Spectrum Brands, Inc.
Form 10-Q
August 10, 2007
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended July 1, 2007

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 001-13615

Spectrum Brands, Inc.

(Exact name of registrant as specified in its charter)

Wisconsin	**22-2423556**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**
Six Concourse Parkway,	
Suite 3300, Atlanta, Georgia	**30328**

(Address of principal executive offices) **(Zip Code)**

(770) 829-6200

(Registrant s telephone number, including area code)

N/A

(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 x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

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

The number of shares outstanding of the Registrant s common stock, $.01 par value, as of August 4, 2007, was 53,011,521.

Table of Contents

SPECTRUM BRANDS, INC.

QUARTERLY REPORT ON FORM 10-Q

FOR QUARTER ENDED July 1, 2007

INDEX

		Page
	Part I Financial Information	
Item 1.	Financial Statements	3
	Condensed Consolidated Balance Sheets (Unaudited) as of July 1, 2007 and September 30, 2006	3
	Condensed Consolidated Statements of Operations (Unaudited) for the three and nine month periods ended July 1, 2007 and July 2, 2006	4
	Condensed Consolidated Statements of Cash Flows (Unaudited) for the nine month periods ended July 1, 2007 and July 2, 2006	5
	Notes to Condensed Consolidated Financial Statements (Unaudited)	6
Item 2.	Management s Discussion and Analysis of Financial Condition and Results of Operations	33
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	47
Item 4.	Controls and Procedures	48
	Part II Other Information	
Item 1.	Legal Proceedings	49
Item 1A.	Risk Factors	49
Item 2.	Issuer Purchases of Equity Securities	61
Item 4.	Submission of Matters to a Vote of Security Holders	61
Item 5.	Other Information	61
Item 6.	Exhibits	64
Signatures		65

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

SPECTRUM BRANDS, INC.

Condensed Consolidated Balance Sheets

July 1, 2007 and September 30, 2006

(Unaudited)

(Amounts in thousands, except per share figures)

	July 1, 2007	September 30, 2006
-ASSETS-		
Current assets:		
Cash and cash equivalents	$ 176,200	$ 28,430
Receivables, less allowance for doubtful accounts of $18,826 and $21,394, respectively	293,891	365,532
Inventories	333,072	460,672
Assets held for sale	849,676	3,499
Deferred income taxes	42,370	50,401
Prepaid expenses and other	46,988	51,281
Total current assets	1,742,197	959,815
Property, plant and equipment, net	260,540	311,839
Goodwill	641,034	1,130,184
Intangible assets, net	843,659	1,061,087
Deferred charges and other	43,299	49,028
Debt issuance costs	47,765	37,367
Total assets	$ 3,578,494	$ 3,549,320
-LIABILITIES AND SHAREHOLDERS EQUITY-		
Current liabilities:		
Current maturities of long-term debt	$ 48,498	$ 42,713
Accounts payable	186,234	309,111
Liabilities held for sale	84,691	
Accrued liabilities	224,575	210,789
Total current liabilities	543,998	562,613
Long-term debt, net of current maturities	2,606,096	2,234,458
Employee benefit obligations, net of current portion	73,257	76,893
Deferred income taxes	64,703	156,578
Other	67,588	66,561
Total liabilities	3,355,642	3,097,103
Shareholders equity:		
Common stock, $.01 par value, authorized 150,000 shares; issued 68,464 and 67,422 shares, respectively; outstanding 52,168 and 51,491 shares, respectively	682	674
Additional paid-in capital	670,290	651,644
Accumulated deficit	(430,370)	(166,657)

Accumulated other comprehensive income	58,333	39,639
	298,935	525,300
Less treasury stock, at cost, 16,296 and 15,931 shares, respectively	(76,083)	(73,083)
Total shareholders equity	222,852	452,217
Total liabilities and shareholders equity	$ 3,578,494	$ 3,549,320

See accompanying notes which are an integral part of these condensed consolidated financial statements (Unaudited).

Table of Contents

SPECTRUM BRANDS, INC.

Condensed Consolidated Statements of Operations

For the three and nine month periods ended July 1, 2007 and July 2, 2006

(Unaudited)

(Amounts in thousands, except per share figures)

	THREE MONTHS		NINE MONTHS	
	2007	2006	2007	2006
Net sales	$ 442,000	$ 427,517	$ 1,446,286	$ 1,408,459
Cost of goods sold	273,718	268,452	891,849	864,833
Restructuring and related charges	4,116	2,708	16,731	4,435
Gross profit	164,166	156,357	537,706	539,191
Selling	94,896	94,263	319,781	292,449
General and administrative	33,034	40,282	115,165	119,925
Research and development	6,052	7,150	19,662	21,517
Goodwill impairment			214,039	
Restructuring and related charges	26,532	4,144	37,738	9,127
Total operating expenses	160,514	145,839	706,385	443,018
Operating income (loss)	3,652	10,518	(168,679)	96,173
Interest expense	41,149	31,364	142,120	91,049
Other expense (income), net	914	(131)	4,513	(5,230)
(Loss) income from continuing operations before income taxes	(38,411)	(20,715)	(315,312)	10,354
Income tax (benefit) expense	(8,249)	(5,751)	(57,404)	3,746
(Loss) income from continuing operations	(30,162)	(14,964)	(257,908)	6,608
Income (loss) from discontinued operations, net of tax	22,774	17,509	(5,805)	(1,183)
Net (loss) income	$ (7,388)	$ 2,545	$ (263,713)	$ 5,425
Basic earnings per share:				
Weighted average shares of common stock outstanding	50,753	49,456	50,827	49,458
(Loss) income from continuing operations	$ (0.60)	$ (0.30)	$ (5.08)	$ 0.13
Income (loss) from discontinued operations	0.45	0.35	(0.11)	(0.02)
Net (loss) income	$ (0.15)	$ 0.05	$ (5.19)	$ 0.11
Diluted earnings per share:				
Weighted average shares and equivalents outstanding	50,753	51,854	50,827	50,959
(Loss) income from continuing operations	$ (0.60)	$ (0.29)	$ (5.08)	$ 0.13
Income (loss) from discontinued operations	0.45	0.34	(0.11)	(0.02)
Net (loss) income	$ (0.15)	$ 0.05	$ (5.19)	$ 0.11

See accompanying notes which are an integral part of these condensed consolidated financial statements (Unaudited).

Table of Contents

SPECTRUM BRANDS, INC.

Condensed Consolidated Statements of Cash Flows

For the nine month periods ended July 1, 2007 and July 2, 2006

(Unaudited)

(Amounts in thousands)

	NINE MONTHS 2007	NINE MONTHS 2006
Cash flows from operating activities:		
(Loss) income from continuing operations	$ (257,908)	$ 6,608
Non-cash adjustments to income from continuing operations:		
Gain on sale of assets		(8,876)
Depreciation	31,819	30,929
Amortization	28,868	22,405
Amortization of debt issuance costs	5,816	4,976
Impairment of goodwill	214,039	
Other non-cash adjustments	(4,329)	29,030
Net changes in assets and liabilities, net of acquisitions and discontinued operations	(87,183)	(52,474)
Net cash (used) provided by operating activities of continuing operations	(68,878)	32,598
Net cash used by operating activities of discontinued operations	(79,504)	(24,293)
Net cash (used) provided by operating activities	(148,382)	8,305
Cash flows from investing activities:		
Purchases of property, plant and equipment	(18,422)	(46,897)
Proceeds from sale of equipment	486	5,379
Proceeds from sale of assets held for sale		10,641
Payment for acquisitions, net of cash acquired		(14,856)
Net cash used by investing activities of continuing operations	(17,936)	(45,733)
Net cash provided by investing activities of discontinued operations		80,171
Net cash (used) provided by investing activities	(17,936)	34,438
Cash flows from financing activities:		
Reduction of debt	(1,826,363)	(741,643)
Proceeds from debt financing	2,178,729	686,996
Debt issuance costs	(40,790)	(5,236)
Proceeds from exercise of stock options		365
Stock option income tax benefit		80
Net cash provided (used) by financing activities	311,576	(59,438)
Effect of exchange rate changes on cash and cash equivalents	2,512	(22)
Net increase (decrease) in cash and cash equivalents	147,770	(16,717)
Cash and cash equivalents, beginning of period	28,430	29,852
Cash and cash equivalents, end of period	$ 176,200	$ 13,135

See accompanying notes which are an integral part of these condensed consolidated financial statements (Unaudited).

5

Table of Contents

SPECTRUM BRANDS, INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

(Amounts in thousands, except per share figures)

1 DESCRIPTION OF BUSINESS

Spectrum Brands, Inc. and its subsidiaries (the Company) is a global branded consumer products company with positions in seven major product categories: consumer batteries; pet supplies; lawn and garden care; electric shaving and grooming; household insect control; electric personal care; and portable lighting. In the third quarter of the Company s fiscal year ended September 30, 2006, the Company engaged advisors to assist it with a potential sale of various assets in order to reduce its outstanding indebtedness. In connection with this undertaking, during the first quarter of fiscal 2007 the Company approved and initiated a plan to sell the assets related to its lawn and garden and household insect control product offerings (the Home and Garden Business). As a result, the Company has designated certain assets and liabilities related to its Home and Garden Business as held for sale and has designated the Home and Garden Business as a discontinued operation (for additional information see footnote 2, Significant Accounting Policies Discontinued Operations and footnote 2, Significant Accounting Policies Assets Held for Sale).

As of January 1, 2007, the Company began managing its business in three reportable segments: (i) Global Batteries & Personal Care, which consists of the Company s worldwide battery, shaving and grooming, personal care and portable lighting business (Global Batteries & Personal Care); (ii) Global Pet Supplies, which consists of the Company s worldwide pet supplies business (Global Pet Supplies); and (iii) Home and Garden, which consists of the discontinued Home and Garden Business (Home and Garden). The presentation of all historical segment reporting herein has been reclassified to conform to this segment structure.

The Company s continuing operations include the worldwide manufacturing and marketing of alkaline, zinc carbon and hearing aid batteries, as well as aquariums and aquatic health supplies and designing and marketing of rechargeable batteries, battery-powered lighting products, electric shavers and accessories, grooming products and hair care appliances. The Company s continuing operations also include the manufacturing and marketing of specialty pet supplies. The Company s continuing operations utilize manufacturing and product development facilities located in the United States, Europe, China and Latin America. Through the Company s Home and Garden Business, presented here as discontinued operations, it manufactures and markets lawn fertilizers, herbicides, insecticides and repellants in North America.

The Company sells its products in approximately 120 countries through a variety of trade channels, including retailers, wholesalers and distributors, hearing aid professionals, industrial distributors and original equipment manufacturers (OEMs) and enjoys name recognition in its markets under the Rayovac, VARTA and Remington brands, each of which has been in existence for more than 80 years, and under the Tetra, 8in1 and various other brands. The Company s Home and Garden Business enjoys name recognition under the Spectracide and Cutter brands, among others. Due to business seasonality, the Company s operating results for the three and nine month periods ended July 1, 2007 are not necessarily indicative of the results that may be expected for the full year ending September 30, 2007.

2 SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation: These condensed consolidated financial statements have been prepared by the Company, without audit, pursuant to the rules and regulations of the United States Securities and Exchange Commission (the SEC) and, in the opinion of the Company, include all adjustments (which are normal and recurring in nature) necessary to present fairly the financial position of the Company at July 1, 2007, and the results of operations and cash flows for the three and nine month periods ended July 1, 2007 and July 2, 2006. Certain information and footnote disclosures normally included in consolidated financial statements prepared in

Table of Contents

accordance with generally accepted accounting principles in the United States of America have been condensed or omitted pursuant to such SEC rules and regulations. These condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company s Annual Report on Form 10-K for the fiscal year ended September 30, 2006. Certain prior period amounts have been reclassified to conform to the current period presentation. The condensed consolidated financial statements included in this Form 10-Q have been adjusted to reflect the planned disposition of certain assets as discontinued operations for all periods presented.

Significant Accounting Policies and Practices: The condensed consolidated financial statements include the condensed consolidated financial statements of Spectrum Brands, Inc. and its subsidiaries and are prepared in accordance with generally accepted accounting principles in the United States of America. All intercompany transactions have been eliminated. The Company s fiscal year ends September 30. References herein to 2007 and 2006 refer to the fiscal years ended September 30, 2007 and 2006, respectively.

The preparation of condensed consolidated financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Discontinued Operations: In the third quarter of the Company s fiscal year ended September 30, 2006, the Company engaged advisors to assist it with a sale of various assets in order for the Company to reduce its outstanding indebtedness. In connection with this undertaking, during the first quarter of fiscal 2007, the Company approved and initiated a plan to sell the assets related to its Home and Garden Business. (See Assets Held for Sale in Note 2 below where the specific assets and liabilities to be sold are further discussed.)

As a result, effective October 1, 2006, the Company reflected the operations of its Home and Garden Business as discontinued operations. The following amounts have been segregated from continuing operations and are reflected as discontinued operations for the three and nine month periods ended July 1, 2007 and July 2, 2006, respectively:

	Three Months		Nine Months	
	2007	**2006**	**2007**	**2006**
Net sales	$ 258,395	$ 270,752	$ 534,269	$ 534,890
Income (loss) from discontinued operations before income taxes	$ 24,495	$ 24,156	$ (12,398)	$ 5,653
Provision for income tax expense (benefit)	1,721	6,647	$ (6,593)	1,556
Income (loss) from discontinued operations, net of tax	$ 22,774	$ 17,509	$ (5,805)	$ 4,097

On January 25, 2006, the Company sold its Nu-Gro fertilizer technology and Canadian professional fertilizer products businesses (Nu-Gro Pro and Tech) to Agrium Inc. Proceeds from the sale were used to reduce outstanding debt. The sale included two divisions of Spectrum Brands Nu-Gro subsidiary, representing fiscal 2005 revenue of approximately $80,000 from sales of high-end specialty controlled-release nitrogen fertilizer and other products to professional turf markets and specialty wholesale fertilizer customers. As part of the transaction, the Company signed multi-year reciprocal supply agreements with Agrium. Proceeds from the sale totaled approximately $83,000 after selling expenses and contractual working capital adjustments which were finalized on October 30, 2006.

Effective October 1, 2005, the Company reflected the operations of Nu-Gro Pro and Tech as discontinued operations. The Company discontinued these operations as part of its integration initiatives related to the Company s acquisition of United Industries Corporation (United). See footnote 10, Restructuring and Related

Table of Contents

Charges, for additional discussion of United integration initiatives. The following amounts have been segregated from continuing operations and are reflected as discontinued operations for the nine month period ended July 2, 2006:

	Nine Months 2006[A]
Net sales	$ 16,314
Loss from discontinued operations before income taxes	$ (6,106)
Provision for income tax benefit	826
Loss from discontinued operations (including estimated loss on disposal of $3,788), net of tax[B]	$ (5,280)

(A) The nine month period ended July 2, 2006 represents results for the discontinued operations for October 2005 through January 2006.

(B) After selling expenses and contractual working capital adjustments were finalized on October 30, 2006, the loss on disposal was adjusted to $3,901. The adjustment to the loss on disposal was recognized in the fourth quarter of fiscal 2006.

Assets Held for Sale: At July 1, 2007, assets totaling $849,676 were included in Assets held for sale in the Condensed Consolidated Balance Sheets (Unaudited). At July 1, 2007, the Company had $841,812 and $84,691 related to certain assets and liabilities, respectively, of the Company s Home and Garden Business included in Assets held for sale and Liabilities held for sale, respectively, in its Condensed Consolidated Balance Sheets (Unaudited). (See Discontinued Operations in this Note 2 above for additional information). All relevant criteria of Statement of Financial Accounting Standards No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, allowing for the classification of assets held for sale have been met for the assets and liabilities of the Home and Garden Business. The following table details the components of the assets and liabilities related to the Company s Home and Garden Business held for sale at July 1, 2007:

	Amount
Receivables, net of allowance for doubtful accounts	$ 135,504
Inventories	130,894
Other current assets	5,397
Property, plant and equipment, net	43,258
Goodwill	298,576
Intangible assets, net	225,405
Other assets	2,778
Total assets held for sale	841,812
Accounts payable	59,585
Other current liabilities	25,106
Total liabilities held for sale	84,691
Total Home and Garden net assets held for sale	$ 757,121

The remaining balance in Assets held for sale in the Condensed Consolidated Balance Sheets (Unaudited) as of July 1, 2007 and the balance as of September 30, 2006 consist primarily of a distribution facility in the Dominican Republic and manufacturing facilities in France and Brazil.

Intangible Assets: Intangible assets are recorded at cost or at fair value if acquired in a purchase business combination. Customer lists and proprietary technology intangibles are amortized, using the straight-line method, over their estimated useful lives of approximately 5 to 19 years. Excess of cost over fair value of net assets acquired (goodwill) and trade name intangibles are not amortized. Goodwill is tested for impairment at least

8

annually at the reporting unit level. If an impairment is indicated, a write-down to fair value (normally measured by discounting estimated future cash flows) is recorded. Trade name intangibles are tested for impairment at least annually by comparing the fair value with the carrying value. Any excess of carrying value over fair value is recognized as an impairment loss in income from operations.

Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets* (SFAS 142) requires that goodwill and indefinite-lived intangible assets be tested for impairment annually, or more often if an event or circumstance indicates that an impairment loss may have been incurred. The fair values of the Company s goodwill and indefinite-lived intangible assets were tested as of April 1, 2007.

In accordance with SFAS 142, the Company, with the assistance of independent third party valuation specialists, conducted impairment testing on the Company s goodwill. The Company used the discounted estimated future cash flows methodology to determine the fair value of its reporting units. Assumptions critical to the Company s fair value estimates were: (i) the present value factors used in determining the fair value of the reporting units and trade names; (ii) royalty rates used in the Company s trade name valuations; (iii) projected average revenue growth rates used in the reporting unit and trade name models; and (iv) projected long-term growth rates used in the derivation of terminal year values. These and other assumptions are impacted by economic conditions and expectations of management and will change in the future based on period specific facts and circumstances. The Company also tested fair value for reasonableness by comparison to the market capitalization of the Company. The Company first compared the fair value of its reporting units with their carrying amounts, including goodwill. This first step indicated that the fair value of the Company s North America reporting unit, which is included in the Global Batteries & Personal Care operating segment, was less than the Company s North America reporting unit s carrying amount and, accordingly, further testing of goodwill was required to determine the impairment charge required by SFAS 142.

Management then compared the carrying amount of the North America reporting unit s goodwill against the respective implied fair value of goodwill. The carrying amount of the North America reporting unit s goodwill was determined to exceed implied fair value and, therefore, management recorded an impairment charge equal to the excess of the carrying amount of the reporting unit s goodwill over the implied fair value of such goodwill. As a result of this goodwill impairment analysis, the Company recorded a non-cash pretax goodwill impairment charge of approximately $214,039.

In addition, in accordance with SFAS 142, the Company, with the assistance of independent third party valuation specialists, also compared the carrying amounts of trade name intangible assets with their respective fair values. Fair value was determined using a relief from royalty methodology. Management concluded that the fair values of the trade name intangible assets were in excess of their respective carrying amounts and, hence, such assets were not impaired.

The recognition of the $214,039 non-cash impairment of goodwill, recorded as a separate component of Operating expenses, has had a material negative effect on the Company s financial condition and results of operations for the nine month period ended July 1, 2007. The impairment will not result in future cash expenditures.

Management uses its judgment in assessing whether assets may have become impaired between annual impairment tests. Indicators such as unexpected adverse business conditions, economic factors, unanticipated technological change or competitive activities, loss of key personnel, and acts by governments and courts may signal that an asset has become impaired. The impairment of goodwill discussed above is primarily attributed to lower forecasted profits of the North America reporting unit, reflecting more conservative future growth rates, coupled with an increase in its carrying value during the six months ended April 1, 2007.

Shipping and Handling Costs: The Company incurred shipping and handling costs of $30,865 and $99,623 for the three and nine month periods ended July 1, 2007, respectively, and $27,819 and $87,353 for the three and

Table of Contents

nine month periods ended July 2, 2006, respectively. These costs are included in Selling expenses. Shipping and handling costs include costs incurred with third-party carriers to transport products to customers as well as salaries and overhead costs related to activities to prepare the Company s products for shipment from its distribution facilities.

Concentrations of Credit Risk: Trade receivables subject the Company to credit risk. Trade accounts receivable are carried at net realizable value. The Company extends credit to its customers based upon an evaluation of the customer s financial condition and credit history, but generally does not require collateral. The Company monitors its customers credit and financial condition based on changing economic conditions and will make adjustments to credit policies as required. Provision for losses on uncollectible trade receivables are determined principally on the basis of past collection experience applied to ongoing evaluations of the Company s receivables and evaluations of the risks of nonpayment for a given customer.

The Company has a broad range of customers including many large retail outlet chains, one of which accounts for a significant percentage of its sales volume. This customer represented approximately 19% and 20% of the Company s Net sales during the three and nine month periods ended July 1, 2007, respectively, and 21% and 22% of the Company s Net sales during the three and nine month periods ended July 2, 2006, respectively. This major customer also represented approximately 16% and 11% of its trade accounts receivable, net as of July 1, 2007 and September 30, 2006, respectively.

Approximately 58% of the Company s sales during the nine month period ended July 1, 2007 occurred outside the United States. These sales and related receivables are subject to varying degrees of credit, currency, political and economic risk. The Company monitors these risks and makes appropriate provisions for collectibility based on an assessment of the risks present.

Stock-Based Compensation: On October 1, 2005 the Company adopted Statement of Financial Accounting Standards 123(R) (SFAS 123(R)) requiring the Company to recognize expense related to the fair value of its employee stock option awards. The Company recognizes the cost of all share-based awards on a straight-line basis over the vesting period of the award. Total stock compensation expense associated with both stock options and restricted stock awards recognized by the Company during the three and nine month periods ended July 1, 2007 was $10,030 and $18,656, or $6,720 and $12,500, net of taxes, respectively. The amounts before tax are included in Total operating expenses within General and administrative expenses and Restructuring and related charges in the Condensed Consolidated Statements of Operations (Unaudited). See footnote 10, Restructuring and related charges, for further detail regarding our restructuring and related charges. The Company expects that total stock compensation expense for 2007 will be approximately $21,000 before the effect of income taxes. As of July 1, 2007, there was $21,756 of unrecognized compensation cost related to restricted stock that is expected to be recognized over a weighted average period of approximately 3 years.

The Company uses or has used two forms of stock based compensation. Shares of restricted stock have been awarded to certain employees and members of management since fiscal 2001. Prior to the fourth quarter of fiscal 2004, the Company also issued stock options to employees, some of which remained unvested at the adoption date of SFAS 123(R). Restricted stock is now the only form of stock based compensation used by the Company.

Stock options previously awarded generally vest under a combination of time-based and performance-based vesting criteria. Under the time-based vesting, the stock options become exercisable primarily in equal increments over a three year period, while under the performance-based vesting such options become exercisable over the same time period or one day prior to the end of the exercise period, if certain performance criteria are not met.

Restricted stock shares granted through fiscal 2006 generally have vesting periods of three to five years. Approximately 50% of the restricted stock shares are purely time-based and vest on a pro rata basis over either a three or four year vesting period and the remaining 50% are time-based and performance-based. Vesting of such performance based restricted stock will occur upon achievement of certain performance goals established by

Table of Contents

the Board of Directors of the Company. Generally, performance targets consist of Earnings Per Share (EPS), segment Earnings Before Interest and Taxes (EBIT) and cash flow components. If such performance targets are not met, the performance component of a restricted stock award will not vest in the year that the performance targets applied to and instead will automatically vest one year after the originally scheduled vesting date, effectively making the award time based. The Company recognizes amortization on the time-based component on a straight-line basis over the vesting period. The Company recognizes amortization on the performance-based component over the vesting period, assuming performance targets will not be met, unless and until it is probable that the performance targets will be met. At the point in time when it is probable that the performance target will be met, the recognition period is shortened one year to account for the accelerated vesting requirement of the performance-based component.

During the nine month period ended July 1, 2007, the Company granted approximately 1,163 shares of restricted stock. Of these grants, 194 shares are time-based and vest on a pro rata basis over a three year period and 969 shares are purely performance-based and vest only upon achievement of certain performance goals. Such performance goals consist of reportable segment and consolidated company Earnings Before Interest Taxes Depreciation and Amortization (EBITDA) and cash flow components. During the three month period ended April 1, 2007 achievement of the performance goals related to the performance-based shares was deemed probable and, accordingly, amortization related to those shares is included in stock compensation expense for the three and nine month periods ended July 1, 2007 disclosed above.

The Company currently has two active incentive plans under which additional shares may be issued to employees as equity compensation. In 1997, the Board adopted the 1997 Rayovac Incentive Plan (1997 Plan). Up to 5,000 shares of Common stock may be issued under the 1997 Plan, which expires on August 31, 2007. As of July 1, 2007, there were options with respect to 1,455 shares of common stock outstanding under the 1997 Plan. In 2004, the Board adopted the 2004 Rayovac Incentive Plan (2004 Plan). The 2004 Plan supplements the 1997 Plan. Up to 3,500 shares of common stock may be issued under the 2004 Plan, which expires in July 2014. As of July 1, 2007, 3,369 restricted shares had been granted under the 2004 Plan. No options have been granted under the 2004 Plan. The fair value of restricted stock is determined based on the market price of the Company s shares on the grant date. A summary of the status of the Company s non-vested restricted stock as of July 1, 2007, and changes during the nine month period ended July 1, 2007, is as follows:

Restricted Stock	Shares	Weighted Average Grant Date Fair Value	Fair Value
Restricted stock at September 30, 2006	2,046	$ 25.91	$ 53,021
Granted	1,163	8.61	10,014
Vested	(1,270)	19.37	(24,599)
Forfeited	(121)	24.43	(2,966)
Restricted stock at July 1, 2007	1,818	$ 19.51	$ 35,470

The following table summarizes the stock option transactions for the nine month period ended July 1, 2007:

Stock Options	Shares	Weighted Average Price	Aggregate Intrinsic Value
Outstanding at September 30, 2006	1,911	$ 14.65	$
Granted			
Exercised			
Forfeited	(85)	14.36	
Outstanding at July 1, 2007	1,826	$ 14.66	$
Exercisable at July 1, 2007	1,642	$ 14.78	$

Table of Contents

The following table summarizes information about options outstanding and options outstanding and exercisable as of July 1, 2007:

Range of Exercise Prices	Options Outstanding: Number of Shares	Options Outstanding: Weighted-Average Remaining Contractual Life	Options Outstanding: Weighted-Average Exercise Price	Options Outstanding and Exercisable: Number of Shares	Options Outstanding and Exercisable: Weighted-Average Exercise Price
$4.39	149	0.25 years	$ 4.39	149	$ 4.39
$11.32 $14.60	1,203	4.87	13.43	1,030	13.53
$16.19 $21.50	205	1.17	18.75	202	18.73
$21.63 $28.70	269	1.99	22.72	261	22.57
	1,826	3.66	$ 14.66	1,642	$ 14.78

Derivative Financial Instruments: Derivative financial instruments are used by the Company principally in the management of its interest rate, foreign currency and raw material price exposures. The Company does not hold or issue derivative financial instruments for trading purposes. When entered into, the Company formally designates the derivative financial instrument as a hedge of a specific underlying exposure if such criteria are met, and documents both the risk management objectives and strategies for undertaking the hedge. The Company formally assesses, both at the inception and at least quarterly thereafter, whether the derivative financial instruments that are used in hedging transactions are effective at offsetting changes in either the fair value or cash flows of the related underlying exposure. Because of the high correlation between the derivative financial instrument and the underlying exposure being hedged, fluctuations in the value of the derivative financial instruments are generally offset by changes in the fair values or cash flows of the underlying exposures being hedged. Any ineffective portion of a derivative financial instrument s change in fair value is immediately recognized in earnings.

The Company uses interest rate swaps to manage its interest rate risk. The swaps are designated as cash flow hedges with the changes in fair value recorded in Accumulated other comprehensive income (AOCI) and as a derivative hedge asset or liability, as applicable. The swaps settle periodically in arrears with the related amounts for the current settlement period payable to, or receivable from, the counter-parties included in accrued liabilities or accounts receivable and recognized in earnings as an adjustment to interest expense from the underlying debt to which the swap is designated. During the three month periods ended July 1, 2007 and July 2, 2006, $2,047 and $667 of pretax derivative gains, respectively, from such hedges were recorded as an adjustment to Interest expense. During the three month periods ended July 1, 2007 and July 2, 2006, ineffectiveness from such hedges was $0. During the three month period ended July 1, 2007, $1,150 of pretax derivative gains were recorded as an adjustment to Interest expense from early termination of a Euro-denominated interest rate swap. The hedge was terminated in connection with a reduction in Euro-denominated debt that also occurred in the quarter. During the nine month periods ended July 1, 2007 and July 2, 2006, $5,792 and $502 of pretax derivative gains, respectively, from such hedges were recorded as an adjustment to Interest expense. During the nine month periods ended July 1, 2007 and July 2, 2006, $0 and $431 of pretax derivative gains, respectively, were recorded as adjustments to Interest expense for ineffectiveness from such hedges and included in the amounts listed above.

At July 1, 2007, the Company had a portfolio of United States Dollar (USD) denominated interest rate swaps outstanding which effectively fixes the interest rates on floating rate debt, exclusive of lender spreads, at rates as follows: 4.15% for a notional principal amount of $175,000 through September 2007, 4.46% for a notional principal amount of $170,000 through October 2008 and 5.49% for a notional principal amount of $225,000 through March 2010. In addition, the Company had a portfolio of EUR-denominated interest rate swaps outstanding which effectively fixes the interest rates on floating rate debt, exclusive of lender spreads, at rates as follows: 2.68% for a notional principal amount of 50,000 through September 2007 and 2.68% for a

Table of Contents

notional principal amount of 185,000 through September 2008. The derivative net gain on these contracts recorded in AOCI at July 1, 2007 was $5,124, net of tax expense of $3,141. The derivative net gain on these contracts recorded in AOCI at September 30, 2006 was $6,385, net of tax expense of $3,913. At July 1, 2007, the portion of derivative net gains estimated to be reclassified from AOCI into earnings over the next 12 months is $2,394, net of tax.

The Company periodically enters into forward foreign exchange contracts to hedge the risk from forecasted foreign denominated third party and intercompany sales or payments. These obligations generally require the Company to exchange foreign currencies for U.S. Dollars, Euros, Pounds Sterling, Australian Dollars, Brazilian Reals, Canadian Dollars or Japanese Yen. These foreign exchange contracts are cash flow hedges of fluctuating foreign exchange related to sales or product or raw material purchases. Until the sale or purchase is recognized, the fair value of the related hedges is recorded in AOCI and as a derivative hedge asset or liability, as applicable. At the time the sale or purchase is recognized, the fair value of the related hedge is reclassified as an adjustment to Net sales or purchase price variance in Cost of goods sold. During the three month periods ended July 1, 2007 and July 2, 2006, $106 and $4, respectively, of pretax derivative gains and losses, from such hedges were recorded as an adjustment to Net sales. During the nine month periods ended July 1, 2007 and July 2, 2006, $644 and $4, respectively, of pretax derivative gains and losses from such hedges were recorded as an adjustment to Net sales. During the three month periods ended July 1, 2007 and July 2, 2006, $1,294 and $384 of pretax derivative losses, respectively, from such hedges were recorded as an adjustment to Cost of good sold. During the nine month periods ended July 1, 2007 and July 2, 2006, $1,843 and $221 of pretax derivative losses, respectively, from such hedges were recorded as an adjustment to Cost of good sold. Following the sale or purchase, subsequent changes in the fair value of the derivative hedge contracts are recorded as a gain or loss in earnings as an offset to the change in value of the related asset or liability recorded in the Condensed Consolidated Balance Sheet (Unaudited). During the three month periods ended July 1, 2007 and July 2, 2006, $390 and $133 of pretax derivative losses, respectively, from such hedges were recorded as an adjustment to earnings in Other income, net. During the nine month periods ended July 1, 2007 and July 2, 2006, $1,146 and $59 of pretax derivative losses, respectively, from such hedges were recorded as an adjustment to earnings in Other income, net. The pretax derivative adjustment to earnings for ineffectiveness from these contracts for the three month periods ended July 1, 2007 and July 2, 2006 was $0. The pretax derivative adjustment to earnings for ineffectiveness from these contracts for the nine month periods ended July 1, 2007 and July 2, 2006 was $0. At July 1, 2007 and September 30, 2006, respectively, the Company had $142,449 and $97,932 of such foreign exchange derivative contracts outstanding. The derivative net loss on these contracts recorded in AOCI at July 1, 2007 was $2,541, net of tax benefit of $1,310. The derivative net gain on these contracts recorded in AOCI at September 30, 2006 was $647, net of tax expense of $326. At July 1, 2007, the portion of derivative net losses estimated to be reclassified from AOCI into earnings over the next 12 months is $1,978, net of tax.

The Company periodically enters into forward and swap foreign exchange contracts to hedge the risk from third party and intercompany payments resulting from existing obligations. These obligations generally require the Company to exchange foreign currencies for U.S. Dollars, Euros, Pounds Sterling, Brazilian Reals or Canadian Dollars. These foreign exchange contracts are fair value hedges of a related liability or asset recorded in the Condensed Consolidated Balance Sheet (Unaudited). The gain or loss on the derivative hedge contracts is recorded in earnings as an offset to the change in value of the related liability or asset. During the three month periods ended July 1, 2007 and July 2, 2006, $3,544 and $3,409 of pretax derivative losses and gains, respectively, from such hedges were recorded as an adjustment to earnings in Other income, net. During the nine month periods ended July 1, 2007 and July 2, 2006, $7,576 and $2,798 of pretax derivative losses and gains, respectively, from such hedges were recorded as an adjustment to earnings in Other income, net. At July 1, 2007 and September 30, 2006, $196,892 and $129,663, respectively, of such foreign exchange derivative contracts were outstanding.

The Company is exposed to risk from fluctuating prices for raw materials, including zinc, urea and di-ammonium phosphates used in its manufacturing processes. The Company hedges a portion of the risk associated with these materials through the use of commodity call options and swaps. The hedge contracts are

Table of Contents

designated as cash flow hedges with the fair value changes recorded in AOCI and as a hedge asset or liability, as applicable. The unrecognized changes in fair value of the hedge contracts are reclassified from AOCI into earnings when the hedged purchase of raw materials also affects earnings. The call options effectively cap the floating price on a specified quantity of raw materials through a specified date. The swaps effectively fix the floating price on a specified quantity of raw materials through a specified date. During the three month periods ended July 1, 2007 and July 2, 2006, $1,788 and $512, of pretax derivative gains, respectively, were recorded as an adjustment to Cost of goods sold for swap or option contracts settled at maturity. During the nine month periods ended July 1, 2007 and July 2, 2006, $14,101 and $238, of pretax derivative gains and losses, respectively, were recorded as an adjustment to Cost of goods sold for swap or option contracts settled at maturity. The hedges are generally highly effective, however, during the three month periods ended July 1, 2007 and July 2, 2006, $160 and $0 respectively, of pretax derivative gains, were recorded as an adjustment to Cost of goods sold for ineffectiveness and $228 and $24 of pretax derivative losses were recorded as an adjustment to Cost of goods sold for ineffectiveness during the nine month periods ended July 1, 2007 and July 2, 2006, respectively. At July 1, 2007, the Company had a series of such swap contracts outstanding through February 2009 with a contract value of $43,244. At September 30, 2006, $43,614 of such commodity contracts was outstanding. The derivative net loss on these contracts recorded in AOCI at July 1, 2007 was $417, net of tax benefit of $212. The derivative net gain on these contracts recorded in AOCI at September 30, 2006 was $3,495, net of tax expense of $1,852. At July 1, 2007, the portion of derivative net losses estimated to be reclassified from AOCI into earnings over the next 12 months is $294, net of tax.

3 OTHER COMPREHENSIVE INCOME

Comprehensive income and the components of other comprehensive income, net of tax, for the three and nine month periods ended July 1, 2007 and July 2, 2006, respectively, are as follows:

	Three Months		Nine Months	
	2007	**2006**	**2007**	**2006**
Net (loss) income	$ (7,388)	$ 2,545	$ (263,713)	$ 5,425
Other comprehensive income:				
Foreign currency translation	16,853	8,521	28,843	10,725
Adjustment of additional minimum pension liability	(114)	(392)	(1,728)	(403)
Net unrealized (loss) gain on derivative instruments	(2,765)	4,560	(8,421)	10,779
Net change to derive comprehensive income for the period	13,974	12,689	18,694	21,101
Comprehensive income (loss)	$ 6,586	$ 15,234	$ (245,019)	$ 26,526

Net exchange gains or losses resulting from the translation of assets and liabilities of foreign subsidiaries are accumulated in the AOCI section of Shareholders equity. Also included are the effects of exchange rate changes on intercompany balances of a long-term nature and transactions designated as hedges of net foreign investments. The changes in accumulated foreign currency translation for the three and nine month periods ended July 1, 2007 and July 2, 2006 were primarily attributable to the impact of translation of the net assets of the Company s European operations, primarily denominated in Euros and Pounds Sterling.

4 NET (LOSS) INCOME PER COMMON SHARE

Net (loss) income per common share for the three and nine month periods ended July 1, 2007 and July 2, 2006, respectively, is calculated based upon the following number of shares:

	Three Months		Nine Months	
	2007	**2006**	**2007**	**2006**
Basic	50,753	49,456	50,827	49,458
Effect of restricted stock and assumed conversion of options		2,128		1,501

Diluted	50,753	51,584	50,827	50,959

Table of Contents

For the three and nine month periods ended July 1, 2007, the Company has not assumed the exercise of common stock equivalents as the impact would be antidilutive.

5 INVENTORIES

Inventories, which are stated at the lower of cost or market, consist of the following:

	July 1, 2007	September 30, 2006
Raw materials	$ 78,120	$ 121,793
Work-in-process	34,316	36,205
Finished goods	220,636	302,674
	$ 333,072	$ 460,672

6 GOODWILL AND ACQUIRED INTANGIBLE ASSETS

Goodwill and intangible assets consist of the following:

	Global Batteries & Personal Care	Home and Garden	Global Pet Supplies	Total
Goodwill:				
Balance as of September 30, 2006	$ 330,465	$ 297,330	$ 502,389	$ 1,130,184
Asset held for sale		(298,576)		(298,576)
Purchase price allocation	834		(8,103)	(7,269)
Goodwill impairment	(214,039)			(214,039)
Effect of translation	5,981	1,246	23,507	30,734
Balance as of July 1, 2007	$ 123,241	$	$ 517,793	$ 641,034
Intangible Assets:				
Trade names Not Subject to Amortization				
Balance as of September 30, 2006	$ 393,110	$ 146,634	$ 297,200 &n	