed, Consolidating Statement of Cash Flows
for the nine months ended July 2, 2011

(in millions)

	Parent	Subsidiary Guarantors	Non- Guarantors	Eliminations	Consolidated
NET CASH (USED IN) PROVIDED BY OPERATING ACTIVITIES	\$ (16.0)	\$ 54.1	\$ (51.6)	\$	\$ (13.5)
INVESTING ACTIVITIES					
Proceeds from sale of long-lived assets		0.2			0.2
Proceeds from sale of business, net of transaction costs		159.0	94.9		253.9
Investments in property, plant and equipment		(49.7)	(3.6)		(53.3)
Payment of contingent consideration		(20.0)			(20.0)
Investments in acquired business, net of cash acquired		(0.8)			(0.8)
Net cash provided by investing activities		88.7	91.3		180.0
FINANCING ACTIVITIES					
Borrowings under revolving and bank lines of credit and term loans		860.5	558.7		1,419.2
Repayments under revolving and bank lines of credit and term loans	(302.4)	(494.6)	(662.2)		(1,459.2)
Proceeds from issuance of Senior Notes	200.0				200.0
Financing and issuance fees	(18.5)				(18.5)
Dividends paid	(49.4)				(49.4)
Purchase of treasury shares	(218.7)				(218.7)
Excess tax benefits from share-based payment arrangements		5.4			5.4
Cash received from exercise of stock options	29.4				29.4
Intercompany financing	375.6	(499.7)	124.1		
Net cash provided by (used in) financing activities	16.0	(128.4)	20.6		(91.8)
Effect of exchange rate changes on cash			1.5		1.5
Net increase in cash and cash equivalents		14.4	61.8		76.2
Cash and cash equivalents, beginning of period		5.0	83.1		88.1
Cash and cash equivalents, end of period	\$	\$ 19.4	\$ 144.9	\$	\$ 164.3

Table of Contents

The Scotts Miracle-Gro Company
Condensed, Consolidating Balance Sheet

As of July 2, 2011

(in millions)

	Parent	Subsidiary Guarantors	Non- Guarantors	Eliminations	Consolidated
ASSETS					
Current assets:					
Cash and cash equivalents	\$	\$ 19.4	\$ 144.9	\$	\$ 164.3
Accounts receivable, net		500.4	193.5		693.9
Inventories, net		362.8	79.4		442.2
Prepaid and other current assets		93.7	43.6		137.3
Total current assets		976.3	461.4		1,437.7
Property, plant and equipment, net		347.1	47.2		394.3
Goodwill		305.8	0.7		306.5
Intangible assets, net		288.6	54.6		343.2
Other assets	28.1	21.7	43.3	(47.6)	45.5
Equity investment in subsidiaries	936.1			(936.1)	
Intercompany assets	599.9	235.2		(835.1)	
Total assets	\$ 1,564.1	\$ 2,174.7	\$ 607.2	\$ (1,818.8)	\$ 2,527.2
LIABILITIES AND SHAREHOLDERS EQUITY					
Current liabilities:					
Current portion of debt	\$	\$ 2.1	\$	\$	\$ 2.1
Accounts payable		185.5	73.3		258.8
Other current liabilities	18.8	335.2	136.2		490.2
Total current liabilities	18.8	522.8	209.5		751.1
Long-term debt	777.0	380.1	2.0	(377.0)	782.1
Other liabilities	0.0	209.9	63.4	(47.6)	225.7
Equity investment in subsidiaries		223.3		(223.3)	
Intercompany liabilities			458.1	(458.1)	
Total liabilities	795.8	1,336.1	733.0	(1,106.0)	1,758.9
Shareholders' equity	768.3	838.6	(125.8)	(712.8)	768.3
Total liabilities and shareholders' equity	\$ 1,564.1	\$ 2,174.7	\$ 607.2	\$ (1,818.8)	\$ 2,527.2

Table of Contents

The Scotts Miracle-Gro Company
Condensed, Consolidating Statement of Operations
for the three months ended July 3, 2010

(in millions)

	Parent	Subsidiary Guarantors	Non- Guarantors	Eliminations	Consolidated
Net sales	\$	\$ 1,005.3	\$ 167.3	\$	\$ 1,172.6
Cost of sales		581.5	109.3		690.8
Cost of sales product registration and recall matters					
Gross profit		423.8	58.0		481.8
Operating expenses:					
Selling, general and administrative		180.0	21.3		201.3
Product registration and recall matters		1.5			1.5
Other (income) expense, net		(1.2)	0.1		(1.1)
Income from operations		243.5	36.6		280.1
Equity income in subsidiaries	(180.1)	(28.3)		208.4	
Other non-operating income	(5.3)			5.3	
Interest expense	9.7	5.4	1.4	(5.3)	11.2
Income from continuing operations before income taxes	175.7	266.4	35.2	(208.4)	268.9
Income tax (benefit) expense from continuing operations	(0.2)	86.6	13.0		99.4
Income from continuing operations	175.9	179.8	22.2	(208.4)	169.5
Income from discontinued operations, net of tax			6.4		6.4
Net income	\$ 175.9	\$ 179.8	\$ 28.6	\$ (208.4)	\$ 175.9

Table of Contents

The Scotts Miracle-Gro Company
Condensed, Consolidating Statement of Operations
for the nine months ended July 3, 2010

(in millions)

	September 30, Parent	September 30, Subsidiary Guarantors	September 30, Non- Guarantors	September 30, Eliminations	September 30, Consolidated
Net sales	\$	\$ 2,073.8	\$ 401.9	\$	\$ 2,475.7
Cost of sales		1,259.2	265.4		1,524.6
Cost of sales product registration and recall matters		1.5			1.5
Gross profit		813.1	136.5		949.6
Operating expenses:					
Selling, general and administrative		454.5	89.8		544.3
Product registration and recall matters		4.3			4.3
Other income, net		(4.8)	(2.0)		(6.8)
Income from operations		359.1	48.7		407.8
Equity income in subsidiaries	(245.2)	(30.6)		275.8	
Other non-operating income	(21.3)			21.3	
Interest expense	30.5	21.4	4.4	(21.3)	35.0
Income from continuing operations before income taxes	236.0	368.3	44.3	(275.8)	372.8
Income tax (benefit) expense from continuing operations	(0.7)	123.4	16.5		139.2
Income from continuing operations	236.7	244.9	27.8	(275.8)	233.6
Income from discontinued operations, net of tax			3.1		3.1
Net income	\$ 236.7	\$ 244.9	\$ 30.9	\$ (275.8)	\$ 236.7

Table of Contents

The Scotts Miracle-Gro Company
Condensed, Consolidating Statement of Cash Flows
for the nine months ended July 3, 2010

(in millions)

	September 30, Parent	September 30, Subsidiary Guarantors	September 30, Non- Guarantors	September 30, Eliminations	September 30, Consolidated
NET CASH (USED IN) PROVIDED BY OPERATING ACTIVITIES	\$ (38.0)	\$ 184.1	\$ 10.1	\$	\$ 156.2
INVESTING ACTIVITIES					
Proceeds from sale of long-lived assets		23.6			23.6
Investments in property, plant and equipment		(44.4)	(2.5)		(46.9)
Net cash used in investing activities		(20.8)	(2.5)		(23.3)
FINANCING ACTIVITIES					
Borrowings under revolving and bank lines of credit and term loans		593.1	334.7		927.8
Repayments under revolving and bank lines of credit and term loans		798.4	(436.4)		(1,234.8)
Proceeds from issuance of Senior Notes, net of discount	198.5				198.5
Financing and issuance fees	(5.5)				(5.5)
Dividends paid	(25.9)				(25.9)
Payments on seller notes		(0.2)			(0.2)
Excess tax benefits from share-based payment arrangements		3.9			3.9
Cash received from exercise of stock options	14.8				14.8
Intercompany financing	(143.9)	37.4	106.5		
Net cash provided by (used in) financing activities	38.0	(164.2)	4.8		(121.4)
Effect of exchange rate changes on cash			(4.4)		(4.4)
Net (decrease) increase in cash and cash equivalents		(0.9)	8.0		7.1
Cash and cash equivalents, beginning of period		6.4	64.2		70.6
Cash and cash equivalents, end of period	\$	\$ 5.5	\$ 72.2	\$	\$ 77.7

Table of Contents

The Scotts Miracle-Gro Company
Condensed, Consolidating Balance Sheet

As of July 3, 2010

(in millions)

	Parent	Subsidiary Guarantors	Non- Guarantors	Eliminations	Consolidated
ASSETS					
Current assets:					
Cash and cash equivalents	\$	\$ 5.5	\$ 72.2	\$	\$ 77.7
Accounts receivable, net		442.0	161.2		603.2
Accounts receivable pledged		23.3			23.3
Inventories, net		339.8	66.1		405.9
Assets held for sale			206.0		206.0
Prepaid and other current assets		113.7	47.5		161.2
Total current assets		924.3	553.0		1,477.3
Property, plant and equipment, net		315.5	43.9		359.4
Goodwill		305.1	0.7		305.8
Intangible assets, net		294.8	52.3		347.1
Other assets	15.4	19.6	40.5	(41.9)	33.6
Equity investment in subsidiaries	1,001.5			(1,001.5)	
Intercompany assets	376.6			(376.6)	
Total assets	\$ 1,393.5	\$ 1,859.3	\$ 690.4	\$ (1,420.0)	\$ 2,523.2
LIABILITIES AND SHAREHOLDERS EQUITY					
Current liabilities:					
Current portion of debt	\$ 180.6	\$ 16.9	\$ 2.5	\$	\$ 200.0
Accounts payable		148.4	64.9		213.3
Liabilities held for sale			44.4		44.4
Other current liabilities	7.2	395.4	133.8		536.4
Total current liabilities	187.8	560.7	245.6		994.1
Long-term debt	367.0	20.8	105.6	(3.2)	490.2
Other liabilities	3.9	185.8	56.3	(41.9)	204.1
Equity investment in subsidiaries		92.6		(92.6)	
Intercompany liabilities		96.1	277.3	(373.4)	
Total liabilities	558.7	956.0	684.8	(511.1)	1,688.4
Shareholders' equity	834.8	903.3	5.6	(908.9)	834.8
Total liabilities and shareholders' equity	\$ 1,393.5	\$ 1,859.3	\$ 690.4	\$ (1,420.0)	\$ 2,523.2

Table of Contents

The Scotts Miracle-Gro Company
Condensed, Consolidating Balance Sheet

As of September 30, 2010

(in millions)

	Parent	Subsidiary Guarantors	Non- Guarantors	Eliminations	Consolidated
ASSETS					
Current assets:					
Cash and cash equivalents	\$	\$ 5.0	\$ 83.1	\$	\$ 88.1
Accounts receivable, net		265.5	85.4		350.9
Inventories, net		287.7	65.2		352.9
Assets held for sale			193.1		193.1
Prepaid and other assets		97.9	35.2		133.1
Total current assets		656.1	462.0		1,118.1
Property, plant and equipment, net		334.7	46.6		381.3
Goodwill		305.1	0.7		305.8
Intangible assets, net		275.2	55.0		330.2
Other assets	13.9	16.1	41.1	(42.5)	28.6
Equity investment in subsidiaries	925.8			(925.8)	
Intercompany assets	344.0			(344.0)	
Total assets	\$ 1,283.7	\$ 1,587.2	\$ 605.4	\$ (1,312.3)	\$ 2,164.0
LIABILITIES AND SHAREHOLDERS EQUITY					
Current liabilities:					
Current portion of debt	\$ 193.2	\$ 1.8	\$	\$	\$ 195.0
Accounts payable		92.2	49.5		141.7
Liabilities held for sale			45.3		45.3
Other current liabilities	3.6	249.1	102.1		354.8
Total current liabilities	196.8	343.1	196.9		736.8
Long-term debt	318.8	25.5	102.1	(9.7)	436.7
Other liabilities	3.6	200.9	64.0	(42.5)	226.0
Equity investment in subsidiaries		97.8		(97.8)	
Intercompany liabilities		92.2	242.1	(334.3)	
Total liabilities	519.2	759.5	605.1	(484.3)	1,399.5
Shareholders' equity	764.5	827.7	0.3	(828.0)	764.5
Total liabilities and shareholders' equity	\$ 1,283.7	\$ 1,587.2	\$ 605.4	\$ (1,312.3)	\$ 2,164.0

Table of Contents

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

The purpose of this discussion is to provide an understanding of the financial condition and results of operations of The Scotts Miracle-Gro Company (Scotts Miracle-Gro) and its subsidiaries (collectively, together with Scotts Miracle-Gro, the Company, we or us) by focusing on changes in certain key measures from year-to-year. Management's Discussion and Analysis is divided into the following sections:

Executive summary

Results of operations

Segment results

Liquidity and capital resources

Regulatory matters

Critical accounting policies and estimates

EXECUTIVE SUMMARY

We are dedicated to delivering strong, consistent financial results and outstanding shareholder returns by providing products of superior quality and value in order to enhance consumers' outdoor living environments. We are a leading manufacturer and marketer of branded products for consumer lawn and garden care in North America and Europe. We are Monsanto's exclusive agent for the marketing and distribution of consumer Roundup® non-selective herbicide products within the United States and other contractually specified countries. We have a presence in similar branded consumer products in Australia, the Far East and Latin America. We also operate Scotts LawnService®, the second largest U.S. lawn care service business. Our operations are divided into the following reportable segments: Global Consumer and Scotts LawnService®.

On February 28, 2011, we completed the sale of a significant majority of the assets of our Global Professional business (excluding our non-European professional seed business, "Global Pro") to Israel Chemicals Ltd. (ICL) for \$270 million in an all-cash transaction, subject to certain adjustments, resulting in \$270.9 million net proceeds received as of July 2, 2011. Effective in our first quarter of fiscal 2011, we classified Global Pro as discontinued operations. Prior to being reported as discontinued operations, Global Pro was included as part of our former Global Professional business segment. Results for our non-European professional seed business have been reclassified to Corporate & Other.

During our first quarter of fiscal 2010, all Smith & Hawken stores were closed and substantially all operational activities of Smith & Hawken were discontinued. As a result, effective in our first quarter of fiscal 2010, we classified Smith & Hawken as discontinued operations.

As a leading consumer branded lawn and garden company, our product development and marketing efforts are largely focused on providing innovative and differentiated products and on continually increasing brand and product awareness to inspire consumers and create retail demand. We have successfully applied this model for a number of years by focusing on research and development and investing approximately 5% of our annual net sales in advertising to support and promote our products and brands. We continually explore new and innovative ways to communicate with consumers. We believe that we receive a significant return on these expenditures and anticipate a similar commitment to research and development, advertising and marketing investments in the future, with the continuing objective of driving category growth and increasing market share.

Our sales in any one year are susceptible to weather conditions in the markets in which our products are sold. For instance, periods of wet weather can adversely impact sales of certain products, while increasing demand for other products. We believe that our diversified product line and our broad geographic diversification reduce this risk, although to a lesser extent in a year where unfavorable weather is geographically wide-spread and extends across a significant portion of the lawn and garden season. We also believe that weather conditions in any one year,

positive or negative, do not materially alter longer-term category growth trends.

Due to the nature of our lawn and garden business, significant portions of our products ship to our retail customers during our second and third fiscal quarters. Our annual sales are further concentrated in the second and third fiscal quarters by retailers who increasingly rely on our ability to deliver products in season when consumers buy our products, thereby reducing retailers' inventories.

Table of Contents

	September 30, Percent of Net Sales from Continuing Operations by Quarter			
	2010	2009	2008	2008
First Quarter	8.7%	8.5%	8.5%	8.5%
Second Quarter	36.2%	32.0%	33.3%	33.3%
Third Quarter	40.5%	42.5%	40.7%	40.7%
Fourth Quarter	14.6%	17.0%	17.5%	17.5%

Management focuses on a variety of key indicators and operating metrics to monitor the financial condition and performance of the continuing operations of our business. These metrics include consumer purchases (point-of-sale data), market share, category growth, net sales (including unit volume, pricing, sales mix and foreign exchange movements), organic sales growth (net sales growth excluding the impact of foreign exchange movements, product recalls and acquisitions), gross profit margins, income from operations, income from continuing operations before income taxes, net income and earnings per share. To the extent applicable, these measures are evaluated with and without product registration and recall matters and impairment, restructuring and other charges, which management believes are not indicative of the earnings capabilities of our businesses. We also focus on measures to optimize cash flow and return on invested capital, including the management of working capital and capital expenditures. The Scotts Miracle-Gro Board of Directors has authorized the repurchase of up to \$700 million of our common shares through September 30, 2014. Further, on August 8, 2011, we announced that the Scotts Miracle-Gro Board of Directors increased our quarterly dividend from \$0.25 to \$0.30 per common share.

The decisions to increase the amount of cash we intend to return to our shareholders reflect our continued confidence in the performance of our business, which should allow us to return increased cash to shareholders while also making strategic investments that drive long-term profitable growth. During the third quarter of fiscal 2011, we repurchased approximately 2.2 million of our common shares in open market transactions for \$125.0 million. Since the inception of this program in the fourth quarter of fiscal 2010, we have repurchased approximately 4.4 million of our common shares for \$243.7 million.

Product Registration and Recall Matters

In April 2008, we became aware that a former associate apparently deliberately circumvented our policies and U.S. Environmental Protection Agency (U.S. EPA) regulations under the Federal Insecticide, Fungicide, and Rodenticide Act of 1947, as amended (FIFRA), by failing to obtain valid registrations for certain products and/or causing certain invalid product registration forms to be submitted to regulators. Since that time, we have been cooperating with both the U.S. EPA and the U.S. Department of Justice (the U.S. DOJ) in related civil and criminal investigations into the pesticide product registration issues as well as a state civil investigation into related allegations arising under state pesticide registration laws and regulations.

In late April 2008, in connection with the U.S. EPA 's investigation, we conducted a consumer-level recall of certain consumer lawn and garden products and a Scotts LawnService® product. Subsequently, the Company and the U.S. EPA agreed upon a Compliance Review Plan for conducting a comprehensive, independent review of our product registration records. Pursuant to the Compliance Review Plan, an independent third-party firm, Quality Associates Incorporated (QAI), reviewed substantially all of our U.S. pesticide product registrations and associated advertisements, some of which were historical in nature and no longer related to sales of our products. The U.S. EPA investigation and the QAI review process resulted in the temporary suspension of sales and shipments of certain products. In addition, as the QAI review process or our internal review identified potential FIFRA registration issues (some of which appear unrelated to the actions of the former associate), we endeavored to stop selling or distributing the affected products until the issues could be resolved. QAI 's review of our U.S. pesticide product registrations and associated advertisements is now substantially complete. The results of the QAI review process did not materially affect our fiscal 2010 or year-to-date fiscal 2011 sales and are not expected to materially affect our sales during the remainder of fiscal 2011.

Settlement discussions relating to potential fines and/or penalties are a frequent outgrowth of governmental investigations. In that regard, on or about June 30, 2011, we received a Notice of Intent to File Administrative Complaint (Notice) from the U.S. EPA Region 5 with respect to the alleged FIFRA violations. The Notice, which does not set forth a proposed penalty amount, offers us an opportunity to present any information that we believe the U.S. EPA should consider prior to filing the complaint and indicates that the U.S. EPA is prepared to meet with us to discuss the alleged violations. We made a timely response to the Notice and communications between the Company and the U.S. EPA are underway. In addition, we recently began settlement discussions with the U.S. DOJ regarding its criminal investigation.

Based on the facts and circumstances known to us at this time (including settlement discussions that have taken place to date), we have established what we believe to be an appropriate reserve. The U.S. EPA and U.S. DOJ investigations continue, however, and may result in future state, federal or private rights of action including fines and/or penalties with respect to known or potential additional product registration issues. Until these investigations are completed, we cannot reasonably estimate the total scope or magnitude of all possible liabilities. It is possible that any such fines and/or penalties, as well as any judgments, litigation costs or other liabilities relating to such known or potential product registration issues, could exceed the amount of the reserve, possibly materially, and could have an adverse effect on our financial condition,

results of operations or cash flows.

Table of Contents

In June 2008, the California Department of Pesticide Regulation (CDPR) issued a request for information to the Company relating to products that had been the subject of the April 2008 recall. We cooperated with that inquiry and reached agreement with CDPR that CDPR would place its investigation on hold pending the completion of our internal audit. In furtherance of that agreement, in May 2010, the Company and CDPR executed a tolling agreement that extended CDPR's rights through April 2012. In July 2010, CDPR notified us that CDPR planned to proceed with its investigation independent of the U.S. EPA and U.S. DOJ, and in March 2011, we received a letter from CDPR offering to settle the matter without the need for an enforcement proceeding for \$245,631. On July 25, 2011, we paid the requested civil penalty and entered into a Settlement Agreement pursuant to which CDPR agreed not to take further civil or criminal action with regard to the affected products.

As a result of these registration and recall matters, we have recorded charges for affected inventory and other registration and recall-related costs. The effects of these adjustments, including the reserve noted above, were pre-tax charges of \$6.8 million and \$1.5 million for the three-month periods, and \$11.0 million and \$5.8 million for the nine-month periods ended July 2, 2011 and July 3, 2010, respectively. We expect that future charges will include costs associated with the rework of certain finished goods inventories, the potential disposal of certain products and ongoing third-party professional services related to the U.S. EPA, U.S. DOJ and state investigations. It may also be appropriate to establish additional reserves as settlement discussions continue.

We are committed to providing our customers and consumers with products of superior quality and value to enhance their lawns, gardens and overall outdoor living environments. We believe consumers have come to trust our brands based on the superior quality and value they deliver, and that trust is highly valued. We also are committed to conducting business with the highest degree of ethical standards and in adherence to the law. While we are disappointed in these events, we believe we have made significant progress in addressing the issues and restoring customer and consumer confidence in our products.

RESULTS OF OPERATIONS

We classified Global Pro and Smith & Hawken as discontinued operations beginning in our first quarter of fiscal 2011 and our first quarter of fiscal 2010, respectively. As a result, and unless specifically stated, all discussions regarding results for the three- and nine-month periods ended July 2, 2011 and July 3, 2010 reflect results from our continuing operations.

The following table sets forth the components of income and expense as a percentage of net sales for the three- and nine-month periods ended July 2, 2011 and July 3, 2010:

	September 30, THREE MONTHS ENDED JULY 2, 2011 (UNAUDITED)	September 30, THREE MONTHS ENDED JULY 3, 2010 (UNAUDITED)	September 30, NINE MONTHS ENDED JULY 2, 2011 (UNAUDITED)	September 30, NINE MONTHS ENDED JULY 3, 2010 (UNAUDITED)
Net sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	62.1	58.9	62.2	61.6
Cost of sales product registration and recall matters	0.1		0.1	
Gross profit	37.8	41.1	37.7	38.4
Operating expenses:				
Selling, general and administrative	18.2	17.2	22.8	22.0
Product registration and recall matters	0.5	0.1	0.3	0.2
Impairment, restructuring and other charges	1.3		0.6	
Other income, net	(0.4)	(0.1)	(0.2)	(0.3)
Income from operations	18.2	23.9	14.2	16.5
Costs related to refinancing	0.1		0.1	
Interest expense	1.4	1.0	1.5	1.4
Income from continuing operations before income taxes	16.7	22.9	12.6	15.1
Income tax expense from continuing operations	6.2	8.4	4.6	5.7
Income from continuing operations	10.5	14.5	8.0	9.4

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

Income from discontinued operations, net of tax		0.5	1.1	0.2
Net income	10.5%	15.0%	9.1%	9.6%

Net sales for the three months ended July 2, 2011 were \$1.06 billion, a decrease of 9.7% from net sales of \$1.17 billion for the three months ended July 3, 2010. Net sales for the first nine months of fiscal 2011 were \$2.42 billion, a decrease of 2.3% from net sales of \$2.48 billion for the comparable period of fiscal 2010. The decline in organic net sales, which excludes the impact of changes in foreign exchange rates, was 11.4% and 3.3% for the three- and nine-month periods ended July 2, 2011, respectively.

Table of Contents

In the Global Consumer segment, organic net sales declined by 14.2% and 4.9% for the third quarter and first nine months of fiscal 2011, respectively. Organic net sales for the Scotts LawnService® segment grew by 1.3% and 5.0% for the three and nine months ended July 2, 2011, respectively. Corporate & Other had an overall sales increase of \$19.3 million for the third quarter of fiscal 2011 and \$24.9 million for the first nine months of fiscal 2011, primarily attributable to our supply agreements to ICL.

As a percentage of net sales, our gross margin rate was 37.8% for the third quarter of fiscal 2011 compared to 41.1% for the third quarter of fiscal 2010. For the first nine months of fiscal 2011, our gross margin rate was 37.7% compared to 38.4% in the comparable period of fiscal 2010. Excluding product registration and recall matters, the gross margin rate decreased by 320 basis points and 60 basis points for the third quarter and first nine months of fiscal 2011, respectively. The gross margin rate decrease for the third quarter and first nine months of fiscal 2011 was driven by unfavorable sales mix, higher commodity costs, increased trade promotions and reduced leverage on fixed manufacturing and storage costs partially offset by cost productivity improvements.

The following table sets forth the components of selling, general and administrative expenses (in millions):

	September 30, THREE MONTHS ENDED JULY 2, 2011 (UNAUDITED)		September 30, THREE MONTHS ENDED JULY 3, 2010 (UNAUDITED)		September 30, NINE MONTHS ENDED JULY 2, 2011 (UNAUDITED)		September 30, NINE MONTHS ENDED JULY 3, 2010 (UNAUDITED)	
Advertising	\$	56.7	\$	56.6	\$	121.8	\$	122.3
Other selling, general and administrative		133.1		142.3		422.6		414.6
Amortization of intangibles		2.6		2.4		7.4		7.4
	\$	192.4	\$	201.3	\$	551.8	\$	544.3

Selling, general and administrative (SG&A) expenses decreased \$8.9 million, or 4.4%, to \$192.4 million for the third quarter and increased \$7.5 million, or 1.4%, to \$551.8 million for the first nine months of fiscal 2011 compared to the same periods of fiscal 2010. Excluding the impact of foreign exchange rates, SG&A decreased 6.0% for the three months ended July 2, 2011 and increased 1.1% for the first nine months of fiscal 2011 compared to the same periods of fiscal 2010. The decrease in SG&A for the third quarter of fiscal 2011 was primarily attributable to lower variable compensation, partially offset by increased bad debt expense, costs associated with two regional offices opened in fiscal 2011 and various other expenses including incremental marketing and research and development. The increase in SG&A for the first nine months was in large part driven by severance costs, the opening of two new regional offices, increased bad debt expense and incremental marketing and research and development, partially offset by lower variable compensation.

We recorded \$5.7 million and \$7.8 million of SG&A-related product registration and recall charges during the third quarter and first nine months of fiscal 2011, respectively, primarily related to reserves established in the third quarter of fiscal 2011 in connection with the U.S. EPA and U.S. DOJ investigations, as well as third-party compliance review, legal and consulting fees. For the quarter and nine months ended July 3, 2010, we recorded \$1.5 million and \$4.3 million of SG&A-related product registration and recall costs, respectively.

During the third quarter and first nine months of fiscal 2011, we recorded \$13.8 million of impairment, restructuring and other charges. On May 26, 2011, we terminated or amended various contracts with the former owners of Turf-Seed, Inc. and settled the contingent consideration associated with the acquisition of that entity, resulting in a net charge of \$10.3 million. We also recorded severance related restructuring charges of \$3.5 million during the third quarter of fiscal 2011.

Other income was \$4.2 million and \$5.0 million for the third quarter and first nine months of fiscal 2011, respectively, compared to \$1.1 million and \$6.8 million for the third quarter and first nine months of fiscal 2010, respectively. The increase for the third quarter of fiscal 2011 was primarily due to the elimination of royalties resulting from the settlement with the former owners of Turf-Seed, Inc. The decrease in the first nine months of fiscal 2011 as compared to the same period in the prior year was primarily driven by a gain on the sale of property in the first quarter of fiscal 2010, partially offset by the elimination of royalties resulting from the settlement with the former owners of Turf-Seed, Inc.

Interest expense for the third quarter and first nine months of fiscal 2011 was \$14.0 million and \$37.3 million, respectively, compared to \$11.2 million and \$35.0 million for the third quarter and first nine months of fiscal 2010, respectively. We also incurred a \$1.2 million charge to write-off deferred financing fees in the third quarter of fiscal 2011 as a result of refinancing our credit facility. The increase in interest expense for the third quarter and first nine months of fiscal 2011 was attributable to an increase in weighted average interest rates as a result of our fiscal

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

2011 refinancing activities, partially offset by a decrease in average borrowings. Weighted average interest rates increased by approximately 158 basis points and 93 basis points during the third quarter and first nine months of fiscal 2011, respectively. Excluding the impact of foreign exchange rates, average borrowings decreased by approximately \$116.9 million and \$137.8 million during the third quarter and first nine months of fiscal 2011, respectively. Refer to NOTE 7. DEBT of the Notes to Condensed, Consolidated Financial Statements for further details of our borrowing facilities.

Table of Contents

The effective tax rate for continuing operations was 36.5% for the first nine months of fiscal 2011, compared to 37.3% for the same period of fiscal 2010. Excluding reserves established in the third quarter of fiscal 2011 for potential fines and penalties associated with the FIFRA investigations and the \$1.9 million tax expense recorded in the second quarter of fiscal 2010 related to the disallowance of the Medicare Part D tax deduction, the effective tax rate for continuing operations was 36.0% and 36.8% for the first nine months of fiscal 2011 and 2010, respectively. The effective tax rate used for interim reporting purposes was based on management's best estimate of factors impacting the effective tax rate for the full fiscal year. Factors affecting the estimated effective tax rate include assumptions as to income by jurisdiction (domestic and foreign), the availability and utilization of tax credits and the existence of elements of income and expense that may not be taxable or deductible, as well as other items. The estimated effective tax rate is subject to revision at fiscal year end as facts and circumstances change. There can be no assurance that the effective tax rate estimated for interim financial reporting purposes will approximate the effective tax rate determined at fiscal year end.

We reported income from continuing operations of \$111.7 million, or \$1.69 per diluted share, for the third quarter of fiscal 2011 compared to \$169.5 million, or \$2.50 per diluted share, for the third quarter of fiscal 2010. Income from continuing operations for the first nine months of fiscal 2011 was \$193.6 million, or \$2.89 per diluted share, versus \$233.6 million, or \$3.46 per diluted share, for the same period of fiscal 2010. The decrease in income from continuing operations for the third quarter and first nine months of fiscal 2011 was driven primarily by unfavorable weather in most of the U.S., which resulted in lower net sales and decreased profitability driven by unfavorable sales mix, higher commodity costs and increased trade promotions. Diluted average common shares used in the diluted net income per common share calculation were 66.2 million for the third quarter of fiscal 2011 compared to 67.9 million for the same period a year ago. Diluted average common shares used in the diluted net income per common share calculation were 67.1 million for the nine months ended July 2, 2011 versus 67.4 million for the nine months ended July 3, 2010. Diluted average common shares included 1.7 million and 1.5 million equivalent shares for the third quarter and first nine months of fiscal 2011, respectively, to reflect the effect of the assumed conversion of dilutive stock options, restricted stock and restricted stock unit awards. Diluted average common shares included 1.4 million and 1.2 million equivalent shares for the third quarter and first nine months of fiscal 2010, respectively. The decrease in diluted average common shares was primarily driven by repurchases of our common shares, partially offset the exercise of stock options and by an increase in the number of equivalent shares due to additional equity based grants and an increase in our average share price.

We reported a loss from discontinued operations, net of tax, of \$0.1 million for the third quarter of fiscal 2011 and income from discontinued operations, net of tax, of \$27.7 million for the first nine months of fiscal 2011. Income from discontinued operations, net of tax, was \$6.4 million and \$3.1 million for the third quarter and first nine months of fiscal 2010, respectively. Income from discontinued operations for the first nine months of fiscal 2011 includes a net after-tax gain of \$21.2 on the sale of Global Pro to ICL. The income from discontinued operations in the three and nine months ended July 3, 2010 is attributable to Global Pro's operations and the sale of the Smith & Hawken intellectual property, partially offset by costs associated with the final closure activities of Smith & Hawken.

SEGMENT RESULTS

Our continuing operations are divided into the following segments: Global Consumer and Scotts LawnService®. This division of reportable segments is consistent with how the segments report to and are managed by our senior management. Reclassifications have been made to prior period segment amounts to reflect changes in the allocation of certain shared expenses among the segments, which in management's judgment better align those expenses with the associated drivers and benefits. Furthermore, our reportable segments have been revised to reflect the sale of Global Pro, which is now reported in discontinued operations. Our non-European professional seed business was not part of the sale and is now included in Corporate & Other, along with revenues and expenses associated with the Company's supply agreements with ICL, as well as corporate and administrative expenses.

Segment performance is evaluated based on several factors, including income from continuing operations before amortization, product registration and recall costs, and impairment, restructuring and other charges, which is not a measure recognized under GAAP. Management uses this measure of operating profit to gauge segment performance because we believe this measure is the most indicative of performance trends and the overall earnings potential of each segment.

The following table sets forth net sales by segment (in millions):

September 30, THREE MONTHS ENDED JULY 2, 2011	September 30, THREE MONTHS ENDED JULY 3, 2010	September 30, NINE MONTHS ENDED JULY 2, 2011	September 30, NINE MONTHS ENDED JULY 3, 2010
--	--	---	---

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

	(UNAUDITED)		(UNAUDITED)					
Global Consumer	\$	951.6	\$	1,085.9	\$	2,225.2	\$	2,314.6
Scotts LawnService®		82.4		81.3		152.2		144.9
Segment total		1,034.0		1,167.2		2,377.4		2,459.5
Corporate & Other		24.9		5.6		41.7		16.8
Roundup® amortization		(0.2)		(0.2)		(0.6)		(0.6)
Consolidated	\$	1,058.7	\$	1,172.6	\$	2,418.5	\$	2,475.7

Table of Contents

The following table sets forth segment income from continuing operations before income taxes (in millions):

	September 30, THREE MONTHS ENDED		September 30, NINE MONTHS ENDED	
	JULY 2, 2011 (UNAUDITED)	JULY 3, 2010 (UNAUDITED)	JULY 2, 2011 (UNAUDITED)	JULY 3, 2010 (UNAUDITED)
Global Consumer	\$ 209.9	\$ 289.5	\$ 453.8	\$ 499.8
Scotts LawnService®	22.4	21.9	2.7	(0.7)
Segment total	232.3	311.4	456.5	499.1
Corporate & Other	(16.0)	(27.3)	(79.5)	(77.4)
Roundup® amortization	(0.2)	(0.2)	(0.6)	(0.6)
Other amortization	(3.1)	(2.3)	(8.1)	(7.5)
Product registration and recall matters	(6.8)	(1.5)	(11.0)	(5.8)
Impairment, restructuring and other charges	(13.8)		(13.8)	
Costs related to refinancing	(1.2)		(1.2)	
Interest expense	(14.0)	(11.2)	(37.3)	(35.0)
Consolidated	\$ 177.2	\$ 268.9	\$ 305.0	\$ 372.8

Global Consumer

Global Consumer segment net sales were \$951.6 million for the third quarter and \$2.23 billion for the first nine months of fiscal 2011, representing a decrease of 12.4% and 3.9% from the third quarter and first nine months of fiscal 2010, respectively. Organic net sales declined by 14.2% and 4.9% for the third quarter and first nine months of fiscal 2011, respectively. The decrease was driven primarily by unit volume declines primarily as a result of unfavorable weather in most of the U.S. during the peak weeks of the lawn and garden season, which negatively impacted consumer activity. Sales were also unfavorably impacted by more competitive promotional landscape and changes in certain retailer strategies within the mass merchant channel. Foreign exchange movements positively impacted net sales by 1.8% and 1.0% for the third quarter and first nine months, respectively.

Organic net sales for U.S. Consumer decreased 17.5% and 6.6% for the third quarter and first nine months of fiscal 2011, respectively, driven primarily by unit volume declines, partially offset by price increases of 0.9% and 1.2% for the third quarter and first nine months of fiscal 2011, respectively. Consumer purchases of our products at our largest U.S. retailers (retail point-of-sale, or POS) decreased by 6.3% and 3.5% for the quarter and first nine months of fiscal 2011, respectively. The decrease in U.S. net sales for the third quarter was largely due to lower sales of lawn fertilizers and control products. On a year-to-date basis, net sales declines in lawn fertilizers and controls were partially offset by increased sales of grass seed and growing media. Organic net sales for International Consumer increased by 4.0% and 3.3% for the third quarter and first nine months of fiscal 2011, respectively, driven primarily by unit volume growth, combined with slight increases in pricing. Foreign exchange movements increased International Consumer net sales by 11.4% and 6.0% for the third quarter and first nine months of fiscal 2011, respectively.

Global Consumer segment operating income decreased by \$79.6 million and \$46.0 million in the third quarter and first nine months of fiscal 2011, respectively. Excluding the impact of foreign exchange movements, Global Consumer segment operating income decreased by \$84.5 million and \$54.3 million in the third quarter and first nine months of fiscal 2011, respectively. The decrease in operating income was driven by a decrease in net sales accompanied by a decline in gross margin rates of 310 and 20 basis points for the third quarter and first nine months of fiscal 2011, respectively. For the third quarter and first nine months of fiscal 2011 unfavorable sales mix, higher commodity costs and higher trade expenses contributed to the decrease in Global Consumer gross margin rates. The gross margin rate for the third quarter of fiscal 2011 was also negatively impacted by reduced leverage of fixed manufacturing and storage costs. Excluding the impact of foreign exchange movements, Global Consumer SG&A spending decreased \$6.3 million for the third quarter of fiscal 2011 and increased \$5.7 million for the first nine months of fiscal 2011. Decreases in variable compensation, which had a greater impact on the third quarter, were offset by higher bad debt expense, incremental expenses associated with two new regional offices, as well as incremental marketing and research and development spending.

Scotts LawnService®

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

Compared to the same periods in the prior fiscal year, Scotts LawnService® net sales increased by \$1.1 million and \$7.3 million in the third quarter and first nine months of fiscal 2011, respectively, primarily due to customer counts that were approximately 3% higher through July 2, 2011.

Scotts LawnService® segment operating income increased by \$0.5 million and \$3.4 million in the third quarter and first nine months of fiscal 2011, respectively. The year-to-date fiscal 2011 increase in operating income was primarily driven by higher revenue and lower SG&A, including lower variable compensation.

Table of Contents

Corporate & Other

The net operating loss for Corporate & Other decreased by \$11.3 million for the third quarter of fiscal 2011 and increased by \$2.1 million for the first nine months of fiscal 2011 as compared to the same periods of fiscal 2010. The net operating loss decline for the third quarter was driven by a decrease in variable compensation, whereas the year-to-date fiscal 2011 increase in net operating loss was primarily related to severance costs, consulting fees and the non-recurrence of a gain on a property sale in fiscal 2010, largely offset by lower variable compensation.

Management's Outlook

We anticipate full year net sales will be roughly flat in fiscal 2011, primarily driven by unfavorable weather conditions in most of the U.S. We anticipate our gross margin rate will decline by at least 50 basis points in fiscal 2011, driven primarily by unfavorable mix, higher commodity costs, increased trade promotional expenses and reduced leverage of fixed manufacturing and storage costs, partially offset by supply chain cost productivity initiatives. Full year SG&A spending is expected to be essentially flat as incremental costs associated with media, marketing, research and development and our regional offices, and higher bad debt expense will be offset by lower variable compensation. We expect interest expense of approximately \$51 million, with the increase from fiscal 2010 driven by higher interest rates associated with the Senior Notes issued in January and December 2010 and our senior secured credit facility that was refinanced on June 30, 2011. For all of fiscal 2011, we anticipate income from continuing operations, excluding product registration and recall matters and impairment, restructuring and other charges, to decrease 8% to 11%.

In the long-term, we remain focused on growing cash provided by operating activities and return on invested capital, both of which are important drivers of shareholder value. Our regular quarterly dividend, which we are increasing to \$0.30 per common share, will allow us to continue to return cash to shareholders while maintaining our targeted capital structure. In addition, we continue to execute our share repurchase program, with the expectation of investing approximately \$358 million for this purpose during fiscal 2011.

For certain information concerning our risk factors, see PART II. OTHER INFORMATION: ITEM 1A. RISK FACTORS of this Quarterly Report on Form 10-Q.

LIQUIDITY AND CAPITAL RESOURCES

Operating Activities

Cash used in operating activities totaled \$13.5 million for the nine months ended July 2, 2011, compared to cash provided by operating activities of \$156.2 million for the comparable period in fiscal 2010. Excluding the impact of discontinued operations, cash provided by operating activities was approximately \$70.7 million and \$170.2 million for the nine months ended July 2, 2011 and July 3, 2010, respectively. Net income from continuing operations decreased by \$40 million during the first nine months of fiscal 2011 primarily as a result of lower net sales, decreased gross profit and a slight increase in SG&A costs. Operating cash flows used to support working capital for continuing operations increased by approximately \$70 million for the nine months ended July 2, 2011 compared to the comparable period in fiscal 2010, driven by higher inventories attributable to lower than anticipated sales and increased in accounts receivable due to the timing of third quarter sales in fiscal 2011.

Investing Activities

Cash provided by investing activities totaled \$180 million for the nine months ended July 2, 2011, compared to cash used by investing activities of \$23.3 million for the comparable period in fiscal 2010. The first nine months of fiscal 2011 included net cash of \$253.9 million provided by the sale of Global Pro. In fiscal 2010, we received cash of \$23.6 million for the sale of long-lived assets, primarily for the intellectual property of Smith & Hawken. Capital spending increased from \$46.9 million in the first nine months of fiscal 2010 to \$53.3 million in the first nine months of fiscal 2011. Significant capital projects during the first nine months of fiscal 2011 included a new growing media plant in Missouri, a new liquids bottling plant in Mississippi, improvements at other growing media facilities and investments in information technology. For the first nine months of fiscal 2010, capital spending involved the completion of new production technology to support the national launch of Scotts EZ Seed®, investments to expand our information technology capabilities and improvements at our growing media facilities. Investing activities for the first nine months of fiscal 2011 also included \$20 million in payments to the former owners of Turf-Seed, Inc.

Financing Activities

Cash used in financing activities totaled \$91.8 million and \$121.4 million for the nine months ended July 2, 2011 and July 3, 2010, respectively. Net repayments under our credit facilities were \$40 million for the nine months ended July 2, 2011

Table of Contents

compared to \$307 million for the comparable period in fiscal 2010. Financing activities for the first nine months of fiscal 2011 also included financing and issuance fees of \$18.5 million, primarily attributable to the refinancing of our credit facility in June 2011 and our \$200 million bond offering in December 2010. Cash returned to shareholders through common share repurchases of \$218.7 million and an increase of \$23.5 million in dividends paid were also significant elements of cash used in financing activities for the nine months ended July 2, 2011.

Borrowing Agreements

Our primary sources of liquidity are cash generated by operations and borrowings under our credit agreement. On June 30, 2011, Scotts Miracle-Gro and certain of its subsidiaries entered into a senior secured five-year revolving loan facility in the aggregate principal amount of up to \$1.7 billion. Under our current structure, we may request an additional \$450 million in revolving and/or term commitments, subject to certain specified conditions, including approval from our lenders. Borrowings may be made in various currencies including U.S. dollars, Euros, British pounds, Australian dollars and Canadian dollars.

As of July 2, 2011, there was \$1.3 billion of availability under our revolving credit facility, including letters of credit. Under our revolving credit facility, we have the ability to issue letter of credit commitments up to \$75 million. At July 2, 2011, we had letters of credit in the aggregate face amount of \$26.3 million outstanding.

On January 14, 2010, Scotts Miracle-Gro issued \$200 million aggregate principal amount of the 7.25% Senior Notes, the net proceeds of which were used to reduce outstanding borrowings under our then existing senior secured revolving credit facility. The 7.25% Senior Notes represent general unsecured senior obligations of Scotts Miracle-Gro, and were sold to the public at 99.254% of the principal amount thereof, to yield 7.375% to maturity. The 7.25% Senior Notes have interest payment dates of January 15 and July 15, which began on July 15, 2010, and may be redeemed prior to maturity at applicable redemption premiums. The 7.25% Senior Notes contain usual and customary incurrence-based covenants, which include, but are not limited to, restrictions on the incurrence of additional indebtedness, the incurrence of liens and the issuance of certain preferred shares, and the making of certain distributions, investments and other restricted payments, as well as other usual and customary covenants, which include, but are not limited to, restrictions on sale and leaseback transactions, restrictions on purchases for or redemptions of Scotts Miracle-Gro stock and prepayments of subordinated debt, limitations on asset sales and restrictions on transactions with affiliates. The 7.25% Senior Notes mature on January 15, 2018.

On December 16, 2010, Scotts Miracle-Gro issued \$200 million aggregate principal amount of the 6.625% Senior Notes, the net proceeds of which were used to reduce outstanding borrowings under our then existing senior secured credit facilities and for general corporate purposes. The Company sold the 6.625% Senior Notes in a private placement exempt from the registration requirements under the Securities Act of 1933, as amended. The 6.625% Senior Notes represent general unsecured senior obligations of Scotts Miracle-Gro and rank equal in right of payment with our existing and future unsecured senior debt, including, without limitation, the 7.25% Senior Notes. The 6.625% Senior Notes have interest payment dates of June 15 and December 15 of each year, commencing on June 15, 2011, and may be redeemed prior to maturity at applicable redemption premiums. The 6.625% Senior Notes contain usual and customary incurrence-base covenants, as well as other usual and customary covenants, substantially similar to those contained in the 7.25% Senior Notes. The 6.625% Senior Notes mature on December 15, 2020.

Certain of Scotts Miracle-Gro's domestic subsidiaries serve as guarantors of both the 7.25% and the 6.625% Senior Notes. Refer to NOTE 16. FINANCIAL INFORMATION FOR SUBSIDIARY GUARANTORS AND NON-GUARANTORS for more information regarding the guarantor entities.

At July 2, 2011, we had outstanding interest rate swap agreements with major financial institutions that effectively converted a portion of our variable-rate debt denominated in U.S. dollars to a fixed rate. Interest payments made between the effective date and expiration date are hedged by the swap agreements, except as noted below. The notional amount, effective date, expiration date and rate of these swap agreements are shown in the table below.

NOTIONAL AMOUNT (IN MILLIONS)	EFFECTIVE DATE (a)	EXPIRATION DATE	FIXED RATE
\$ 200	2/14/2007	2/14/2012	5.20%
50	2/14/2012	2/14/2016	3.78%
150 ^(b)	11/16/2009	5/16/2016	3.26%
50 ^(c)	2/16/2010	5/16/2016	3.05%
150 ^(b)	12/20/2011	6/20/2016	2.61%

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

150 ^(c)	2/7/2012	5/7/2016	2.42%
100 ^(c)	2/21/2012	5/23/2016	2.40%
50 ^(d)	12/6/2012	9/6/2017	2.96%

Table of Contents

- (a) The effective date refers to the date on which interest payments were first hedged by the applicable swap agreement.
- (b) Interest payments made during the six-month period of each year that begins with the month and day of the effective date are hedged by the swap agreement.
- (c) Interest payments made during the three-month period of each year that begins with the month and day of the effective date are hedged by the swap agreement.
- (d) Interest payments made during the nine-month period of each year that begins with the month and day of the effective date are hedged by the swap agreement.

On May 1, 2009, we entered into a Master Accounts Receivable Purchase Agreement (the 2009 MARP Agreement), with an initial stated termination date of May 1, 2010, or such later date as may be mutually agreed by us and our lender. The 2009 MARP Agreement provided for the discounted sale, on an uncommitted, revolving basis, of accounts receivable generated by a specified account debtor, with aggregate limits not to exceed \$80 million. The 2009 MARP Agreement provided an interest rate that approximated the 7-day LIBOR rate plus 225 basis points.

On May 13, 2010, we entered into a First Amendment (the First Amendment) to the 2009 MARP Agreement with our lender. The First Amendment, which was effective May 1, 2010, extended the stated termination date of the 2009 MARP Agreement through May 12, 2011, or such later date as may be mutually agreed by us and our lender. On May 10, 2011, we entered into a Second Amendment to the 2009 MARP Agreement with our lender which further extended the stated termination date through September 30, 2011, or such later date as may be mutually agreed by us and our lender.

The 2009 MARP Agreement, as amended by the First Amendment, provides an interest rate that approximates the 7-day LIBOR rate plus 125 basis points. The amendments did not otherwise modify any substantive provisions of the 2009 MARP Agreement. There were no borrowings under the amended 2009 MARP Agreement as of July 2, 2011.

As of July 2, 2011, we were in compliance with all debt covenants. Our senior secured revolving credit facility contains among other obligations, an affirmative covenant regarding our leverage ratio, calculated as indebtedness relative to our earnings before interest, taxes, depreciation and amortization. Under the terms of the senior secured revolving credit facility, the maximum leverage ratio was 3.50 as of July 2, 2011. Our leverage ratio was 1.83 at July 2, 2011. Our senior secured revolving credit facility also includes an affirmative covenant regarding our interest coverage. Under the terms of the senior secured revolving credit facility, the minimum interest coverage ratio was 3.50 for the twelve months ended July 2, 2011. Our interest coverage ratio was 8.51 for the twelve months ended July 2, 2011. We continue to monitor our compliance with the leverage ratio, interest coverage ratio and other covenants contained in the senior secured revolving credit facility and, based upon our current operating assumptions, we expect to remain in compliance with the permissible leverage ratio and interest coverage ratio throughout fiscal 2011. However, an unanticipated charge to earnings, an increase in debt or other factors could materially adversely affect our ability to remain in compliance with the financial or other covenants of our senior secured revolving credit facility, potentially causing us to have to seek an amendment or waiver from our lending group which could result in repricing of our senior secured revolving credit facility. While we believe we have good relationships with our banking group, we can provide no assurance that such a request would be likely to result in a modified or replacement credit facility on reasonable terms, if at all.

Judicial and Administrative Proceedings

Apart from the proceedings surrounding the FIFRA compliance matters, which are discussed separately, we are party to various pending judicial and administrative proceedings arising in the ordinary course of business, including, among others, proceedings based on accidents or product liability claims and alleged violations of environmental laws. We have reviewed these pending judicial and administrative proceedings, including the probable outcomes, reasonably anticipated costs and expenses, and the availability and limits of our insurance coverage, and have established what we believe to be appropriate reserves. We do not believe that any liabilities that may result from these pending judicial and administrative proceedings are reasonably likely to have a material adverse effect on our financial condition, results of operations or cash flows; however, there can be no assurance that future quarterly or annual operating results will not be materially affected by final resolution of these matters.

Liquidity

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

In our opinion, cash flows from operations and capital resources will be sufficient to meet debt service and working capital needs during fiscal 2011, and thereafter for the foreseeable future. However, we cannot ensure that our business will generate sufficient cash flow from operations or that future borrowings will be available under our credit facilities in amounts sufficient to pay indebtedness or fund other liquidity needs. Actual results of operations will depend on numerous factors, many of which are beyond our control.

Table of Contents

REGULATORY MATTERS

We are subject to local, state, federal and foreign environmental protection laws and regulations with respect to our business operations and believe we are operating in substantial compliance with, or taking actions aimed at ensuring compliance with, such laws and regulations. Apart from the proceedings surrounding the FIFRA compliance matters, which are discussed separately, we are involved in several legal actions with various governmental agencies related to environmental matters. While it is difficult to quantify the potential financial impact of actions involving these environmental matters, particularly remediation costs at waste disposal sites and future capital expenditures for environmental control equipment, in the opinion of management, the ultimate liability arising from such environmental matters, taking into account established reserves, should not have a material adverse effect on our financial position, results of operations or cash flows. However, there can be no assurance that the resolution of these matters will not materially affect our future quarterly or annual results of operations, financial condition or cash flows. Additional information on environmental matters affecting us is provided in Scotts Miracle Gro's Annual Report on Form 10-K for the fiscal year ended September 30, 2010, under **ITEM 1. BUSINESS Regulatory Considerations** and **ITEM 3. LEGAL PROCEEDINGS**.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preceding discussion and analysis of our consolidated results of operations and financial condition should be read in conjunction with our condensed, consolidated financial statements included elsewhere in this Quarterly Report on Form 10-Q. Scotts Miracle-Gro's Annual Report on Form 10-K for the fiscal year ended September 30, 2010, includes additional information about us, our operations, our financial condition, our critical accounting policies and accounting estimates, and should be read in conjunction with this Quarterly Report on Form 10-Q.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risks have not changed significantly from those disclosed in Scotts Miracle-Gro's Annual Report on Form 10-K for the fiscal year ended September 30, 2010.

ITEM 4. CONTROLS AND PROCEDURES

The Scotts Miracle-Gro Company (the Registrant) maintains disclosure controls and procedures, as such term is defined under Exchange Act Rule 13a-15(e), that are designed to ensure that information required to be disclosed in the Registrant's Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the Registrant's management, including its principal executive officer and its principal financial officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, the Registrant's management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and in reaching a reasonable level of assurance, the Registrant's management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

With the participation of the principal executive officer and principal financial officer of the Registrant, the Registrant's management has evaluated the effectiveness of the Registrant's disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)) as of the end of the fiscal quarter covered by this Quarterly Report on Form 10-Q. Based upon that evaluation, the Registrant's principal executive officer and principal financial officer have concluded that the Registrant's disclosure controls and procedures were effective at the reasonable assurance level.

In addition, there were no changes in the Registrant's internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during the Registrant's fiscal quarter ended July 2, 2011 that have materially affected, or are reasonably likely to materially affect, the Registrant's internal control over financial reporting.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Other than as discussed in **NOTE 3. PRODUCT REGISTRATION AND RECALL MATTERS** and **NOTE 12. CONTINGENCIES** of the Notes to Condensed, Consolidated Financial Statements, pending material legal proceedings have not changed significantly since those disclosed in Scotts Miracle-Gro's Annual Report on Form 10-K for the fiscal year ended September 30, 2010.

Table of Contents**ITEM 1A. RISK FACTORS**

The company's risk factors as of July 2, 2011 have not changed materially from those described in ITEM 1A. RISK FACTORS in Scotts Miracle-Gro's Annual Report on Form 10-K for the fiscal year ended September 30, 2010.

Cautionary Note Regarding Forward-Looking Statements

This Quarterly Report on Form 10-Q, including the exhibits hereto and the information incorporated by reference herein, contains

forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, which are subject to risks and uncertainties. Other than statements of historical fact, information regarding activities, events and developments that we expect or anticipate will or may occur in the future, including, but not limited to, information relating to our future growth and profitability targets and strategies designed to increase total shareholder value, are forward-looking statements based on management's estimates, assumptions and projections. Forward-looking statements also include, but are not limited to, statements regarding our future economic and financial condition and results of operations, the plans and objectives of management and our assumptions regarding our performance and such plans and objectives, as well as the amount and timing of repurchases of Scotts Miracle-Gro common shares. These forward-looking statements generally can be identified through the use of words such as guidance, outlook, projected, believe, target, predict, estimate, forecast, strategy, may, goal, expect, anticipate, intend, plan, foresee, likely, will, should and other similar

Forward-looking statements contained in this Quarterly Report on Form 10-Q are predictions only and actual results could differ materially from management's expectations due to a variety of factors, including those described in ITEM 1A. RISK FACTORS in Scotts Miracle-Gro's Annual Report on Form 10-K for the fiscal year ended September 30, 2010. All forward-looking statements attributable to us or persons working on our behalf are expressly qualified in their entirety by such risk factors.

The forward-looking statements that we make in this Quarterly Report on Form 10-Q are based on management's current views and assumptions regarding future events and speak only as of their dates. We disclaim any obligation to update developments of these risk factors or to announce publicly any revisions to any of the forward-looking statements that we make, or to make corrections to reflect future events or developments, except as required by the federal securities laws.

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

The payment of future dividends, if any, on common shares of Scott Miracle-Gro will be determined by the Board of Directors in light of conditions then existing, including the Company's earnings, financial condition and capital requirements, restrictions in financing agreements, business conditions and other factors. The Company's revolving credit facility restricts future dividend payments to an aggregate of \$125 million annually through fiscal year 2013 and \$150 million annually beginning in fiscal year 2014 if the Company's leverage ratio, after giving effect to any such annual dividend payment, exceeds 2.50. The Company's leverage ratio was 1.83 at July 2, 2011. See NOTE 7. DEBT of the Notes to Condensed, Consolidated Financial Statements for further discussion regarding the restrictions on dividend payments.

(c) Issuer Purchases of Equity Securities

The following table shows the purchases of common shares of Scotts Miracle-Gro (Common Shares) made by or on behalf of Scotts Miracle-Gro or any affiliated purchaser (as defined in Rule 10b-18(a)(3) under the Securities Exchange Act of 1934, as amended) of Scotts Miracle-Gro for each fiscal month in the three months ended July 2, 2011:

Period	September 30, Total Number of Common Shares Purchased(1)	September 30, Average Price Paid Per Common Share(2)	September 30, Total Number of Common Shares Purchased as Part of Publicly Announced Plans or Programs(3)	September 30, Approximate Dollar Value of Common Shares That May Yet be Purchased Under the Plans or Programs(3)
April 3 through April 30, 2011	687,401	\$ 57.90	687,300	\$ 541,489,071

Edgar Filing: SCOTTS MIRACLE-GRO CO - Form 10-Q

May 1 through May 28, 2011	722,200	\$	57.97	722,200	\$	499,620,319
May 29 through July 2, 2011	834,322	\$	52.03	832,979	\$	456,283,988
Total	2,243,923	\$	55.74	2,242,479		

Table of Contents

- (1) All of the Common Shares purchased during the quarter were purchased in open market transactions. The total number of Common Shares purchased during the quarter includes 1,444 Common Shares purchased by the trustee of the rabbi trust established by the Company as permitted pursuant to the terms of The Scotts Company LLC Executive Retirement Plan (the ERP). The ERP is an unfunded, non-qualified deferred compensation plan which, among other things, provides eligible employees the opportunity to defer compensation above specified statutory limits applicable to The Scotts Company LLC Retirement Savings Plan and with respect to any Executive Management Incentive Pay (as defined in the ERP), Performance Award (as defined in the ERP) or other bonus awarded to such eligible employees. Pursuant to the terms of the ERP, each eligible employee has the right to elect an investment fund, including a fund consisting of Common Shares (the Scotts Miracle-Gro Common Stock Fund), against which amounts allocated to such employee's account under the ERP, including employer contributions, will be benchmarked (all ERP accounts are bookkeeping accounts only and do not represent a claim against specific assets of the Company). Amounts allocated to employee accounts under the ERP represent deferred compensation obligations of the Company. The Company established the rabbi trust in order to assist the Company in discharging such deferred compensation obligations. When an eligible employee elects to benchmark some or all of the amounts allocated to such employee's account against the Scotts Miracle-Gro Common Stock Fund, the trustee of the rabbi trust purchases the number of Common Shares equivalent to the amount so benchmarked. All Common Shares purchased by the trustee are purchased on the open market and are held in the rabbi trust until such time as they are distributed pursuant to the terms of the ERP. All assets of the rabbi trust, including any Common Shares purchased by the trustee, remain, at all times, assets of the Company, subject to the claims of its creditors. The terms of the ERP do not provide for a specified limit on the number of Common Shares that may be purchased by the trustee of the rabbi trust.
- (2) The average price paid per Common Share is calculated on a settlement basis and excludes commissions.
- (3) In August 2010, the Scotts Miracle-Gro Board of Directors authorized the repurchase of up to \$500 million of the Common Shares over a four-year period (through September 30, 2014). On May 4, 2011, the Scotts Miracle-Gro Board of Directors authorized the repurchase of up to an additional \$200 million of the Common Shares, resulting in authority to repurchase up to a total of \$700 million of the Common Shares through September 30, 2014. The dollar amounts in the Approximate Dollar Value column reflect the total \$700 million authorized repurchase program.

ITEM 6. EXHIBITS

See Index to Exhibits at page 44 for a list of the exhibits included herewith.

Table of Contents

SIGNATURES

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

Date: August 10, 2011

THE SCOTTS MIRACLE-GRO COMPANY

/s/ DAVID C. EVANS

David C. Evans

Chief Financial Officer and Executive Vice President,

Strategy and Business Development

(Principal Financial and Principal Accounting Officer)

(Duly Authorized Officer)

Table of Contents

THE SCOTTS MIRACLE-GRO COMPANY

QUARTERLY REPORT ON FORM 10-Q

FOR THE QUARTERLY PERIOD ENDED JULY 2, 2011

INDEX TO EXHIBITS

EXHIBIT NO.	DESCRIPTION	LOCATION
4.1	Second Amended and Restated Credit Agreement, dated as of June 30, 2011, by and among The Scotts Miracle-Gro Company as the "Borrower" the Subsidiary Borrowers (as defined in the Second Amended and Restated Credit Agreement); the several banks and other financial institutions from time to time parties to the Second Amended and Restated Credit Agreement (the "Lenders"); Bank of America, N.A., as Syndication Agent; Cobank, ACB, BNP Paribas, Credit Agricole Corporate and Investment Bank, Rabobank Nederland, Citizens Bank of Pennsylvania, The Bank of Nova Scotia and Wells Fargo Bank, N.A., as Documentation Agents; and JPMorgan Chase Bank, N.A., as Administrative Agent	Incorporated herein by reference to the Current Report on Form 8-K of The Scotts Miracle-Gro Company (the Registrant) filed July 1, 2011 (File No. 1-11593) [Exhibit 4.1]
4.2	Second Amended and Restated Guarantee and Collateral Agreement, dated as of June 30, 2011, made by The Scotts Miracle-Gro Company, each domestic Subsidiary Borrower under the Second Amended and Restated Credit Agreement, and certain of its and their domestic subsidiaries, in favor of JPMorgan Chase Bank, N.A., as Administrative Agent	Incorporated herein by reference to the Registrant's Current Report on Form 8-K filed July 1, 2011 (File No. 1-11593) [Exhibit 4.2]
10.1	The Scotts Company LLC Executive Severance Plan, adopted on May 4, 2011	Incorporated herein by reference to the Registrant's Current Report on Form 8-K filed May 10, 2011 (File No. 1-11593) [Exhibit 10.1]
10.2	Form of Tier 1 Participation Agreement under The Scotts Company LLC Executive Severance Plan	Incorporated herein by reference to the Registrant's Current Report on Form 8-K filed May 10, 2011 (File No. 1-11593) [Exhibit 10.2]
10.3	Second Amendment to Employment Agreement, effective as of June 27, 2011, by and between The Scotts Company LLC and Barry Sanders	Incorporated herein by reference to the Registrant's Current Report on Form 8-K filed June 30, 2011 (File No. 1-11593) [Exhibit 10.3]
10.4	First Amendment to Employment Agreement, effective as of June 27, 2011, by and between The Scotts Company LLC and David C. Evans	Incorporated herein by reference to the Registrant's Current Report on Form 8-K filed June 30, 2011 (File No. 1-11593) [Exhibit 10.5]

Table of Contents

10.5	Second Amendment, dated as of May 10, 2011, to the Master Accounts Receivable Purchase Agreement, dated as of May 1, 2009, among The Scotts Company LLC as the Company, The Scotts Miracle-Gro Company as the Parent and Credit Agricole Corporate and Investment Bank New York Branch (formerly known as Calyon New York Branch) as the Bank	Incorporated herein by reference to the Registrant's Quarterly Report on Form 10-Q for the quarterly period ended April 2, 2011 (File No. 1-11593) [Exhibit 10.7]
31.1	Rule 13a-14(a)/15d-14(a) Certifications (Principal Executive Officer)	*
31.2	Rule 13a-14(a)/15d-14(a) Certifications (Principal Financial Officer)	*
32	Section 1350 Certifications (Principal Executive Officer and Principal Financial Officer)	*
101.INS**	XBRL Instance Document	*
101.SCH**	XBRL Taxonomy Extension Schema	*
101.CAL**	XBRL Taxonomy Extension Calculation Linkbase	*
101.DEF**	XBRL Taxonomy Extension Definition Linkbase	*
101.LAB**	XBRL Taxonomy Extension Label Linkbase	*
101.PRE**	XBRL Taxonomy Extension Presentation Linkbase	*

* Included herewith

** Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933 or Section 18 of the Securities Exchange Act of 1934 and otherwise are not subject to liability.