

SCOTTS LIQUID GOLD INC  
Form 10-K  
March 16, 2009  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**  
**FORM 10-K**

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the fiscal year ended December 31, 2008

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 001-13458

**SCOTT S LIQUID GOLD-INC.**

(Name of small business as specified in its charter)

**Colorado**  
(State or other jurisdiction of

incorporation or organization)

**4880 Havana Street, Denver, CO 80239**

(Address of principal executive offices and Zip Code)

**(303) 373-4860**

(Registrant's telephone number, including area code)

**84-0920811**  
(I.R.S. Employer

Identification No.)

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act: \$0.10 Par Value Common Stock

## Edgar Filing: SCOTTS LIQUID GOLD INC - Form 10-K

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Exchange Act.  Yes  No

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

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

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 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  Smaller reporting company

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

The aggregate market value of the common stock held by non-affiliates of the issuer, assuming directors are affiliates, was \$2,317,033 on June 30, 2008.

As of January 31, 2009, there were 10,695,000 shares of common stock, \$0.10 par value per share, outstanding.

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The following documents are incorporated by reference: The Registrant's definitive Proxy Statement for the Annual Meeting of shareholders scheduled to be held on May 12, 2009, is incorporated by reference in Part III.

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**PART I**

**Item 1. Business**  
General

Scott's Liquid Gold-Inc., a Colorado corporation, was incorporated on February 15, 1954. Through our wholly-owned subsidiaries, we manufacture and market quality household and skin care products and act as a distributor in the United States of beauty care products contained in individual sachets and manufactured by Montagne Jeunesse and of certain other products. In this Report, collectively, the terms "we", "us" or "our" refers to Scott's Liquid Gold-Inc. and our subsidiaries. Our business is comprised of two segments, household products and skin care products.

Our household products consist of (a) Scott's Liquid Gold® for wood, a wood preservative and cleaner, sold nationally for over 30 years; (b) a wood wash and wood wipes under the name of Scott's Liquid Gold; (c) Scott's Liquid Gold Mold Control 500, a consumer product that helps rid homes of mold, introduced in 2006; (d) Touch of Scent®, an aerosol room air freshener; and (e) Cube Scents, a room air freshener introduced in 2008. In early 1992, we entered into the skin care business through our subsidiary, Neoteric Cosmetics, Inc. Our skin care products consist primarily of Alpha Hydrox® products, our Neoteric Diabetic product, and our Neoteric massage oil products. In addition to manufacturing the aforementioned skin care products, we further act as the distributor in the United States for other beauty, bath and hair care products manufactured by Montagne Jeunesse, COSMEX International (Davinci & Moosehead men's grooming products), Baylis & Harding, and Keyline Brands.

For information on our operating segments, please see Note 8, Segment Information, to our Consolidated Financial Statements.

This report may contain forward-looking statements within the meaning of U.S. federal securities laws. These statements are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements and our performance inherently involve risks and uncertainties that could cause actual results to differ materially from the forward-looking statements. Factors that would cause or contribute to such differences include, but are not limited to, continued acceptance of each of our significant products in the marketplace; the degree of success of any new product or product line introduction by us; uncertainty of consumer acceptance of the new Alpha Hydrox products introduced in 2005 and 2007, and Mold Control 500 and wood wash products; competitive factors; any decrease in distribution of (i.e., retail stores carrying) our significant products; continuation of our distributorship agreement with Montagne Jeunesse; the need for effective advertising of our products; limited resources available for such advertising; new competitive products and/or technological changes; dependence upon third party vendors and upon sales to major customers; changes in the regulation of our products, including applicable environmental regulations; continuing losses which could affect our liquidity; the loss of any executive officer; and other matters discussed in this Report. We undertake no obligation to revise any forward-looking statements in order to reflect events or circumstances that may arise after the date of this Report.

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### Strategy

Our strategy is to manufacture and market high quality consumer products which are distinct within each category in which we compete. Scott's Liquid Gold for wood distinguishes itself from competing products as a wood cleaner and preservative, not simply a polish. Mold Control 500 is based on technology developed and patented by a national laboratory. Touch of Scent offers a convenience because it does not require shaking before use and it can be activated by an attractive dispenser which may be mounted on any hard, smooth surface. With respect to our line of skin care products, Alpha Hydrox was one of the first alpha hydroxy acid skin care products sold to retailers for resale to the public at affordable prices. In 1998, we added a retinol product to our skin care line. In the first half of 1999, we introduced *Neoteric Diabetic Skin Care*<sup>®</sup>. Since 2001, we have sold Montagne Jeunesse sachets which are reasonably priced and designed for single use by the consumer. We will continue to examine other possible new products which we believe may fit well with our expertise and financial capabilities. We have introduced other new products or variants of products in subsequent years.

The growth in sales of Alpha Hydrox from 1992 through 1996 caused us to make substantial investments in property, plant and equipment to handle that growth and the anticipated future growth of our skin care products. The decline in sales of those products in 1998 through 2004 and in 2006 and 2007, as well as declines in sales of household products, has resulted in efforts by us to maintain or increase sales of the existing products, to introduce new products, and to decrease our costs of doing business. We have introduced new household products each year since 2004, some of which have been discontinued. Additionally, we introduced several new Alpha Hydrox products in 2005, two new Alpha Hydrox products in 2006, and four new Alpha Hydrox products in 2007. We have engaged in cost-cutting programs during 2008 and at various other times since 2000.

Our goal for 2009 is to resume sales growth and attain profitability. To achieve these goals, we will continue to work on expanding the retail presence of products manufactured by others for whom we act as a distributor, as well as expanding the distribution of our Alpha Hydrox and other skin care products, our household products (Scott's Liquid Gold for wood and our mold remediation product Mold Control 500) and introducing new products within our product lines. Further, we will also consider the development of new niche products, remain open to manufacturing private label products for others and explore the possibility of joint ventures and other projects which would utilize our manufacturing or marketing capabilities.

### Products

Scott's Liquid Gold for wood, a wood cleaner and preservative, has been our core product since our inception. It has been popular throughout the U.S. for over forty years. Scott's Liquid Gold for wood, when applied to wood surfaces such as furniture, paneling, kitchen cabinets, outside stained doors and decking, penetrates microscopic pores in the surface and lubricates beneath, restoring moisture and, at the same time, minimizes the appearance of scratches, darkening the wood slightly. Scott's Liquid Gold preserves wood's natural complexion and beauty without wax. In May 2004, we commenced the introduction of an additional wood care product in a wipe form; however, sales have been minimal so far. In the second quarter of 2005 we introduced a wood wash product under the Scott's Liquid Gold product line; however, we have obtained limited distribution so far.

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During the second quarter of 2006 we began the introduction of our mold remediation product Mold Control 500. Scott's Liquid Gold Mold Control 500 is an advanced restoration, remediation and antibacterial disinfectant system designed for consumer use on mildew, fungus, mold and fungal spores.

In 1982, we added the room air freshener Touch of Scent to our line of household products. Touch of Scent, available in many fragrances, is intended to be used in conjunction with a decorative dispenser which can be mounted on any hard surface and into which the consumer inserts an aerosol refill unit. At a touch, the dispenser propels the fragrance from a refill unit into the air.

Household products accounted for 45.8% of our consolidated net sales in 2008 and 44.9% in 2007.

In early 1992, we began to market two skin care products under the trade name of Alpha Hydrox. Since that time we have made additions to our skin care products, some of which were discontinued. In 2005, we introduced four new Alpha Hydrox products with refined formulas, and in 2007 we introduced a value priced Alpha Hydrox White line of products. Our Alpha Hydrox skin care products are sold through a wholly-owned subsidiary, Neoteric<sup>®</sup> Cosmetics, Inc. Except for the Montagne Jeunesse sachets and other products noted below which are distributed by us, our skin care products are manufactured by Neoteric Cosmetics. Several of the Alpha Hydrox products contain alpha hydroxyethanoic acids in low but effective concentrations. Properly blended with a carrier, alpha hydroxyethanoic acids gently slough off dead skin cells to promote a healthier, more youthful appearance and diminish fine lines and wrinkles. Our products with alpha hydroxy acids ( AHAs ) include facial care products, a body lotion and a foot crème. Our other skin care products do not contain AHAs. These products include Neoteric Diabetic Skin Care, which is a healing crème and a therapeutic moisturizer developed by us to address the skin conditions of diabetics, caused by poor blood circulation, and which contains a patented oxygenated oil technology; an Alpha Hydrox Oxygenated Moisturizer, which is our second skin care product based on the oxygenated oil technology; a Retinol product containing a patented Microsponge technology that softens fine lines and wrinkles; and a body wash. The Montagne Jeunesse sachets, described more below, do not contain AHAs.

In April of 2001, we made our first sale of skin care sachets under a distributorship agreement with Montagne Jeunesse. Our agreement covers sales in the United States. Montagne Jeunesse is a trading division of Medical Express (UK) Ltd., a company located in England. Montagne Jeunesse sachet products are currently sold in over 70 countries around the world. Examples of the Montagne Jeunesse products are a facial scrub, face masks, and a cream for feet. A significant portion of our sales are now generated through the distribution of the Montagne Jeunesse products and, therefore, are dependent on the agreement under which they are purchased by us. See Manufacturing and Suppliers below.

Other products distributed in the United States by us as of December 31, 2008 are DaVinci and Moosehead men's grooming products (introduced in 2006 and 2007), and bath, body and hair care products of both Keyline and Baylis & Harding (introduced in 2007).

Our business is seasonal to some extent. Sales of Montagne Jeunesse products have been higher in the fourth quarter than other quarters because of holiday promotions.

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Through our research and development group, we continually consider and evaluate possible new products to be manufactured or sold by us. Generally these products involve household products or skin care products. However, the Company will also consider consumer products in other areas.

### Marketing and Distribution

Our products in general are sold nationally, directly and through independent brokers, to mass marketers, drugstores, supermarkets, and other retail outlets and to wholesale distributors. In 2008 and 2007, Wal-Mart Stores, Inc. ( Wal-Mart ) accounted for approximately 32% and 28% of our sales of household products. With regard to our skin care products, Wal-Mart accounted for approximately 28% of 2008 sales (35% in 2007), and Rite-Aid accounted for approximately 10% of 2008 sales (13% in 2007).

Wal-Mart and Rite-Aid accounted for approximately 30% and 6% of the combined sales of household products and skin care products in 2008. No long-term contracts exist between us and Wal-Mart, Rite Aid or any other customer. We permit returns of our products by our customers, a common industry practice. A recent practice of retailers has been to return products that have either been discontinued or not sold after a period of time. We subtract any returns from gross sales in determining our net sales and provide a reserve for such returns which is netted against accounts receivable and gross sales on our financial statements.

We also use our websites for sales of our products. Such sales are less than 10% of total net sales but have increased in recent years.

During the years 2001 through 2004, and again in 2006, 2007 and 2008, we experienced a decrease in the distribution of the Alpha Hydrox products as a result of slowing sales. In 2005, we introduced four new items in our Alpha Hydrox line of cosmetics, which resulted in some increased distribution by selling those products to retail store chains not carrying any of our other Alpha Hydrox products. As a result of decreased sales and our efforts to manage marketing costs, the distribution of Alpha Hydrox is limited to certain retail chains and the Company's websites. If sales of one of our products continue to decline, other retail stores, including potentially Wal-Mart may discontinue the product. The level of advertising for our products is constrained by our size and financial resources. Any significant decrease in the distribution of skin care products or Scott's Liquid Gold products at retail stores could have a material adverse effect on our sales and operating results.

Our Scott's Liquid Gold wood care products, Mold Control 500 product, and Alpha Hydrox products have been advertised nationally on network television, on cable television, and, at times, in print media. Expenditures for these purposes in 2008 and 2007 were a small amount relative to net sales and these expenditures in prior years. To date, we have not used television advertising for the Montagne Jeunesse products. We periodically review our advertising plans and may revise planned advertising expenditures based upon actual sales results and competitive conditions.

To enable consumers to make informed decisions, our containers and promotional materials note the concentration of alpha hydroxy acid contained in each of our Alpha Hydrox products which contain such acids. We recommend the use of sunscreen in our written directions contained in every box of Alpha Hydrox products with such acids. We do not exaggerate benefits to be expected from the use of our products. We also maintain a 24-hour, toll free telephone number and website for use by consumers of our products.

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Our household (except for the Mold Control 500 product) and skin care products are sold in Canada and other foreign countries. Please see Note 8, Segment Information, to the Consolidated Financial Statements for information regarding sales in foreign countries. Currently, foreign sales are made to distributors who are responsible for the marketing of the products, and we are paid for these products in United States currency.

### **Manufacturing and Suppliers**

We own and operate our manufacturing facilities and equipment. With the exception of the other products mentioned below, our wood wipes, and our Mold Control 500 product, we manufacture all of our products, maintaining a high quality standard. Products manufactured by others include those products for which we act as distributor in the United States, our wood wipes, and our Mold Control 500 product. We fill and package our Mold Control 500 product at our facilities. For all of our products, we must maintain sufficient inventories to ship most orders as they are received. We also manufacture the plastic over-caps for our household products in addition to a plastic dispensing unit for Touch of Scent.

Quality control is enforced at all stages of production, as well as upon the receipt of raw materials from suppliers. Raw materials are purchased from a number of suppliers and, at the present time, are readily available. Since 2007, a designated distributor for E.I. DuPont has been our sole supplier of glycolic acid, which is a type of alpha hydroxy acid used in our Alpha Hydrox products. The supply agreement includes a pass-through license authorizing the use of various cosmetic and anti-aging claims for the alpha hydroxy acid products. Our sole supply for the oxygenated oil used in our Neoteric Diabetic Skin Care product is a French company with which we have a non-exclusive supply agreement. Relations with this and other suppliers are satisfactory.

Most of our manufacturing operations, including most packaging, are highly automated, and, as a result, our manufacturing operations are not labor intensive, nor, for the most part, do they involve extensive training. An addition to our plant facilities, completed in early 1996, greatly increased our capacity to produce skin care products. We currently operate on a one-shift basis. Our manufacturing facilities are capable of producing substantially more quantities of our products without any expansion, and, for that reason, we believe that our physical plant facilities are adequate for the foreseeable future.

In 2001, we commenced purchases of the skin care sachets from Montagne Jeunesse under a distributorship agreement covering the United States. On May 4, 2005, our wholly-owned subsidiary, Neoteric Cosmetics, Inc. ( Neoteric ), entered into a new distribution agreement with Montagne Jeunesse International Ltd ( Montagne Jeunesse ) covering our distribution of Montagne Jeunesse products. It replaces a distribution agreement in effect since 2000. In the new agreement, Montagne Jeunesse appoints Neoteric as its exclusive distributor to market and distribute Montagne Jeunesse products in the United States of America. The appointment had an initial term of 18 months, commencing May 3, 2005, and continues in force until terminated by either party by giving to the other party no less than three or six months notice in writing of a termination.

In the agreement, Neoteric agrees, among other things: Not to distribute during the duration of the agreement and for 36 months thereafter any goods of the same description as and which compete with the Montagne Jeunesse products; to use its best endeavors to develop, promote and sell the products in the United States and to expand the sale of the products to all potential purchasers by all



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reasonable and proper means; to purchase certain core products; and to maintain an inventory of the products for Neoteric's own account for sale of these products throughout the United States. Montagne Jeunesse undertakes to use all reasonable endeavors to meet all orders for the products to the extent that such orders do not exceed the forecast for each type of the products. Both parties agree to suggested targeted sales for the first five years of the agreement as stated in the agreement. The prices for our purchases of these products are the published list prices as established by Montagne Jeunesse from time to time, with three months written notice of any change in the published list prices. No party may assign or transfer any rights or obligations under the agreement or subcontract the performance of any obligation.

The agreement may also be terminated for a material breach if the breaching party has failed to remedy the breach within 30 days after receipt of notice in writing and for certain other events. Montagne Jeunesse may terminate the agreement (1) if Neoteric changes its organization or methods of business in a way viewed by Montagne Jeunesse as less effective or (2) if there is a change in control of Neoteric.

The principal and controlling owner of Montagne Jeunesse, Gregory Butcher, owned beneficially, to the best of our knowledge, during 2005 more than 5% of our outstanding common stock; to the best of our knowledge, at February 16, 2009, he owned beneficially less than 5.0% of our outstanding common stock.

On April 4, 2006, we entered into a Product Development, Production and Marketing Agreement with Modec, Inc., a Colorado corporation. Pursuant to this Agreement, we purchase from Modec a product for the treatment of mold; we sell this product as Mold Control 500. We fill and package the product at our facilities and market the product to retail stores in North America. The Agreement provides us with a license for this purpose. We are required to use our commercially reasonable efforts to develop a consumer market for the product in the territory. The initial term of the Agreement was until December 31, 2007, which is automatically renewed for successive one-year terms and was thereby renewed on December 31, 2007 and December 31, 2008.

### Competition

Our business is highly competitive in both household and skin care products. The wood care, air freshener, and mold treatment product categories are dominated by three to five companies significantly larger than us, each of which produce several products. Irrespective of the foregoing, we maintain a visible position in the wood care category, but do not have sufficient information to make an accurate representation as to the market share of our products. Over the last several years, sales of our air freshener products have fallen off significantly and may continue to do so in the future.

The skin care category is also highly competitive. Several competitors are significantly larger than Scott's Liquid Gold-Inc., and each of these competitors produces several products. Some of these companies also produce retinol and alpha hydroxy acid products with which Alpha Hydrox must compete. Because of the number of varied products produced by competitors, we cannot make an accurate representation as to the market share of our skin care products.

Conforming to our corporate philosophy, we compete on the basis of quality and distinguishing characteristics of our products.

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### Regulation

We are subject to various federal, state and local laws and regulations that pertain to the type of products we manufacture and sell. Our skin care products containing Alpha Hydroxy Acids (AHAs) are cosmetics within the definition of the Federal Food Drug and Cosmetic Act (FFDCA). The FFDCA defines cosmetics as products intended for cleansing, beautifying, promoting attractiveness or altering the appearance. Our cosmetic products are subject to regulation under the FFDCA and the Fair Packaging and Labeling Act (FPLA), and the regulations promulgated under these acts. The relevant laws and regulations are enforced by the U.S. Food and Drug Administration (FDA). Such laws and regulations govern the ingredients and labeling of cosmetic products and set forth good manufacturing practices for companies to follow. Although FDA regulations require that the safety of a cosmetic ingredient be substantiated prior to marketing, there is no requirement that a company submit the results of any testing performed or any other data or information with respect to any ingredient to the FDA. Prior to marketing our products, we conduct studies to demonstrate that our Alpha Hydrox products do not irritate the skin or eyes. Consistent with regulations, we do not submit the results of our studies to the FDA.

In July 1997, because of questions raised earlier by the FDA and as requested by the FDA, the Cosmetic Ingredient Review Expert Panel( CIR ) sponsored by the cosmetic industry issued a report concerning the safety of alpha hydroxy acids. The final report, among other things, concluded that glycolic acid (the most common type of alpha hydroxy acid that we currently use) is safe for use at concentrations of up to 10%, with a pH level of no less than 3.5 and when directions for use includes the daily use of sun protection. In January 2005, the FDA issued a final guidance that products containing AHA s alert users that those products may increase skin sensitivity to sun and possible sunburn and the steps to avoid such consequences. All of our labeling reflects this guidance.

Since 2003, the FDA s National Center for Toxicological Research has been investigating the effect of long term exposure to AHAs. Further, on December 31, 2003, the FDA published a call for data on certain ingredients in various products, including AHAs that are part of wrinkle remover products. Manufacturers were asked to submit any data supporting the reclassification of these cosmetic products as over-the-counter drugs. On October 27, 2008, FDA published a set of Q&As that dealt with both issues. With respect to the drug/cosmetic issue, FDA restated its traditional position that certain AHA products intended for therapeutic use, such as acne treatments or skin lighteners, are considered drugs. Other AHA products, including those marketed by Neoteric are considered cosmetics. The Q&A also reported on the results of two studies on the issue of skin damage caused by UV rays, and the potential photocarcinogenicity of the AHA product. The studies concluded that applying AHAs to the skin resulted in increasing UV sensitivity, but that the effect was completely reversible. In addition another study on potential photocarcinogenesis found that AHAs had no effect on the process. Accordingly, Neoteric may continue to market its products as cosmetics.

Our advertising is subject to regulation under the Federal Trade Commission Act and related regulations, which prohibit false and misleading claims in advertising. Our labeling and promotional materials are believed to be in full compliance with applicable regulations.

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Many chemicals used in consumer products, some of which are used in several of our product formulations, have come under scrutiny by various state governments and the Congress of the United States in connection with clean air laws. These chemicals are volatile organic compounds (VOCs) that are contained in various categories of consumer products. As a result of these VOC regulations, it has been necessary for us to reformulate some of our products, such as Touch of Scent, Scott's Liquid Gold Aerosol and Pourable, to conform to certain limits set by the California Air Resources Board (CARB), other states and the Environment Protection Agency. Our household chemical products currently meet the most stringent VOC regulations. CARB, in 2007, adopted changes to California's consumer product regulations that reduce VOC limits for Scott's Liquid Gold pourable formula from 7% to 3%, effective December 31, 2008. This product was formulated to meet that limit.

The CARB regulations concerning VOC content are relevant to our household products, and it appears that one of skin care products will be affected by new limits under CARB. CARB had originally proposed a VOC limit of 10% on skin toners/astringents which are not regulated by the FDA. The current proposed VOC limit is now 35%. If this limit is approved, it will go into effect on December 31, 2010. This will affect Alpha Hydrox Toner.

Any new or revised regulations of CARB could apply to our products and could potentially require additional reformulation of those products. We continue to monitor CARB regulatory activities.

Limitations regarding the VOC content of consumer products by both state and federal agencies will continue to be a part of regulatory efforts to achieve compliance for ozone at or near ground level. Under the Clean Air Act Amendments of 1990, the Environmental Protection Agency (EPA) conducted a study on the contribution of consumer products to ozone problems and published regulations in 1998 designed to reduce the VOC content of consumer products. Various states, in addition to California, have enacted or are considering VOC regulations for consumer products. We are unable to predict how many or which other states might enact legislation regulating the VOC content of consumer products or what effect such legislation might have on our household products.

A group of twelve northeastern states and the District of Columbia collectively drafted the Ozone Transport Commission (OTC) Model Consumer Products Rule in 2001, which is a model that members may choose to adopt and which has standards that are substantially the same as the CARB consumer product VOC regulations. More than a majority of the OTC members have adopted the model rule. In September 2006, the OTC released a new draft model consumer products rule with an effective date of January 1, 2009. Scott's Liquid Gold products would not be affected by the changes in this new model rule. The OTC considers CARB Consumer Products VOC regulations and we continue to monitor the regulatory activities in these states.

There are also potential regulations in a five state region covered by the Lake Michigan Air Directors Consortium (LADCO), which released an interim report detailing possible strategies for reducing VOC emissions. These states include Illinois, Michigan, Wisconsin, Ohio and Indiana. Michigan and Ohio are the two states in the LADCO group that have promulgated such regulations. Both Michigan's and Ohio's final rules were promulgated in 2007 and both are consistent with the OTC Model Rule.

In January 2008, Illinois EPA submitted a proposed consumer products regulation to the Illinois Pollution Control Board. This proposed regulation appears to be consistent with the OTC Model Rule and other states' regulations based on that model.

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We believe that we have done all that is necessary to satisfy the current requirements of the Clean Air Act and laws of various state governments. Currently, all of our products may be sold in all areas of the United States.

### Employees

We employ 66 persons (compared to 77 persons at the end of 2007), 33 in plant and production related functions and 33 in administrative, sales and advertising functions. No contracts exist between us and any union. We monitor wage and salary rates in the Rocky Mountain area and pursue a policy of providing competitive compensation to our employees. The compensation of our executive officers is under the review of the Compensation Committee of our Board of Directors. Fringe benefits for our employees include a medical and dental plan, life insurance, a 401(k) plan with matching contributions for lower paid employees (those earning \$35,000 or less per annum), an employee stock ownership (ESOP) plan, and a profit sharing plan. We consider our employee relations to be satisfactory.

### Patents and Trademarks

At present, we own one patent covering an ingredient used in some of our skin care products. Additionally, we actively use our registered trademarks for Scott's Liquid Gold, Liquid Gold, Touch of Scent, Alpha Hydrox, TriOxygen<sup>®</sup>, and Neoteric in the United States and have registered trademarks in a number of additional countries. Our registered trademarks and pending trademark applications concern names and logos relating to our products as well as the design of boxes for certain of our products.

In December 2000 (amended October 1, 2003), we entered into a license agreement with TriStrata Technology, Inc. which owns patents dealing with the use of alpha hydroxy acids for the purpose of reducing the appearance of wrinkles or fine lines. Under the license agreement, Neoteric Cosmetics and its affiliates were granted a non-exclusive license for the life of the patents to make and sell skin care products using alpha hydroxy acids for, among other things, the reduction of the appearance of skin wrinkles and the reduction in the appearance of skin changes associated with aging. The license agreement covered a territory which includes the United States and certain foreign countries. In accordance with the license agreement, Neoteric Cosmetics paid a royalty on net sales of products covered by the agreement. This license agreement was part of the settlement of a lawsuit brought by TriStrata Technology against us and others alleging infringement of patents in selling and promoting skin care products which contain alpha hydroxy acid. By a notice sent to TriStrata Technology, we terminated this license agreement in October of 2007. We rely on a pass-through license from E.I. DuPont (our supplier) for our uses of glycolic acid regarding wrinkle reduction and anti-aging. The pass-through license applies to customers of DuPont. Although DuPont is a long-time supplier of ours, we have no contracts with DuPont other than orders for our purchases.

### Available Information and Code of Ethics

We will make available free of charge through the website <http://www.businesswire.com/cnn/slkd.htm>, this annual report, our quarterly reports on Form 10-Q, our current reports on Form 8-K, and amendments to such reports, as soon as reasonably practicable after we electronically file or furnish such material with the Securities and Exchange Commission. These reports are also available through a link on our website. We will provide upon request and at no charge electronic or paper copies of these filings with the Securities and Exchange Commission (excluding exhibits).

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We will provide to any person without charge, upon request, a copy of the code of business conduct and ethics which has been adopted by us and which applies to our principal executive officer, principal financial officer and principal accounting officer, among others.

A request for reports filed with the SEC or the code of business conduct and ethics may be made to: Corporate Secretary, Scott's Liquid Gold-Inc., 4880 Havana Street, Denver, Colorado 80239.

### **Item 1A. Risk Factors.**

The following is a discussion of certain risks that may affect our business. These risks may negatively impact our existing business, future business opportunities, our financial condition or our financial results. In such case, the trading price of our common stock could also decline. Additional risks and uncertainties not presently known to us, or that we currently see as immaterial, may also negatively impact our business.

#### ***We need to increase our revenues in order to become profitable under our present cost structure.***

We have experienced net losses in nine of our last ten years. These losses result primarily from declining sales of our skin care products and our primary household products. Maintaining or increasing our revenues is uncertain and involves a number of factors including consumer acceptance of our products, distribution of our products and other matters described below.

#### ***Our cash flow is dependent upon operating cash flow, available cash and borrowing available under the Summit Financial Resources financing agreement.***

Because we are dependent on our operating cash flow, any loss of a significant customer, any further decreases in the distribution of our skin care or household products, new competitive products affecting sales levels of our products or any significant expense not included in our internal budget could result in the need to raise cash. The financing agreement with Summit Financial Resources has a term of one year ending March 2010 and which automatically renews for successive one year terms unless either party provides written notice of non-renewal at least 60 days prior to the end of a one-year financing period. Except for the existing bank debt and the Summit Financial Resources agreement, we have no arrangements for an external financing of debt or equity, and we are not certain whether any such financing would be available on acceptable terms. In order to improve our operating cash flow, we need to achieve profitability or change significantly our cost structure.

#### ***Sale of our real estate is uncertain.***

We continue to pursue a sale of all or part of our real estate. The purpose of such a sale is to reduce our fixed costs and to repay bank debt of approximately \$4.6 million at December 31, 2008 secured by the real estate. Our ability to complete a sale of the real estate is uncertain and may have been affected by a downturn in the commercial real estate market in the Denver, Colorado area.

#### ***Current economic conditions may materially and adversely impact our business.***

The turmoil in the investment market of the United States, the tightening of credit and relatively high level of unemployment in the United States have led to an increased level of commercial and consumer delinquencies, lack of consumer confidence, increased market volatility and possibly a reduction in business activity generally. A continuation of these conditions could have, among other

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things, the following potential negative effects: A reduction in spending of consumers in general including in the area of household products and skin care products, which could reduce our net sales; the potential increase in bad debts or reserve for bad debts affecting our financial condition or cash flow; and exposure to any increased interest expense to the extent that any financing or refinancing could be at costs higher than our existing debt.

### ***Sales of our existing products are affected by changing consumer preferences.***

Our primary market is retail stores in the United States which sell to consumers or end users in the mass market. Consumer preferences can change rapidly and are affected by new competitive products. This situation is true for both skin care and household products and has affected our established products, most significantly our earlier established Alpha Hydrox products. For example, in the skin care area, we believe that our products with AHAs are effective in diminishing fine lines and wrinkles, but consumers may change permanently or temporarily to other products using other technologies or otherwise viewed as new. Any changes in consumer preferences can affect materially the sales and distribution of our products and thereby our revenues and results of operation.

### ***In both skin care and household products, we compete every day against the largest consumer product companies in the United States.***

Our large competitors regularly introduce new products and spend multiples of dollars more than we do on advertising, particularly television advertising. The distribution of our product and sales can be adversely impacted by the actions of our competitors.

### ***We have limited resources to promote our products with effective advertising.***

We sell our products in the consumer retail marketplace. Advertising, particularly television advertising, can be important in reaching consumers, although the effectiveness of any particular advertisement cannot be predicted.

### ***Maintaining or increasing our revenues is dependent on the introduction of new products that are successful in the marketplace.***

Sales of our Alpha Hydrox products, Scott's Liquid Gold for wood and Touch of Scent have declined in recent years. In order to address these declines, we have introduced new products, including Montagne Jeunesse sachets in 2001, the wood wipe and wood wash products in 2004 and 2005, our new Alpha Hydrox products in 2005, a value priced Alpha Hydrox White line in 2007, our mold remediation product Mold Control 500 during the second quarter of 2006, and air freshener products in 2007 and 2008. We plan the introduction of additional products. If we are not successful in making ongoing sales of our newer products to retail store chains or these products are not well received by consumers, our revenues could be materially and adversely affected.

### ***A loss of one or more of our major customers could have a material adverse effect on our product sales.***

For more than a majority of our sales, we are dependent upon sales to major customers, including Wal-Mart which is our largest customer. The easy access of consumers to our products is dependent upon major retail stores and other retail stores carrying our products, particularly mass merchandisers.

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The willingness of these customers (i.e., retail stores) to carry any of our products depends on various matters, including the level of sales of the product at the stores. Any declines in sales of a product to consumers can result in the loss of retail stores as our customers and the corresponding decreases in the distribution of the product. It is uncertain whether the consumer base served by these stores would purchase our products at other retail outlets. In the past, sales of our products have been affected by retail store chains which discontinue a product or carry the product in a lesser number of stores.

*More than a majority of our sales of skin care products are represented by the Montagne Jeunesse products which depend upon the continuation of our distributorship agreement with Montagne Jeunesse.*

Our distributorship agreement with Montagne Jeunesse is for a period of 18 months that ended in November, 2006 and continues in force after this initial term subject to the right of either party to terminate the agreement with three or six months notice. As a practical matter, we also believe that the distribution of Montagne Jeunesse sachets is dependent upon our good relationship with Montagne Jeunesse.

*We face the risk that raw materials for our products may not be available or that costs for these materials will increase, thereby affecting our ability to either manufacture the products or our gross margin on the products.*

We obtain our raw materials from third party suppliers, some of which are sole source suppliers. While there are two suppliers of glycolic acid, we use one supplier. We have no long term contracts with our suppliers; and, if a contract exists, it is subject to termination or cost increases. We may not have sufficient raw materials for production of products manufactured by us if there is a shortage in raw materials or one of our suppliers terminates our relationship. In addition, changing suppliers could involve delays that restrict our ability to manufacture or buy products in a timely manner to meet delivery requirements of our customers. Our suppliers of products which we distribute can also be subject to the same risk with their vendors.

*Our sales are affected adversely by returns.*

In our industry, retail stores have the ability to return products. These returns result in refunds, a reduction of our revenues and usually the need to dispose of the resulting inventory at discounted prices. Accordingly, the level of returns can significantly impact our revenues and cash flow. See information about returns in Note 12 to our Consolidated Financial Statements in this Report.

*Changes in the regulation of our products, including environmental regulations, could have an adverse effect on the distribution, cost or function of our products.*

Regulations affecting our products include requirements of the FDA for cosmetic products and environmental regulations affecting emissions from our products. The FDA has mentioned in the past the treatment of AHA products as drugs, which could make more expensive or prohibitive our production and sale of certain Alpha Hydrox products. Also, in the past, we have changed the formulation of our household products to satisfy environmental regulations and will continue to do so as required.

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### ***Any adverse developments in litigation could have a material impact on us.***

We are subject to lawsuits from time to time in the ordinary course of business. While we expect those lawsuits not to have a material effect on us, an adverse development in any such lawsuit or the insurance coverage for a lawsuit could materially and adversely affect our financial condition and cash flow.

### ***Any loss of our key executives or other personnel could harm our business.***

Our success has depended on the experience and continued service of our executive officers and key employees. If we fail to retain these officers, our ability to continue our business and effectively compete may be substantially diminished. Because of our size, we must rely in many departments within our company on one or two managers; the loss of any one of those could slow our product development, production of a product, and sale and distribution of a product.

### ***Our stock price can be volatile and can decline substantially.***

Our stock is traded on the OTC Bulletin Board. The volume of our stock varies but is relatively limited. As a result, any events affecting us can result in volatile movements in the price of our stock and can result in significant declines in the market price of our stock.

### **Item 1B. Unresolved Staff Comments.**

Not applicable.

### **Item 2. Properties.**

Our facilities, located in Denver, Colorado, are currently comprised of three connected buildings and a parking garage (approximately 261,100 square feet in total) and about 16.2 acres of land, of which approximately 6 acres are available for future expansion. These buildings range in age from approximately 10 to 35 years (126,600 square feet having been added in 1995 and 1996). The Denver facility houses our corporate headquarters and all of our operations, and serves as one of several distribution points. We believe that our current space will provide capacity for growth for the foreseeable future. All of our land and buildings serve as collateral under a deed of trust for a \$5.2 million bank loan (\$4.6 million at December 31, 2008) consummated by us on June 26, 2006.

As indicated in this Report, the Company uses less than the capacity of its facilities and is also interested in reducing its expenses. As part of this process, starting as of July 2007, the Company has engaged a commercial real estate broker, currently CB Richard Ellis, in Denver to explore alternatives. These alternatives include the sale of all or part of the facilities, a sale of all or part of the facilities combined with a leaseback by the Company of the facilities, or a lease of all or part of the facilities by the Company to a third party. There is, however, no assurance that acceptable transactions will be offered or completed.

### **Item 3. Legal Proceedings.**

#### **Wayne Taylor, et al. v. The Sherwin-Williams Companies, et al.**

The Company was served with a complaint February 25, 2009, naming it as a defendant in this personal injury action filed in the Superior Court of New Jersey, Camden County. Plaintiffs Wayne Taylor and Leslie Taylor, his wife, claim that Mr. Taylor has contracted Acute Myelogenous Leukemia (AML) as a result of work related exposure to benzene and that the Company is one of a minimum 15 co-defendant product manufacturers which used benzene in products sold to Mr. Taylor or his employers and used by Mr. Taylor in his work. Plaintiffs allege exposure to defendants' products containing benzene and that the exposure caused personal injuries, including AML. Fifty John Doe corporations are asserted to be similarly liable. Claims are asserted against all defendants for negligence, breach of warranty, consumer fraud, intentional tort and loss of consortium.

The extent of the defense and indemnity obligations of its product liability insurers is to be determined and is uncertain at this time. The Company has submitted the claim to its product liability insurers and believes that insurers will assume the defense of the claim and retain counsel accordingly. The Company believes that Mr. Taylor was not exposed to benzene as the result of use of the Company's products and



intends to vigorously defend the action.

**Table of Contents****Item 4. Submission of Matters to a Vote of Security Holders.**

Not applicable.

**PART II****Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.**

## Market Information

Our \$0.10 par value common stock is listed on the OTC Bulletin Board (a regulated quotation service) under the ticker symbol SLGD. The high and low prices of Scott's Liquid Gold-Inc. common stock as traded on the OTC Bulletin Board were as follows. The over-the-counter market quotations reflect inter-dealer prices, without retail mark-up, mark-down or commission and may not necessarily represent actual transactions.

	<b>2008</b>	
	<b>Three Months Ended</b>	
	<b>High</b>	<b>Low</b>
March 31	\$ 0.75	\$ 0.43
June 30	\$ 0.55	\$ 0.35
September 30	\$ 0.40	\$ 0.27
December 31	\$ 0.35	\$ 0.11
	<b>2007</b>	
	<b>Three Months Ended</b>	
	<b>High</b>	<b>Low</b>
March 31	\$ 0.87	\$ 0.75
June 30	\$ 0.95	\$ 0.73
September 30	\$ 1.12	\$ 0.72
December 31	\$ 0.95	\$ 0.54

## Shareholders

As of January 31, 2009, we had approximately 937 shareholders of record.

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## Dividends

We did not pay any cash dividends during the two most recent fiscal years. No decision has been made as to future dividends. See Management's Discussion and Analysis or Plan of Operation - Liquidity and Capital Resources for information concerning restrictions on dividends.

## Other

Current stock quotes, our SEC filings, quarterly earnings and press releases can be found at: <http://www.businesswire.com/cnn/slqd.htm>.

## Equity Plans

The following table provides, as of December 31, 2008, information regarding our equity compensation plans, which consist of the 1997, 1998, and 2005 Stock Option Plans. The 1997 and 1998 Plans have expired, but options under those Plans remain outstanding. We also have an Employee Stock Ownership Plan which invests only in our common stock, but which is not included in the table below.

<b>Plan Category</b>	<b>Number of securities to be issued upon exercise of outstanding options, warrants and rights</b>	<b>Weighted-average exercise price of outstanding options, warrants and rights</b>	<b>Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))</b>
	<b>(a)</b>	<b>(b)</b>	<b>(c)</b>
Equity compensation plans approved by security holders	1,862,650	\$ 0.62	608,350
Equity compensation plans not approved by security holders			
<b>Total</b>	<b>1,862,650</b>	<b>\$ 0.62</b>	<b>608,350</b>

Stock Purchases

We did not make any repurchases of our outstanding shares during the fourth quarter of 2008.

## Stock Contributions

Pursuant to board resolutions, on May 6, 2008, September 23, 2008, and December 12, 2008 we issued and contributed 30,000 shares, 30,000 shares, and 40,000 shares, respectively, of our common stock to our Employee Stock Ownership Plan (the Plan). No consideration was paid by the Plan for these contributions. We believe that these contributions were not subject to the securities registration requirements of the Securities Act of 1933 because they did not involve a sale. The contributions of the shares to the Plan may also be exempt from such securities registration as a non-public offering under Section 4(2) of the Securities Act of 1933.

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### **Item 6. Selected Financial Data**

Not applicable.

### **Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.**

General

We manufacture and market both household and skin care products. Our products are sold throughout the United States and Canada and insignificantly in other countries.

#### Critical Accounting Policies

We have identified the policies below as critical to our business operations and the understanding of our results of operations. These policies involve significant judgments, estimates and assumptions by our management. For a detailed discussion on the application of these and other accounting policies, see Note 1 in the Notes to the Consolidated Financial Statements.

#### *Revenue Recognition*

Our revenue recognition policy is significant because the amount and timing of revenue is a key component of our results of operations. We follow the guidance of Staff Accounting Bulletin No. 104 ( SAB 104 ), which requires that a strict series of criteria are met in order to recognize revenue related to product shipment. If these criteria are not met, the associated revenue is deferred until the criteria are met. Generally, these criteria are that there be an arrangement to sell the product, we have delivered the product in accordance with that arrangement, the sales price is determinable, and collectibility is probable.

Our reserves for accounts receivable consist of a bad debt reserve and reserves for returns and customer allowances. Reserves for marketing rebates, pricing allowances and returns, coupons and certain other promotional activities involve estimates made by management based upon an assessment of historical trends, information from customers, and anticipated returns and allowances related to current sales activity. The level of returns and allowances are impacted by, among other things, promotional efforts performed by customers, changes in customers, changes in the mix of products sold, and the stage of the relevant product life cycle. Changes in estimates may occur based on actual results and consideration of other factors that cause returns and allowances. In the event that actual results differ from these estimates, results of future periods may be impacted.

Reserves for bad debts (\$59,500 at December 31, 2008 and \$62,900 at December 31, 2007) are recorded based on estimates by management including factors surrounding the credit risk of specific customers and historical trends. We have been exposed to potential losses on receivables due from specific customers that have suffered financial difficulties. We have provided reserves against certain receivables from such customers in addition to amounts related to unidentified losses. Those

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reserves are reduced as those accounts are settled or written off. In the event that actual losses differ from these estimates or there is an increase in exposure relating to sales to specific customers, results of future periods may be impacted. We believe our reserve is adequate to absorb any losses which may arise.

*Income Taxes*

As of December 31, 2008, we have net deferred income tax assets of \$3,037,800 which primarily relate to net operating loss carryforwards, expenses that are not yet deductible for tax purposes and tax credit carryforwards, offset by deferred income tax liabilities for differences in the book and tax bases of property and equipment. The net deferred tax asset is fully reserved by a valuation allowance. The valuation allowance represents management's determination that we will more likely than not be unable to realize the value of such assets due to the uncertainty of future profitability.

*Inventory Valuation and Reserves*

Our inventory is a significant component of our total assets. In addition, the carrying value of such inventory directly impacts the gross margins that we recognize when we sell the inventory and record adjustments to carrying values. Our inventory is valued at the lower of cost or market, cost being determined under the first-in, first-out method. We estimate reserves for slow moving and obsolete products and raw materials based upon historical and anticipated sales. In the event that actual results differ from these estimates, results of future periods may be impacted.

Recently Issued Accounting Pronouncements

Please see Note 1 (p) of our Consolidated Financial Statements.

**Table of Contents****Results of Operations**

During 2008, we experienced a decrease in sales of both our Scott's Liquid Gold household products and our Montagne Jeunesse line of skin care products and a slight increase in net sales of our line of Alpha Hydrox skin care products. Our net loss for 2008 was \$1,497,000 versus a loss of \$1,310,800 for 2007. The slight increase in our loss for 2008 compared to 2007 results from a decrease in sales, mitigated somewhat by a reduction in our operating costs and expenses.

**Summary of Results as a Percentage of Net Sales**

	<b>Year Ended December 31,</b>	
	<b>2008</b>	<b>2007</b>
Net sales		
Scott's Liquid Gold household products	45.8%	44.9%
Skin care products	54.2%	55.1%
Total net sales	100.0%	100.0%
Cost of sales	56.9%	56.5%
Gross profit	43.1%	43.5%
Other revenue	0.2%	0.4%
	43.3%	43.9%
Operating expenses	50.6%	48.9%
Interest expense	2.1%	2.3%
	52.7%	51.2%
Loss before income taxes	(9.4%)	(7.3%)

Our gross margins may not be comparable to those of other entities because some entities include all of the costs related to their distribution network in cost of sales and others, like us, exclude a portion of them (freight out to customers and nominal outside warehouse costs) from gross margin, including them instead in the selling expense line item. See Note 1(o), Operating Costs and Expenses Classification, to the Consolidated Financial Statements in this Report.

Year Ended December 31, 2008

Compared to Year Ended December 31, 2007

**Comparative Net Sales**

	<b>2008</b>	<b>2007</b>	<b>Percentage Increase (Decrease)</b>
Scott's Liquid Gold and other household products	\$ 6,414,100	\$ 7,021,800	(8.7%)
Touch of Scent	880,000	1,029,900	(14.6%)
Total household products	7,294,100	8,051,700	(9.4%)
Alpha Hydrox and other skin care	3,848,000	3,302,100	16.5%
Montagne Jeunesse and other distributed skin care	4,769,700	6,564,700	(27.3%)

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Total skin care products	8,617,700	9,866,800	(12.7%)
Total net sales	\$ 15,911,800	\$ 17,918,500	(11.2%)

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Consolidated net sales for 2008 were \$15,911,800 versus \$17,918,500 for 2007, a decrease of \$2,006,700 or about 11.2%. Average selling prices for 2008 were up by \$932,800 over those of the comparable period of 2007, prices of household products being up by \$468,200, and average selling prices of skin care products being up by \$464,600. This increase was primarily due to fewer price promotions on selected cosmetic products. Co-op advertising, marketing funds, slotting fees and coupon expenses (promotional allowances) paid to retailers were subtracted from gross sales in accordance with current accounting policies totaling \$1,510,100 in 2008 versus \$2,294,700 in 2007, a decrease of \$784,600 or about 34.2%. This decrease consisted of a decrease in coupon expense of \$345,400, a decrease in co-op marketing funds of \$309,500 and a decrease in slotting fee expenses of \$129,700.

From time to time, our customers return product to us. For our household products, we permit returns only for a limited time, and generally only if there is a manufacturing defect. With regard to our skin care products, returns are more frequent under an unwritten industry standard that permits returns for a variety of reasons. In the event a skin care customer requests a return of product, the Company will consider the request, and may grant such request in order to maintain or enhance relationships with customers, even in the absence of an enforceable right of the customer to do so. Some retailers have not returned products to us. Return price credit (used in exchanges typically, or rarely, refunded in cash) when authorized is based on the original sale price plus a handling charge of the retailer that ranges from 8-10%. The handling charge covers costs associated with the return and shipping of the product. Additions to our reserves for estimated returns are subtracted from gross sales.

From January 1, 2006 through December 31, 2008, our product returns (as a percentage of gross revenue) have averaged as follows: household products 0.2%, Montagne Jeunesse products 3.3%, and our Alpha Hydrox and other skin care products 5.7%. The level of returns as a percentage of gross revenue for the household products and Montagne Jeunesse products have remained fairly constant as a percentage of sales over that period while the Alpha Hydrox and other skin care products return levels have fluctuated. More recently, as our sales of the skin care products have declined we have seen a decrease in returns as a percentage of gross revenues. The products returned in 2008 (indicated as a percentage of gross revenues) were: household products 0.1%, Montagne Jeunesse products 3.3%, and our Alpha Hydrox and other skin care products 2.0%. We are not aware of any industry trends, competitive product introductions or advertising campaigns at this time which would cause returns as a percentage of gross sales to be materially different for the current fiscal year than for the above averages. Furthermore, the Company's management is not currently aware of any changes in customer relationships that we believe would adversely impact anticipated returns. However, we review our reserve for returns quarterly and we regularly face the risk that the existing conditions related to product returns will change.

During 2008, net sales of skin care products accounted for 54.2% of consolidated net sales compared to 55.1% for 2007. Net sales of these products for those periods were \$8,617,700 in 2008 compared to \$9,866,800 in 2007, a decrease of \$1,249,100 or about 12.7%.

Net sales of Montagne Jeunesse and other distributed products were \$4,769,700 in 2008 versus \$6,564,700 in 2007, a decrease of \$1,795,000 or 27.3%. The decrease primarily reflects a reduction holiday display orders placed by retailers for the fourth quarter of 2008. The decrease in sales of Montagne Jeunesse was offset somewhat by increased sales of Moosehead Men's grooming products and Baylis & Harding products which were not sold during the first half of 2007 or only had nominal sales during that period.



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Net sales of our Alpha Hydrox and other skin care products were \$3,848,000 in 2008 versus \$3,302,100 in 2007, an increase of \$545,900 or 16.5%. The increase is primarily the result of the contraction in distribution of Alpha Hydrox products at drug store and grocery chains where retail support in the form of product returns, marketing co-op funds, coupon and promotion programs, damage claims and similar matters are expensive. With this contraction in distribution, the corresponding reduction in these associated costs has resulted in greater net sales reported in 2008.

Sales of household products for 2008 accounted for 45.8% of consolidated net sales compared to 44.9% for the same period in 2007. These products are comprised of Scott's Liquid Gold wood care products (Scott's Liquid Gold for wood, a wood wash and wood wipes), mold remediation products, Touch of Scent products. During 2008 sales of household products were \$7,294,100 as compared to \$8,051,700 for the same period in 2007, a decrease of \$757,600, or 9.4%. Sales of Scott's Liquid Gold wood care products decreased by \$607,700 in 2008 versus 2007. We believe this reduction to be a result of a decrease in media advertising of our wood care products in 2008 versus 2007. Mold Control 500 sales, which are shown in the sales for Scott's Liquid Gold and other household products, were \$446,600 for 2008 versus \$849,700 in 2007, primarily due to new product promotional introductions occurring in 2007 with two major hardware chains which were not replicated in 2008. Sales of air fresheners were down by \$149,900 or 14.6%, primarily due to a decrease in distribution in present and past quarters, offset in part by introductory sales of Cube Scents, introduced in the third quarter of 2008. It is too early to tell about consumer acceptance of this addition.

As sales of a consumer product decline, there is the risk that retail stores will stop carrying the product. The loss of any significant customer for any skin care products, Scott's Liquid Gold wood care or mold remediation products, could have a significant adverse impact on our revenues and operating results. We believe that our future success is highly dependent on favorable acceptance and sales in the marketplace of Montagne Jeunesse products, our Alpha Hydrox products introduced in 2005 and 2007 and our Scott's Liquid Gold wood care and mold remediation products.

We also believe that the introduction of successful new products, including line extensions of existing products, such as the wood wash and our new mold remediation product, using the name Scott's Liquid Gold, are important in our efforts to maintain or grow our revenue. Late in the fourth quarter of 2006, we introduced two new items within our Alpha Hydrox cosmetic line of products. Late in the fourth quarter of 2007, we introduced new items within the Moosehead Men's grooming products and also products of Baylis & Harding. In early 2008, we introduced bath, body and hair care products manufactured by Keyline Brands. We have introduced in the first quarter of 2009 and expect to commence shipping in the second quarter of 2009 a new household product under the Scott's Liquid Gold brand which is designed for use in cleaning the screens of today's sensitive electronics including televisions, computer monitors and more. Additionally, we regularly review possible additional products to sell through distribution agreements or to manufacture ourselves. To the extent that we manufacture a new product rather than purchase it from external parties, we are also benefited by the use of existing capacity in our facilities. The actual introduction of additional products, the timing of any additional introductions and any revenues realized from new products is uncertain.

On a consolidated basis, cost of goods sold was \$9,048,300 for 2008 compared to \$10,117,600 for 2007, a decrease of \$1,069,300 or 10.6%, on a sales decrease of 11.2%. As a percentage of consolidated net sales, cost of goods sold was 56.9% in 2008 versus 56.5% in 2007. The cost of goods reflects the combined result of an increase in raw material costs (primarily in both

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oil and steel cans) and the decrease in sales promotion expenses which increased our revenues and thus affected our margins. We have seen significant increases in steel can costs, beginning in the first quarter of 2009. We currently expect that these higher costs will be offset by anticipated declines in the cost of our process oils used to manufacture Scott's Liquid Gold for wood products.

**Operating Expenses, Interest Expense and Other Income**

	2008	2007	Percentage Increase (Decrease)
Operating Expenses			
Advertising	\$ 345,300	\$ 332,800	3.8%
Selling	4,943,100	5,433,500	(9.0%)
General & Administrative	2,760,500	2,994,800	(7.8%)
<b>Total operating expenses</b>	<b>\$ 8,048,900</b>	<b>\$ 8,761,100</b>	<b>(8.1%)</b>
Interest Income and Other	\$ 23,000	\$ 72,300	(68.2%)
Interest Expense	\$ 334,600	\$ 422,900	(20.9%)

Operating expenses, comprised primarily of advertising, selling and general and administrative expenses, decreased \$712,200 in 2008, when compared to 2007. The various components of operating expenses are discussed below.

Advertising expenses for 2008 were \$345,300 compared to \$332,800 for the comparable period of 2007, an increase of \$12,500 or 3.8%. As in prior years, we have limited advertising as part of our costs reduction efforts.

Selling expenses for 2008 were \$4,943,100 compared to \$5,433,500 for 2007, a decrease of \$490,400 or 9.0%. That decrease was comprised of a \$93,700 decrease in royalty fees due to cancellation of a direct licensing contract related to our cosmetic products containing hydroxy-acids (products which are now manufactured under a pass-through license from our supplier of these materials), a decrease of \$170,200 in promotional displays and products, brokerage fees, freight expense and business insurance associated with fewer sales in 2008 compared to 2007, a decrease in salaries, fringe benefits and related travel expense of \$79,400 primarily resulting from a reduction in salaries and personnel in 2008 versus 2007, a \$84,300 decrease in consumer rebates and associated postage related to a direct rebate program introduced in 2007, a decrease of \$38,900 in telephone expenses primarily related to the elimination of an outside call center service in early 2008, and a net decrease in other selling expenses, none of which by itself is significant, of \$23,900.

General and administrative expenses for 2008 were \$2,760,500 compared to \$2,994,800 for 2007, a decrease of \$234,300 or 7.8%. That decrease was primarily attributable to a decrease in legal, audit and other professional fees of \$161,600, a decrease of \$22,200 in salaries and fringe benefits and related travel expense resulting from a reduction in salaries and personnel, and a net decrease in other general and administrative expenses, none of which by itself is significant, of \$50,500. Early in the fourth quarter of 2008 we reduced our selling and general administrative staff and decreased the compensation of some of our executive officers. We expect this cost cutting to save the Company approximately \$225,000 on an annual basis.

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Interest expense for 2008 was \$334,600 versus \$422,900 for the comparable period of 2007. Interest expense decreased because of lower interest rates, offset by increased borrowing levels during the fourth quarter of 2008. Interest expense may increase in future periods with the addition of the line of credit established in November 2008. See *Liquidity and Capital Resources* below. Interest and other income for 2008 was \$23,000 as compared to \$72,300 of interest income for 2007 and consists of interest earned on our cash reserves.

During 2008 and 2007, expenditures for research and development were not material (under 2% of revenues).

### *Liquidity and Capital Resources*

#### *Citywide Loan*

On June 28, 2006, we entered into a loan with a fifteen year amortization with Citywide Banks for \$5,156,600 secured by the land, building and fixtures at our Denver, Colorado facilities. Interest on the bank loan (5.0% at December 31, 2008) is at the prime rate as published in The Wall Street Journal, adjusted annually each June. This loan requires 180 monthly payments, currently of approximately \$42,000, which commenced on July 28, 2006. The loan agreement contains a number of covenants, including the requirement for maintaining a current ratio of at least 1:1 and a ratio of consolidated long-term debt to consolidated net worth of not more than 1:1. We may not declare any dividends that would result in a violation of either of these covenants. The foregoing requirements were met at the end of 2008.

#### *Financing Agreement*

On November 3, 2008, effective as of October 31, 2008, we entered into a financing agreement with an asset-based lender for the purpose of improving working capital. An amendment to this agreement was executed March 12, 2009 extending the initial anniversary date to March 12, 2010. The agreement provides for up to \$1,200,000 and is secured primarily by accounts receivable, inventory, any lease in which we are a lessor, all investment property and guarantees by our active subsidiaries. Under the financing agreement, the lender will make loans at our request and in the lender's discretion (a) based on purchases of our Accounts by the lender, with recourse against us and an advance rate of 70% (or such other percentage determined by the lender in its discretion), and (b) based on Acceptable Inventory not to exceed certain amounts, including an aggregate maximum of \$250,000. The term of the agreement is one year, renewable for additional one-year terms unless either party provides written notice of non-renewal at least 60 days prior to the end of the current financing period. Advances under the agreement bear interest at a rate of 1% over the prime rate (as published in the Wall Street Journal) for the accounts receivable portion of the advances and 3% over the prime rate for the inventory portion of the borrowings. The prime rate (3.25% as of December 31, 2008) adjusts with changes to the rate. In addition there are collateral management fees of 0.28% for each 10-day period that an advance on an accounts receivable invoice remains outstanding and a 1.35% collateral management fee on the average monthly loan outstanding on the inventory portion of any advance. The agreement provides that no change in control concerning us or any of our active subsidiaries shall occur except with the prior written consent of the lender. Events of default include, but are not limited to, the failure to make a payment when due or a default occurring on any indebtedness of ours. See Note 1(f) regarding the accounting treatment of funds obtained under this agreement.

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*Liquidity*

During 2008, our working capital decreased by \$1,149,200, and concomitantly, our current ratio (current assets divided by current liabilities) decreased from 1.9:1 at December 31, 2007 to 1.6:1 at December 31, 2008. This decrease in working capital is attributable to a net loss in 2008 of \$1,497,000, reduction in long-term debt of \$300,300, offset by depreciation and amortization in excess of capital additions of \$546,300, the exercise of stock options for \$9,200, and the granting of stock options valued at \$67,000 and the issuance of stock to the Employee Stock Option Plan totaling \$25,400, the latter two items requiring no outlay of cash.

At December 31, 2008, trade and other receivables were \$570,300 versus \$1,037,400 at the end of 2007, largely because sales in the last quarter of 2008 were less than those of the last quarter of 2007 due in large part to a reduction in holiday display orders for Montagne Jeunesse products from retailers in 2008. Accounts payable decreased from the end of 2007 through the end of 2008 by \$211,500 corresponding primarily with the decrease and timing of purchases of inventory over that period. At December 31, 2008 inventories were \$300,000 less than at December 31, 2007, primarily due to a decrease in household products inventory as a result of a decrease in our Touch of Scent product sales and the timing of inventory purchases. Prepaid expenses decreased from the end of 2007 by \$117,400 primarily due to a decrease in prepaid promotional expenses.

In spite of current economic conditions in the United States, our management expects net sales in 2009 will be on a par, or close to on a par, with net sales in 2008. This sales projection involves, among other things, the following matters. Sales of Scott's Liquid Gold for wood have remained relatively steady in 2008 compared to 2007; we expect the sales of this product in 2009 to be approximately the same as in 2008. Our wood wash product could provide some small growth. The Mold Control 500 sales are at a relatively low level, which we should be able to maintain. In 2009, Montagne Jeunesse is expected to be offered for sale in a greater number of stores operated by some existing customers, as well as in the stores of a few retail chains which did not carry the product in 2008. The sales impact resulting from this distribution expansion is expected to be offset in full or in part by a reduction in the number of product variants that these customers carried prior to 2009. As a result, Montagne Jeunesse net sales in 2009 are expected to remain approximately the same as in 2008, with limited or no holiday displays as was the case in 2008. Alpha Hydrox products are now distributed at a limited number of retailers, where marketing and support costs are manageable, as well as being sold on our internet site. Our Diabetic cream products continue at a level similar to 2008 as they continue to react to product sampling efforts. Massage oils continue to perform satisfactorily at Wal-Mart. We also have the planned introduction of a screen cleaner which will provide additional sales volume in 2009.

Our management also expects that the cost of goods will increase only moderately in 2009 compared to 2008. The increase results from a substantial increase in the costs of steel cans, offset in part by anticipated lower prices for oils used in our Scott's Liquid Gold for wood products and possibly a decrease in freight costs as fuel prices decline. We have also reduced our operating costs through the elimination or consolidation of staffing and compensation reductions or freezes. Thus we expect that operating costs in 2009 to remain about the same as or somewhat below 2008 operating costs.

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As indicated above, we have in place a financing agreement, for working capital, with Summit Financial Resources, an asset-based lender. The agreement is for up to \$1.2 million and is expected to provide working capital which may be necessary to meet the needs of the Company for 2009. We have, in general, high quality accounts receivable which may be sold pursuant to this agreement. The Summit Financial Resources agreement has a term of one year which expires March 12, 2010; however, it is automatically renewed for 12 months unless either party elects to cancel in writing at least 60 days prior to the anniversary date. We have no intention to exercise this cancellation right, and the lender has not given any indication that they have any such intentions.

We have no significant capital expenditures planned for 2009.

As a result of the foregoing, we expect that our available cash, projected cash flows from operating activities, and borrowing available under the Summit Financial Resources agreement will fund the next twelve months cash requirements, ending December 31, 2009.

In order to improve our liquidity and our operating results, we will also continue to pursue the following steps: the sale of all or a portion of our real estate which we have listed with a real estate firm (see Item 2. Property above), efforts to improve revenues, a further reduction in our fixed operating expense if needed, and potentially the addition of external financing.

Our dependence on operating cash flow means that risks involved in our business can significantly affect our liquidity. Any loss of a significant customer, any further decreases in distribution of our skin care or household products, any new competitive products affecting sales levels of our products, or any significant expense not included in our internal budget could result in the need to raise cash. We have no arrangements for any additional external financing of debt or equity, and we are not certain whether any such financing would be available on acceptable terms. In order to improve our operating cash flow, we need to achieve profitability. Please see Risk Factors in Item 1 above.

The following table sets forth our contractual obligations in the aggregate. We have no capital lease obligations, unconditional purchase obligations or other long-term contractual obligations. Our long-term debt interest rate is a variable rate. The table below assumes a 5.0% annual interest rate for our long-term debt.

**CONTRACTUAL OBLIGATIONS**

	Payments due by Period				
	Total	Less than 1-Year	1 3 Years	4 5 Years	After 5 Years
Long-term debt, including interest	\$ 6,283,900	\$ 502,700	\$ 1,508,100	\$ 1,005,400	\$ 3,267,700
Operating lease obligations	182,000	82,900	89,300	9,800	
<b>Total Contractual Cash Obligations</b>	<b>\$ 6,465,900</b>	<b>\$ 585,600</b>	<b>\$ 1,597,400</b>	<b>\$ 1,015,200</b>	<b>\$ 3,267,700</b>

**Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

Not applicable.

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**Item 8. Financial Statements and Supplementary Data.**

**Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Shareholders of Scott's Liquid Gold-Inc.

We have audited the accompanying consolidated balance sheets of Scott's Liquid Gold-Inc. and subsidiaries (the Company) as of December 31, 2008 and 2007, and the related consolidated statements of operations, shareholders' equity and comprehensive income (loss), and cash flows for each of the years in the two-year period ended December 31, 2008. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Scott's Liquid Gold-Inc. and subsidiaries as of December 31, 2008 and 2007, and the results of their operations and their cash flows for each of the years in the two-year period ended December 31, 2008, in conformity with U.S. generally accepted accounting principles.

/s/ EHRHARDT KEEFE STEINER & HOTTMAN PC

Denver, Colorado

March 16, 2009

**Table of Contents****Consolidated Statements of Operations**

	<b>Year ended December 31,</b>	
	<b>2008</b>	<b>2007</b>
Net sales	\$ 15,911,800	\$ 17,918,500
Operating costs and expenses:		
Cost of sales	9,048,300	10,117,600
Advertising	345,300	332,800
Selling	4,943,100	5,433,500
General and administrative	2,760,500	2,994,800
	17,097,200	18,878,700
Loss from operations	(1,185,400)	(960,200)
Interest income	23,000	72,300
Interest expense	(334,600)	(422,900)
Loss before income taxes	(1,497,000)	(1,310,800)
Income tax expense (Note 5)		
Net loss	\$ (1,497,000)	\$ (1,310,800)
Net loss per common share (Note 7):		
Basic	\$ (0.14)	\$ (0.12)
Diluted	\$ (0.14)	\$ (0.12)
Weighted average shares outstanding:		
Basic	10,621,300	10,543,400
Diluted	10,621,300	10,543,400

See accompanying notes to consolidated financial statements.

**Table of Contents****Consolidated Balance Sheets**

	<b>December 31,</b>	
	<b>2008</b>	<b>2007</b>
<b>ASSETS</b>		
<b>Current assets:</b>		
Cash and cash equivalents	\$ 909,900	\$ 1,483,300
Investment securities	4,500	50,400
Trade receivables, net of allowance of \$59,800 and \$62,900 for doubtful accounts	349,600	1,004,900
Other receivables	220,700	32,500
Inventories, net (Note 2)	2,754,500	3,054,500
Prepaid expenses	120,700	238,100
<b>Total current assets</b>	<b>4,359,900</b>	<b>5,863,700</b>
Property, plant and equipment, net (Note 3)	12,081,900	12,624,000
Other assets	51,100	55,400
	<b>\$ 16,492,900</b>	<b>\$ 18,543,100</b>
<b>LIABILITIES AND SHAREHOLDERS EQUITY</b>		
<b>Current liabilities:</b>		
Accounts payable	\$ 1,348,800	\$ 1,560,300
Accrued payroll and benefits	691,800	866,200
Other accrued expenses	353,100	390,500
Current maturities of long-term debt (Note 4)	273,600	204,900
<b>Total current liabilities</b>	<b>2,667,300</b>	<b>3,021,900</b>
Long-term debt, net of current maturities (Note 4)	4,371,300	4,671,600
<b>Total liabilities</b>	<b>7,038,600</b>	<b>7,693,500</b>
<b>Commitments and contingencies (Notes 4, 6, 9 and 10)</b>		
<b>Shareholders equity (Note 6):</b>		
Common stock; \$.10 par value, authorized 50,000,000 shares; issued and outstanding 10,695,000 shares (2008), and 10,575,000 shares (2007)	1,069,500	1,057,500
Capital in excess of par	5,179,700	5,090,100
Accumulated comprehensive income	500	400
Retained earnings	3,204,600	4,701,600
<b>Shareholders equity</b>	<b>9,454,300</b>	<b>10,849,600</b>
	<b>\$ 16,492,900</b>	<b>\$ 18,543,100</b>

See accompanying notes to consolidated financial statements.



**Table of Contents****Consolidated Statements of Shareholders Equity and Comprehensive Income (Loss)**

Years ended December 31, 2008, 2007	Common Stock		Capital in Excess of Par	Accumulated Comprehensive Income (loss)	Retained Earnings	Comprehensive Income (loss)
	Shares	Amount				
Balance, December 31, 2006	10,533,000	\$ 1,053,300	\$ 5,015,800	\$ 1,100	\$ 6,012,400	
Stock issued to ESOP Plan	42,000	4,200	31,400			
Stock options granted			42,900			
Unrealized loss on investment securities				(700)		\$ (700)
Net loss					(1,310,800)	(1,310,800)
Balance, December 31, 2007	10,575,000	\$ 1,057,500	\$ 5,090,100	\$ 400	\$ 4,701,600	
Total comprehensive loss						\$ (1,311,500)
Stock option exercised	20,000	2,000	7,200			
Stock issued to ESOP Plan	100,000	10,000	15,400			
Stock options granted			67,000			
Unrealized gain on investment securities				100		\$ 100
Net loss					(1,497,000)	(1,497,000)
Balance, December 31, 2008	10,695,000	\$ 1,069,500	\$ 5,179,700	\$ 500	\$ 3,204,600	
Total comprehensive loss						\$ (1,496,900)

See accompanying notes to consolidated financial statements.

**Table of Contents****Consolidated Statements of Cash Flows**

	<b>Year ended December 31,</b>	
	<b>2008</b>	<b>2007</b>
<b>Cash Flows from Operating Activities:</b>		
Net loss	\$ (1,497,000)	\$ (1,310,800)
Adjustments to reconcile net loss to net cash provided (used) by operating activities:		
Depreciation and amortization	560,300	603,400
Stock issued to ESOP	25,400	35,600
Stock options granted	67,000	42,900
Change in assets and liabilities:		
Trade and other receivables, net	216,000	(238,200)
Inventories, net	300,000	236,900
Prepaid expenses and other assets	113,300	(76,500)
Accounts payable and accrued expenses	(423,100)	(360,100)
Total adjustments to net loss	859,000	244,000
<b>Net Cash Used by Operating Activities</b>	<b>(638,000)</b>	<b>(1,066,800)</b>
<b>Cash Flows from Investing Activities:</b>		
Proceeds from sale of securities	50,000	
Purchases of property, plant and equipment	(14,000)	(63,400)
<b>Net Cash Provided (Used) by Investing Activities</b>	<b>36,000</b>	<b>(63,400)</b>
<b>Cash Flows from Financing Activities:</b>		
Proceeds from sale of accounts receivable	251,000	
Principal payments on long-term borrowings	(231,600)	(190,600)
Proceeds from exercise of stock option	9,200	
<b>Net Cash Provided (Used) by Financing Activities</b>	<b>28,600</b>	<b>(190,600)</b>
<b>Net Decrease in Cash and Cash Equivalents</b>	<b>(573,400)</b>	<b>(1,320,800)</b>
Cash and Cash Equivalents, beginning of year	1,483,300	2,804,100
<b>Cash and Cash Equivalents, end of year</b>	<b>\$ 909,900</b>	<b>\$ 1,483,300</b>
Supplemental disclosures:		
Cash paid during the year for:		
Interest	\$ 336,100	\$ 423,000
Income taxes	\$	\$ 3,600

See accompanying notes to consolidated financial statements.

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### **Note 1. Organization and Summary of Significant Accounting Policies**

#### **(a) Company Background and Management's Plans**

Scott's Liquid Gold-Inc. (a Colorado corporation) was incorporated on February 15, 1954. Scott's Liquid Gold-Inc. and its wholly owned subsidiaries (collectively, we or our) manufacture and market quality household and skin care products, and we fill, package and market our Mold Control 500 product. Since the first quarter of 2001, we have acted as a distributor in the United States of beauty care products contained in individual sachets and manufactured by Montagne Jeunesse. In 2006 and 2007, we began the distribution of certain other products. Our business is comprised of two segments, household products and skin care products.

We have experienced significant losses over an extended number of years and have used a significant amount of our cash reserves to fund operations and debt service. To address these trends, management has implemented cost reduction initiatives, entered into a new financing agreement (Note 4) and continues to focus on old and new product sales and distribution at improved margins to increase our cash provided by operations.

As a result of the foregoing, the Company expects that available cash, projected cash flows from operating activities, and borrowing available under the Summit Financial Resources financing agreement will fund the cash requirements for the year ending December 31, 2009.

#### **(b) Principles of Consolidation**

Our consolidated financial statements include our accounts and those of our wholly-owned subsidiaries. All intercompany accounts and transactions have been eliminated.

#### **(c) Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the 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. Significant estimates include, but are not limited to, realizability of deferred tax assets, reserves for slow moving and obsolete inventory, customer returns and allowances, coupon redemptions, and bad debts.

#### **(d) Cash Equivalents**

We consider all highly liquid investments with an original maturity of three months or less at the date of acquisition to be cash equivalents.

#### **(e) Investments in Marketable Securities**

We account for investments in marketable securities in accordance with Statement of Financial Accounting Standards (SFAS) No. 115 Accounting for Certain Investments in Debt and Equity Securities, which requires that we classify investments in marketable securities according to management's intended use of such investments. We invest our excess cash and have established guidelines relative to diversification and maturities in an effort to maintain safety and liquidity. These guidelines are periodically reviewed and modified to take advantage of trends in yields and interest rates. We consider all investments as available for use in our

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current operations and, therefore, classify them as short-term, available-for-sale investments. Available-for-sale investments are stated at fair value, with unrealized gains and losses, if any, reported net of tax, as a separate component of shareholders' equity and comprehensive income (loss). The cost of the securities sold is based on the specific identification method. Investments in corporate and government securities as of December 31, 2008, are scheduled to mature within one year.

**(f) Sale of Accounts Receivable**

We have adopted SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities (SFAS 140). SFAS 140 provides consistent standards for distinguishing transfers of financial assets that are sales from transfers that are secured borrowings. On November 3, 2008, effective as of October 31, 2008, we established a \$1,200,000 factoring line with an asset-based lender (Lender) and secured by accounts receivable, inventory, any lease in which we are a lessor, all investment property and guarantees by our active subsidiaries. This facility enables us to sell selected accounts receivable invoices to the Lender with full recourse against us. These transactions qualify for a sale of assets since (1) we have transferred all of our rights, title and interest in the selected accounts receivable invoices to the Lender, (2) the Lender may pledge, sell or transfer the selected accounts receivable invoices, and (3) we have no effective control over the selected accounts receivable invoices since we are not entitled to or obligated to repurchase or redeem the invoices before their maturity and we do not have the ability to unilaterally cause the Lender to return the invoices. Under SFAS 140, after a transfer of financial assets, an entity recognizes the financial and servicing assets it controls and the liabilities it has incurred, derecognizes financial assets when control has been surrendered, and derecognizes liabilities when extinguished. During 2008, we sold approximately \$358,000 of our accounts receivable invoices to the Lender under a financing agreement for approximately \$251,000. Pursuant to the provisions of SFAS 140, we reflected the transaction as a sale of assets and established an accounts receivable from the Lender for the retained amount less the costs of the transaction and less any anticipated future loss in the value of the retained asset. The retained amount is equal to 30% of the total accounts receivable invoice sold to the Lender less 1.12% of the total invoice as an administrative fee plus a daily finance fee, based on Wall Street Journal prime plus 1% (4.25% at December 31, 2008), imposed on (a) the net of the outstanding accounts receivable invoices less (b) any retained amounts due to us. The estimated future loss reserve for each receivable included in the estimated value of the retained asset is based on the payment history of the customer. Included in Other receivables at December 31, 2008, we have an outstanding retained receivable of approximately \$78,400 representing 30% of \$261,400 of unsettled receivable invoices sold to the Lender as well as \$123,100 due to us resulting from customer remittances paid direct to the Lender on invoices which were not sold to the Lender. Also, at December 31, 2008, approximately \$1,017,000 of this credit line was available for future factoring of accounts receivable invoices. See Note 4 regarding this agreement.

**(g) Inventories**

Inventories consist of raw materials and finished goods and are stated at the lower of cost (first-in, first-out method) or market. We record a reserve for slow moving and obsolete products and raw materials. We estimate reserves for slow moving and obsolete products and raw materials based upon historical and anticipated sales. Amounts are stated in Note 2.

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### **(h) Property, Plant and Equipment**

Property, plant and equipment are recorded at historical cost. Depreciation is provided using the straight-line method over estimated useful lives of the assets ranging from three to forty-five years. Building structures and building improvements are estimated to have useful lives of 35 to 45 years and 3 to 20 years, respectively. Production equipment and production support equipment are estimated to have useful lives of 15 to 20 years and 3 to 10 years, respectively. Office furniture and office machines are estimated to have useful lives 10 to 20 and 3 to 5 years, respectively. Carpeting, drapes and company vehicles are estimated to have useful lives of 5 to 10 years. Maintenance and repairs are expensed as incurred. Improvements that extend the useful lives of the assets or provide improved efficiency are capitalized.

### **(i) Financial Instruments**

Financial instruments which potentially subject us to concentrations of credit risk include cash and cash equivalents, investments in marketable securities, and trade receivables. We maintain our cash balances in the form of bank demand deposits with financial institutions that management believes are creditworthy. As of the balance sheet date and periodically throughout the year, the Company has maintained balances in various operating accounts in excess of federally insured limits. We establish an allowance for doubtful accounts based upon factors surrounding the credit risk of specific customers, historical trends and other information. We have no significant financial instruments with off-balance sheet risk of accounting loss, such as foreign exchange contracts, option contracts or other foreign currency hedging arrangements.

The recorded amounts for cash and cash equivalents, receivables, other current assets, and accounts payable and accrued expenses approximate fair value due to the short-term nature of these financial instruments. The fair value of investments in marketable securities is based upon quoted market value. Our long-term debt bears interest at a fixed rate that adjusts annually on the anniversary date to a then prime rate. The carrying value of long-term debt approximates fair value as of December 31, 2008 and December 31, 2007.

### **(j) Long-Lived Assets**

We account for long-lived assets in accordance with the provisions of SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. This Statement requires that long-lived assets and certain identifiable intangibles be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

### **(k) Income Taxes**

We account for income taxes in accordance with the provisions of SFAS No. 109, *Accounting for Income Taxes*, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences attributable to differences between the financial statement carrying amounts of assets and liabilities and their respective income tax bases. A valuation allowance is provided when it is more likely than not that some portion or all of a deferred tax asset will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the period in which related temporary differences become deductible. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled.

**Table of Contents****(l) Revenue Recognition**

Revenue is recognized when an arrangement exists to sell our product, we have delivered such product in accordance with that arrangement, the sales price is determinable, and collectibility is probable. Reserves for estimated market development support, pricing allowances and returns are provided in the period of sale as a reduction of revenue. Reserves for returns and allowances are recorded as a reduction of revenue, and are maintained at a level that management believes is appropriate to account for amounts applicable to existing sales. Reserves for coupons and certain other promotional activities are recorded as a reduction of revenue at the later of the date at which the related revenue is recognized or the date at which the sales incentive is offered. At December 31, 2008 and 2007 approximately \$600,000 and \$695,700, respectively, had been reserved as a reduction of accounts receivable, and approximately \$23,000 and \$27,000, respectively, had been reserved as current liabilities. Co-op advertising, marketing funds, slotting fees and coupons are deducted from gross sales and totaled \$1,510,100, and \$2,294,700 in 2008 and 2007, respectively.

**(m) Advertising Costs**

Advertising costs are expensed as incurred.

**(n) Stock-based Compensation**

During 2008, we granted 450,800 options for shares of our common stock to employees and directors at an average exercise price of \$0.29 per share. The options which vest ratably over forty-eight months, or upon a change in control, and which expire after five years, were granted at or above the market value as of the date of grant.

The weighted average fair market value of the options granted in 2008 was estimated on the date of grant, using a Black-Scholes option pricing model with the following assumptions:

Expected life of options	4.5 years
Average risk-free interest rate	2.4%
Average expected volatility of stock	75%
Expected dividend rate	None

Compensation cost related to stock options recognized in operating results (included in general and administrative expenses) under SFAS 123R was \$67,000 in the year ended December 31, 2008. Approximately \$193,000 of total unrecognized compensation costs related to non-vested stock options is expected to be recognized over the next forty-four months. In accordance with SFAS 123R, there was no tax benefit from recording the non-cash expense as relates to the options granted to employees as these were qualified stock options which are not normally tax deductible. With respect to the non-cash expense associated with the options granted to the non-employee directors, no tax benefit was recognized due to the existence of as yet unutilized net operating losses. At such time as these operating losses have been utilized and a tax benefit is realized from the issuance of non-qualified stock options, a corresponding tax benefit may be recognized.

**(o) Comprehensive Income**

We follow SFAS No. 130, *Reporting Comprehensive Income* which establishes standards for reporting and displaying comprehensive income and its components. Comprehensive income includes all changes in equity during a period from non-owner sources.

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### **(p) Operating Costs and Expenses Classification**

Cost of sales includes costs associated with manufacturing and distribution including labor, materials, freight-in, purchasing and receiving, quality control, internal transfer costs, repairs, maintenance and other indirect costs, as well as warehousing and distribution costs. We classify shipping and handling costs comprised primarily of freight-out and nominal outside warehousing costs as a component of selling expense on the accompanying Consolidated Statement of Operations. Shipping and handling costs totaled \$1,561,800 and \$1,596,500, for the years ended December 31, 2008 and 2007, respectively.

Selling expenses consist primarily of shipping and handling costs, wages and benefits for sales and sales support personnel, travel, brokerage commissions, promotional costs, as well as other indirect costs.

General and administrative expenses consist primarily of wages and benefits associated with management and administrative support departments, business insurance costs, professional fees, office facility related expenses, and other general support costs.

### **(q) Recently Issued Accounting Pronouncements**

In December 2007 the Financial Accounting Standards Board (FASB) issued SFAS No. 141R, *Business Combinations*. This statement replaces SFAS 141 and defines the acquirer in a business combination as the entity that obtains control of one or more businesses in a business combination and establishes the acquisition date as the date that the acquirer achieves control. SFAS No. 141R requires an acquirer to recognize the assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree at the acquisition date, measured at their fair values as of that date. SFAS No. 141R also requires the acquirer to recognize contingent consideration at the acquisition date, measured at its fair value at that date. This statement is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. Earlier adoption was prohibited. The adoption of this statement did not have a material effect on the Company's financial statements.

In December 2007, the Financial Accounting Standards Board (FASB) issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements - an Amendment of ARB No. 51*. This statement amends ARB 51 to establish accounting and reporting standards for the Noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. This statement is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. Earlier adoption is prohibited. The adoption of this statement is not expected have a material effect on the Company's future reported financial position or results of operations.

In February 2007, the Financial Accounting Standards Board ( FASB ) issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities - Including an Amendment of FASB Statement No. 115*. This statement permits entities to choose to measure certain financial instruments and liabilities at fair value. Most of the provisions of SFAS No. 159 apply only to entities that elect the fair value option. However, the amendment to SFAS No. 115 *Accounting for Certain Investments in Debt and Equity Securities* applies to all entities with available-for-sale and trading securities. SFAS No. 159 is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. The adoption of this statement did not have a material effect on the Company's financial statements.

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In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements ( SFAS No. 157 ). This Statement defines fair value as used in numerous accounting pronouncements, establishes a framework for measuring fair value in generally accepted accounting principles ( GAAP ) and expands disclosure related to the use of fair value measures in financial statements. SFAS No. 157 does not expand the use of fair value measures in financial statements, but standardizes its definition and guidance in GAAP. The Standard emphasizes that fair value is a market-based measurement and not an entity-specific measurement based on an exchange transaction in which the entity sells an asset or transfers a liability (exit price). SFAS No. 157 establishes a fair value hierarchy from observable market data as the highest level to fair value based on an entity's own fair value assumptions as the lowest level. SFAS No. 157 is effective in fiscal years beginning after November 15, 2007. Adoption of this statement did not have a material impact on our results of operations or financial position.



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## Note 2: Inventories

Inventories, consisting of materials, labor and overhead at December 31 were comprised of the following:

	2008	2007
Finished goods	\$ 1,898,100	\$ 2,178,000
Raw Materials	1,241,300	1,284,200
Inventory reserve for obsolescence	(384,900)	(407,700)
	\$ 2,754,500	\$ 3,054,500

## Note 3: Property, Plant and Equipment

Property, plant and equipment at December 31 were comprised of the following:

	2008	2007
Land	\$ 1,091,500	\$ 1,091,500
Buildings	16,394,300	16,308,900
Production equipment	6,027,200	6,023,000
Office furniture and equipment	1,636,400	1,634,800
Other	34,200	240,600
	25,183,600	25,298,800
Less accumulated depreciation	(13,101,700)	(12,674,800)
	\$ 12,081,900	\$ 12,624,000

Depreciation expense for the years ended December 31, 2008 and 2007, was \$556,000 and \$599,100, respectively.

## Note 4: Debt

We have a term loan agreement in the original amount of \$5,156,600 with a commercial bank. The loan agreement with our bank contains affirmative and negative covenants, including the requirement for maintaining a current ratio of at least 1:1 and a ratio of consolidated long-term debt to consolidated net worth of not more than 1:1 and limits the payment of dividends on common stock.

Long-term debt at December 31 is presented below:

	2008	2007
First mortgage loan, secured by land and buildings due June 28, 2021, principal and interest of \$41,900 payable monthly, the interest rate is based on prime rate as published in the Wall Street Journal and is adjusted annually in June. The interest rate on this loan at December 31, 2008 was 5.00%	\$ 4,644,900	\$ 4,876,500
Less current maturities	273,600	204,900
Long-term debt	\$ 4,371,300	\$ 4,671,600

Maturities of long-term debt for the years 2009 through 2013 are \$273,600, \$287,800, \$302,700, \$317,800, and \$334,900.

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On November 3, 2008, effective as of October 31, 2008, we entered into a financing agreement with an asset-based lender for the purpose of improving working capital. An amendment to this agreement was executed March 12, 2009 extending the initial anniversary date to March 12, 2010. The agreement provides for up to \$1,200,000 and is secured primarily by accounts receivable,

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inventory, any lease in which we are a lessor, all investment property and guarantees by our active subsidiaries. Under the financing agreement, the lender will make loans at our request and in the lender's discretion (a) based on purchases of our Accounts by the lender, with recourse against us and an advance rate of 70% (or such other percentage determined by the lender in its discretion), and (b) based on Acceptable Inventory not to exceed certain amounts, including an aggregate maximum of \$250,000. The term of the agreement is one year, renewable for additional one-year terms unless either party provides written notice of non-renewal at least 60 days prior to the end of the current financing period. Advances under the agreement bear interest at a rate of 1% over the prime rate (as published in the Wall Street Journal) for the accounts receivable portion of the advances and 3% over the prime rate for the inventory portion of the borrowings. The prime rate (3.25% as of December 31, 2008) adjusts with changes to the rate. In addition there are collateral management fees of 0.28% for each 10-day period that an advance on an accounts receivable invoice remains outstanding and a 1.35% collateral management fee on the average monthly loan outstanding on the inventory portion of any advance. The agreement provides that no change in control concerning us or any of our active subsidiaries shall occur except with the prior written consent of the lender. Events of default include, but are not limited to, the failure to make a payment when due or a default occurring on any indebtedness of ours. See Note 1(f) regarding the accounting treatment of funds obtained under this agreement.

## Note 5: Income Taxes

The provision for income tax for the years ended December 31 is as follows:

	2008	2007
Current provision (benefit):		
Federal	\$	\$
State		
Total current provision (benefit)		
Deferred provision (benefit):		
Federal	(539,000)	(373,500)
State	(47,000)	(32,200)
Valuation allowance	586,000	405,700
Total deferred provision (benefit)		
Provision (benefit):		
Federal		
State		
Total provision (benefit)	\$	\$

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Income tax expense (benefit) at the statutory tax rate is reconciled to the overall income tax expense (benefit) as follows:

	2008	2007
Federal income tax at statutory rates	\$ (509,000)	\$ (445,700)
State income taxes, net of federal tax effect	(45,700)	(40,100)
Change in unrecognized benefit	(42,000)	77,500
Other	10,700	2,600
<b>Total</b>	<b>(586,000)</b>	<b>(405,700)</b>
Change in valuation allowance	586,000	405,700
<b>Provision for income taxes</b>	<b>\$</b>	<b>\$</b>

Deferred income taxes are based on estimated future tax effects of differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amount used for income tax purposes given the provision of enacted tax laws. The net deferred tax assets and liabilities as of December 31, 2008 and 2007 are comprised of the following:

	2008	2007
<b>Deferred tax assets:</b>		
Net operating loss carryforwards	\$ 3,338,500	\$ 2,797,500
Tax credit and other carryforwards	208,500	193,600
Trade receivables	22,100	23,300
Inventories	123,900	132,300
Accrued vacation	237,900	247,400
Other	13,800	6,700
<b>Total deferred tax assets</b>	<b>3,944,700</b>	<b>3,400,800</b>
<b>Deferred tax liability:</b>		
Accelerated depreciation for tax purposes	(906,900)	(949,000)
<b>Total deferred tax liabilities</b>	<b>(906,900)</b>	<b>(949,000)</b>
<b>Net deferred tax asset, before allowance</b>	<b>3,037,800</b>	<b>2,451,800</b>
<b>Valuation allowance</b>	<b>(3,037,800)</b>	<b>(2,451,800)</b>
<b>Net deferred tax asset</b>	<b>\$</b>	<b>\$</b>

At December 31, 2008, we had federal net operating loss carryforwards of approximately \$8,480,000 and federal tax credit carryforwards related to research and development efforts of approximately \$208,000, both of which expire over a period ending in 2028. State tax loss carryforwards at December 31, 2008 are approximately \$14,900,000 expiring over a period ending in 2028.

A valuation allowance was established due mainly to the uncertainty relating to the future utilization of net operating loss carryforwards. The valuation allowance was further increased by \$586,000 and \$405,700 for 2008 and 2007, respectively, primarily related to uncertainty as to realization of our operating losses and tax credits for these years. The amount of the deferred tax assets considered realizable could be adjusted in the future based upon changes in circumstances that result in a change in our assessment of our ability to realize those deferred tax assets through the generation of taxable income or other tax events.

On January 1, 2007, we adopted the provisions of FASB Interpretation No. 48 ( FIN 48 ) Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109, Accounting for Income Taxes . FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to



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be taken in a tax return. It requires that we recognize in our consolidated financial statements, only those tax positions that are more-likely-than-not of being sustained as of the adoption date, based on the technical merits of the position. As a result of the implementation of FIN 48, we perform each year a comprehensive review of our material tax positions in accordance with recognition and measurement standards established by FIN 48.

As a result of this review, we identified certain deferred tax assets that need to be adjusted. As of January 1, 2007, the date of adoption of FIN 48, our uncertain tax benefits totaled approximately \$295,200. As of December 31, 2008 and December 31, 2007, this amount had reduced to approximately \$95,900 and \$209,200, respectively.

Balance at January 1, 2008	\$ 209,200
Additions based on tax positions related to current year	
Additions for tax positions of prior years	
Reductions for tax positions of prior years	(113,300)
 Balance at December 31, 2008	 \$ 95,900

Due to our net operating loss position and valuation allowance against our net deferred tax assets, the recognition of the unrecognized tax benefits detailed above would not affect our effective tax rate. We do not expect that the amount of unrecognized benefits will change significantly within the next 12 months.

Our policy is to recognize interest and penalties related to uncertain tax benefits in income tax expense. As a result of our net operating loss carryforward position, we have no accrued interest or penalties related to uncertain tax positions as of January 1, 2007, December 31, 2007, or December 31, 2008.

We and our subsidiaries are subject to the following material taxing jurisdictions: U.S. federal and Colorado. The tax years that remain open to examination by the U.S. Internal Revenue Service are years 2005 through 2008. The tax years that remain open to examination by the state of Colorado are years 2004 through 2008.

However, due to net operating loss carryforwards from prior periods, the Internal Revenue Service could potentially review the losses related to years back to 2000.

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Note 6: Shareholders Equity

In 1997, an incentive stock option plan was adopted for our employees. This plan expired on November 7, 2007. Accordingly no shares are available for the grant of options under that plan. In 1998 and 2005, stock option plans for our employees, officers and directors were adopted. The 1998 plan expired on November 27, 2008. Accordingly no shares are available for the grant of options under that plan. All of the plans permitted us to grant options up to an aggregate of 2,900,000 shares of common stock. Options are granted at not less than fair market value of the stock on the date of grant and are exercisable for up to ten years from the grant date. All options granted through 2006 have been vested on the date of grant. The options granted in 2007 and 2008 are vested each month over a four-year period or upon a change in control.

	1997 Plan		1998 Plan		2005 Plan	
	Number of Shares	Average Option Price Per Share	Number of Shares	Average Option Price Per Share	Number of Shares	Average Option Price Per Share
Maximum number of shares under the plans	300,000		1,100,000		1,500,000	
Outstanding,						
December 31, 2006	53,000	\$ 0.54	980,100	\$ 0.67	513,000	\$ 0.59
Granted in 2007	287,750	0.82	167,900	0.83	86,900	0.82
Exercised						
Cancelled/Expired	(53,000)	0.57	(79,500)	0.66	(14,000)	0.54
Outstanding,						
December 31, 2007	287,750	\$ 0.81	1,068,500	\$ 0.70	585,900	\$ 0.62
Granted in 2008			139,000	0.55	311,750	0.17
Exercised			(20,000)	0.46		
Cancelled/Expired	(30,250)	0.81	(474,000)	0.59	(6,000)	0.54
Outstanding,						
December 31, 2008	257,500	\$ 0.81	713,500	\$ 0.74	891,650	\$ 0.46
Available for issuance,						
December 31, 2008					608,350	

A summary of additional information related to the options outstanding as of December 31, 2008 is as follows:

Range of Exercise Prices	Options Outstanding and Exercisable		
	Number Outstanding	Weighted Average Remaining Contractual Life	Exercise Price
\$ 0.17 \$ 0.96	1,844,250	2.76 years	\$ 0.61
\$ 1.06	18,400	2.92 years	\$ 1.06
Total	1,862,650	2.76 years	\$ 0.62

Subsequent to year-end, on February 26, 2009, 90,000 five-year options were granted to Directors, Officers, and employees at \$0.17 per share. These options will vest over four years or upon a change in control.

We have an Employee Stock Ownership Plan ( Plan ) to provide retirement benefits for our employees. The Plan is designed to invest primarily in our common stock and is non-contributory on the part of our employees. Contributions to the Plan are discretionary as determined by our Board

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of Directors. We expense the cost of contributions to the Plan which amounted to \$25,400 (100,000 shares) in 2008, and \$35,600 (42,000 shares) in 2007. In 2008 and 2007, from authorized and unissued shares, we issued and contributed 100,000 and 42,000 shares respectively of our common stock to the Plan.



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## Note 7: Earnings per Share

We present basic and diluted earnings or loss per share in accordance with SFAS No. 128 Earnings per Share which establishes standards for computing and presenting basic and diluted earnings per share. Per share data is determined by using the weighted average number of common shares outstanding. Common equivalent shares are considered only for diluted earnings per share, unless considered anti-dilutive (as in the years 2008 and 2007). Common equivalent shares, determined using the treasury stock method, result from stock options with exercise prices that are below the average market price of the common stock. A reconciliation of the weighted average number of common shares outstanding is as follows:

	2008	2007
Common shares outstanding, beginning of the year	10,575,000	10,533,000
Common stock issued to ESOP	100,000	42,000
Stock options exercised	20,000	
Common shares outstanding, end of year	10,695,000	10,575,000
Weighted average number of common shares outstanding Common share equivalents	10,621,300	10,543,400
Diluted weighted average number of common shares outstanding	10,621,300	10,543,400

We have authorized 20,000,000 shares of preferred stock issuable in one or more series, none of which is issued or outstanding as of December 31, 2008.

Stock options outstanding which have been excluded from diluted shares outstanding due to their antidilutive effect totaled 1,862,650 at December 31, 2008 and 1,942,150 at December 31, 2007.

## Note 8: Segment Information

We operate in two different segments: household products and skin care products. Our products are sold nationally and internationally (primarily Canada), directly and through independent brokers, to mass merchandisers, drug stores, supermarkets, wholesale distributors and other retail outlets. Management has chosen to organize our business around these segments based on differences in the products sold. The household products segment includes Scott's Liquid Gold for wood, a wood cleaner which preserves as it cleans, Mold Control 500, a mold remediation product, and Touch of Scent room air fresheners. The skin care segment includes Alpha Hydrox, alpha hydroxy acid cleansers and lotions; a retinol product; Diabetic Skin Care, a healing cream and moisturizer developed to address skin conditions of diabetics; and beauty care sachets of Montagne Jeunesse and certain other products distributed by us.

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Accounting policies for our segments are the same as those described in Note 1, Summary of Significant Accounting Policies. Our Management evaluates segment performance based on segment income or loss before profit sharing, bonuses, income taxes and nonrecurring gains and losses. The following provides information on our segments as of and for the years ended December 31:

	2008		2007	
	Household Products	Skin Care Products	Household Products	Skin Care Products
Net sales to external customers	\$ 7,294,100	\$ 8,617,700	\$ 8,051,700	\$ 9,866,800
Income (loss) before profit sharing, bonuses and income taxes	\$ (411,900)	\$ (1,085,100)	\$ 288,500	\$ (1,599,300)
Identifiable assets	\$ 2,968,900	\$ 4,558,200	\$ 2,974,900	\$ 5,646,200

The following is a reconciliation of segment information to consolidated information:

	2008	2007
Net sales to external customers	\$ 15,911,800	\$ 17,918,500
Loss before profit sharing, bonuses and income taxes	\$ (1,497,000)	\$ (1,310,800)
Consolidated loss before income taxes	\$ (1,497,000)	\$ (1,310,800)
Identifiable assets	\$ 7,527,100	\$ 8,621,100
Corporate assets	8,965,800	9,922,000
Consolidated total assets	\$ 16,492,900	\$ 18,543,100

Corporate assets noted above are comprised primarily of our cash and investments, and property and equipment not directly associated with the manufacturing, warehousing, shipping and receiving activities

We attribute our net sales to different geographic areas based on the location of the customer. All of our long-lived assets are located in the United States. For the year ended December 31, revenues for each geographical area are as follows:

	2008	2007
United States	\$ 15,834,300	\$ 17,801,700
Foreign countries	77,500	116,800
Total net sales	\$ 15,911,800	\$ 17,918,500

In 2008 and 2007, one customer accounted for approximately \$5,250,000 and \$6,750,000, respectively, of consolidated net sales. Both segments sell to this customer. This customer is not related to us. The outstanding trade receivable from this same customer accounted for 24.4% and 22.6% of total trade receivables at December 31, 2008 and 2007, respectively. A loss of this customer could have a material adverse effect on us because it is uncertain whether our consumer base served by this customer would purchase our products at other retail outlets. No long-term contracts exist between us and this customer or any other customer.

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Note 9: Retirement Plans

We have a 401(k) Profit Sharing Plan ( 401(k) Plan ) covering our full-time employees who have completed four months of service as defined in the 401(k) Plan, and are age 18 or older. Participants may defer up to 75% of their compensation up to the maximum limit determined by law. We may make discretionary matching contributions up to a maximum of 6% of each participant's compensation, but only for those employees earning no more than \$35,000 annually. Additionally, we can make discretionary profit sharing contributions to eligible employees. Participants are always fully vested in their contributions, matching contributions and allocated earnings thereon. Vesting in our profit sharing contribution is based on years of service, with a participant fully vested after five years. Our Company matching contributions totaled \$4,700 and \$6,500, in 2008 and 2007, respectively. We have made no discretionary profit sharing contributions in 2008 and 2007.

Note 10. Commitments and Contingencies

We have entered into various operating lease agreements, primarily for office equipment. Annual rental expense under these leases totaled \$97,500 and \$100,200, in 2008 and 2007, respectively. Minimum annual rental payments under noncancellable operating leases are approximately \$82,900, \$54,700, and \$25,400 for the years ending December 31, 2009, 2010, and 2011, respectively.

Wayne Taylor, et al. v. The Sherwin-Williams Companies, et al.

The Company was served with a complaint February 25, 2009, naming it as a defendant in this personal injury action filed in the Superior Court of New Jersey, Camden County. Plaintiffs Wayne Taylor and Leslie Taylor, his wife, claim that Mr. Taylor has contracted Acute Myelogenous Leukemia (AML) as a result of work related exposure to benzene and that the Company is one of a minimum 15 co-defendant product manufacturers which used benzene in products sold to Mr. Taylor or his employers and used by Mr. Taylor in his work. Plaintiffs allege exposure to defendants' products containing benzene and that the exposure caused personal injuries, including AML. Fifty John Doe corporations are asserted to be similarly liable. Claims are asserted against all defendants for negligence, breach of warranty, consumer fraud, intentional tort and loss of consortium.

The extent of the defense and indemnity obligations of its product liability insurers is to be determined and is uncertain at this time. The Company has submitted the claim to its product liability insurers and believes that insurers will assume the defense of the claim and retain counsel accordingly. The Company believes that Mr. Taylor was not exposed to benzene as the result of use of the Company's products and intends to vigorously defend the action.

Note 11. Transactions with Related Parties

In 2001, we commenced purchases of the skin care sachets from Montagne Jeunesse under a distributorship agreement covering the United States. Montagne Jeunesse is the sole supplier of that product. Sales of these products represent a significant source of our revenues. On May 4, 2005, our wholly-owned subsidiary, Neoteric Cosmetics, Inc. ( Neoteric ), entered into a new distribution agreement with Montagne Jeunesse International Ltd ( Montagne Jeunesse ) covering our distribution of Montagne Jeunesse products. It replaces a distribution agreement in effect since 2000. In the new agreement, Montagne Jeunesse appoints Neoteric as its exclusive distributor to market and distribute Montagne Jeunesse products in the United States of America. The appointment had an initial term of 18 months, commencing May 3, 2005, and continues in force until terminated by either party by giving to the other party no less than three months' notice in writing of a termination. The principal and controlling owner of Montagne Jeunesse is the managing director and sole owner of Atchinson Investments, Ltd., which owned, to our knowledge, in 2005 more than 5% of our outstanding common stock; to the best of our knowledge, at February 28, 2009, he owned beneficially less than 5.0% of our outstanding common stock.

We adopted a bonus plan for our executive officers for 2008 and 2007. The plan provided that an amount would be distributed to our executive officers equal to 10% of the annual before tax profit exceeding \$1,000,000, excluding items that are infrequent, unusual, or extraordinary. In 2008 and 2007, no bonuses were accrued or paid due to net losses. We will consider the adoption of substantially the same plan for our executive officers in 2009.

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Note 12. Valuation and Qualifying Accounts (in thousands)

	Balance at beginning of year	Additions charged to expense	Deductions	Balance at end of year
<b>Year ended December 31, 2007</b>				
Returns and allowances, market development support and doubtful accounts reserve	\$ 711,000	3,508,600	3,461,000	\$ 758,600
<b>Year ended December 31, 2008</b>				
Returns and allowances, market development support and doubtful accounts reserve	\$ 758,600	2,096,900	2,195,700	\$ 659,800

**Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.**

None.

**Item 9A(T). Controls and Procedures.**

## Disclosure Controls and Procedures

As of December 31, 2008, we conducted an evaluation, under the supervision and with the participation of the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective as of December 31, 2008.

## Management's Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting. A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management, including the Chief Executive Officer and Chief Financial Officer, has conducted an evaluation of the effectiveness of the Company's internal control over financial reporting as of December 31, 2008, based on the criteria for effective internal control described in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on its assessment, management concluded that the Company's internal control over financial reporting was effective as of December 31, 2008.

This Annual Report does not include an attestation report of the Company's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's registered public accounting firm pursuant to temporary rules of the SEC that permit the Company to provide only management's report in this Annual Report.

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This report shall not be deemed to be filed for purposes of Section 18 of the Securities Exchange Act of 1934, or otherwise subject to the liabilities of that section, and is not incorporated by reference into any filing of the Company, whether made before or after the date hereof, regardless of any general incorporation language in such filing.

**Changes in Internal Control over Financial Reporting**

There was no change in our internal control over financial reporting during the quarter ended December 31, 2008 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**Item 9B. Other Information.**

The initial term of the financing agreement with Summit Financial Resources was extended in March 2009 from November 2009 to March 12, 2010. See Note 4 to the consolidated financial statements in Item 8 of this Report.

**PART III**

For Part III, except Item 15, Exhibits, Financial Statement Schedules, the information set forth in our definitive Proxy Statement for our Annual Meeting of Shareholders to be held in May, 2009, hereby is incorporated by reference into this Report.

**Item 10. Directors, Executive Officers and Corporate Governance.**

**Item 11. Executive Compensation.**

**Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.**

**Item 13. Certain Relationships and Related Transactions, and Director Independence.**

**Item 14. Principal Accounting Fees and Services.**

**Item 15. Exhibits, Financial Statement Schedules.**

Consolidated Financial Statements:

<u>Report of Independent Registered Public Accounting Firm</u>	25
<u>Consolidated Statements of Operations for the years ended December 31, 2008 and 2007</u>	26
<u>Consolidated Balance Sheets as of December 31, 2008 and 2007</u>	27
<u>Consolidated Statements of Shareholders' Equity and Comprehensive Income (Loss) for the years ended December 31, 2008 and 2007</u>	28
<u>Consolidated Statements of Cash Flows for the years ended December 31, 2008 and 2007</u>	29
<u>Notes to Consolidated Financial Statements</u>	30



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Exhibits

<b>Exhibit Number</b>	<b>Document</b>
3.1	Restated Articles of Incorporation, as amended and restated through May 1, 1996, incorporated by reference to Exhibit 3.1 of our Annual Report on Form 10-KSB for the year ended December 31, 2007.
3.2	Bylaws, as amended through February 27, 1996, incorporated by reference to Exhibit 3.2 of our Annual Report on Form 10-K for the year ended December 31, 2004.
4.1	Change in Terms Agreement with Citywide Banks, dated June 28, 2006, between us and Citywide Banks, incorporated by reference to Exhibit 10.1 of our Current Report on Form 8-K filed on June 30, 2006.
4.2	Business Loan Agreement, dated June 28, 2006, between us and Citywide Banks, incorporated by reference to Exhibit 10.2 of our Current Report on Form 8-K filed on June 30, 2006.
4.3	Addendum to Loan Documents, dated June 28, 2006, incorporated by reference to Exhibit 10.3 of our Current Report on Form 8-K filed on June 30, 2006.
4.4	Promissory Note dated June 7, 2006 by us to Citywide Banks; Deed of Trust dated June 7, 2006 among us, Citywide Banks and the Public Trustee of the City and County of Denver, Colorado; Assignment of Rents dated June 7, 2006 between us and Citywide Banks; letter agreement dated June 7, 2006 regarding the change in the amount under the existing bank line of credit with Citywide Banks, incorporated by reference to Exhibit 10.0 of our Current Report on Form 8-K filed on June 12, 2006.
10.1*	Scott's Liquid Gold-Inc. Health and Accident Plan, Plan Document and Summary Plan Description Amended and Restated Effective October 1, 2003 incorporated by reference to Exhibit 10.1 of our Annual Report on Form 10-K for the year ended December 31, 2004.
10.2	Scott's Liquid Gold & Affiliated Companies Employee Benefit Health And Welfare Plan Amendment #1-2004 incorporated by reference to Exhibit 10.2 of our Annual Report on Form 10-K for the year ended December 31, 2004.
10.3*	Indemnification Agreement dated May 6, 1987, between the Registrant and Mark E. Goldstein; Indemnification Agreement dated December 23, 1991, between the Registrant and Dennis H. Field; Amendment to Indemnification Agreement dated January 17, 1992, between the Registrant and Dennis H. Field; Indemnification Agreement, dated July 12, 2000, between the Registrant and Jeffrey R. Hinkle; Indemnification Agreement, dated August 16, 2000, between the Registrant and Carl A. Bellini; Indemnification Agreement, dated November 2, 2000, between the Registrant and Jeffrey B. Johnson; Indemnification Agreement, dated November 20, 2002 between the Registrant and Dennis P. Passantino; Indemnification Agreement, dated January 26, 2004 between the Registrant and Gerald J. Laber, incorporated by reference to Exhibit 10.4 of our Annual Report on Form 10-K for the year ended December 31, 2003; and Indemnification Agreement, dated February 24, 2009 between the Registrant and Brian L. Boberick, incorporated by reference to Exhibit 10.1 of our current report on Form 8-K filed February 27, 2009.

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**Exhibit**

<b>Number</b>	<b>Document</b>
10.4	Agreement dated as of May 3, 2005 between Montagne Jeunesse International Ltd. and Neoteric Cosmetics, Inc., incorporated by reference to Exhibit 10.2 of our Quarterly Report on Form 10-Q for the quarter ended March 31, 2005.
10.5*	Scott's Liquid Gold-Inc. Employee Stock Ownership Plan and Trust Agreement, Amended and Restated Effective January 1, 2001; and Second Amendment to Scott's Liquid Gold-Inc. Employee Stock Ownership Plan, effective as of January 1, 2003, incorporated by reference to Exhibit 10.6 of our annual Report on Form 10-K for the year ended December 31, 2003.
10.6*	Third Amendment to Scott's Liquid Gold-Inc. Employee Stock Ownership Plan, effective March 28, 2005, incorporated by reference to Exhibit 10.1 of our Quarterly Report on Form 10-Q for the quarter ended March 31, 2005.
10.7*	Scott's Liquid Gold-Inc. 1998 Stock Option Plan, incorporated by reference to Exhibit 4.3 of our Registration Statement No. 333-51710, filed with the Commission on December 12, 2000.
10.8*	2005 Stock Incentive Plan, as amended, incorporated by reference to Exhibit 4 of our Registration Statement No. 333-156191, filed with the Commission on December 16, 2008.
10.9	Product Development, Production and Marketing Agreement with Modec, Inc. dated April 4, 2006, incorporated by reference to Exhibit 10.1 of our Quarterly Report on Form 10-Q for the quarter ended June 30, 2006.
10.10	Amendment to Modec Agreement dated November 9, 2007, incorporated by reference to Exhibit 10.12 of our Annual Report on Form 10-KSB for the year ended December 31, 2007.
10.11	Form of 1997 Stock Option Plan Incentive Stock Option Agreement, incorporated by reference to Exhibit 10.2 of our Quarterly Report on Form 10-QSB for the quarter ended March 31, 2007.
10.12	Form of 1998 Stock Option Plan Incentive Stock Option Agreement, incorporated by reference to Exhibit 10.3 of our Quarterly Report on Form 10-QSB for the quarter ended March 31, 2007.
10.13	Form of 2005 Stock Option Plan Incentive Stock Option Agreement, incorporated by reference to Exhibit 10.4 of our Quarterly Report on Form 10-QSB for the quarter ended March 31, 2007.
10.14	Form of 1998 Stock Option Plan Nonqualified Stock Option Agreement, incorporated by reference to Exhibit 10.5 of our Quarterly Report on Form 10-QSB for the quarter ended March 31, 2007.
10.15	Form of 2005 Stock Incentive Plan Nonqualified Stock Option Agreement, incorporated by reference to Exhibit 10.6 of our Quarterly Report on Form 10-QSB for the quarter ended March 31, 2007.
10.16	Financing Agreement and Addendum to Financing Agreement, both dated October 31, 2008, between Summit Financial Resources, L.P. and the Company, incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed with the Commission on November 4, 2008.



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**Exhibit**

**Number Document**

- 10.17 Guarantees, dated October 31, 2008, by SLG Plastics, Inc. Advertising Promotions Incorporated, Colorado Product Concepts, Inc., Neoteric Cosmetics, Inc., and SLG Chemicals, Inc., incorporated by reference to Exhibit 10.2 of the Company's Current Report on Form 8-K filed with the Commission on November 4, 2008.
- 10.18 First Amendment to Financing Agreement dated March 12, 2009 between Summit Financial Resources, L.P. and the Company.
- 21 List of Subsidiaries, incorporated by reference to Exhibit 21 in our Annual Report of Form 10-KSB for the year ended December 31, 2007.
- 23 Consent of Ehrhardt, Keefe, Steiner & Hottman PC.
- 24 Powers of Attorney.
- 31.1 Rule 13a-14(a) Certification of the Chief Executive Officer.
- 31.2 Rule 13a-14(a) Certification of the Chief Financial Officer.
- 32.1 Section 1350 Certification.

\* Management contract or compensatory plan or arrangement

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SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

SCOTT S LIQUID GOLD-INC.,

a Colorado corporation

By: /s/ Mark E. Goldstein  
 Mark E. Goldstein, President and Chief  
 Executive Officer  
 Principal Executive Officer

By: /s/ Brian L. Boberick  
 Brian L. Boberick, Treasurer and  
 Chief Financial Officer  
 Principal Financial Officer and  
 Principal Accounting Officer

Date: March 16, 2009

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

Date	Name and Title	Signature
March 16, 2009	Mark E. Goldstein, Director, President and Chief Executive Officer	) ) ) ) ) )
March 16, 2009	Jeffrey R. Hinkle, Director,	) ) )
March 16, 2009	Dennis P. Passantino, Director	) /s/ Mark E. Goldstein ) Mark E. Goldstein, for himself ) and as Attorney-in-Fact for the ) named directors who together
March 16, 2009	Carl A. Bellini, Director	) constitute all of the members ) of the Board of Directors and ) for the named Officers
March 16, 2009	Dennis H. Field, Director	) ) )
March 16, 2009	Jeffry B. Johnson, Director	) ) )
March 16, 2009	Gerald J. Laber, Director	) ) )
March 16, 2009	Brian L. Boberick, Treasurer and Chief Financial Officer	) ) )

