

Prestige Brands Holdings, Inc.  
Form 10-Q  
November 08, 2007

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**U. S. SECURITIES AND EXCHANGE COMMISSION  
Washington, DC 20549**

**FORM 10-Q**

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

**For the quarterly period ended September 30, 2007**

**or**

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

**For the transition period from \_\_\_\_ to \_\_\_\_**

**Commission File Number: 001-32433**

**PRESTIGE BRANDS HOLDINGS, INC.**

(Exact name of Registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of  
incorporation or organization)

**20-1297589**

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

**90 North Broadway**

**Irvington, New York 10533**

(Address of Principal Executive Offices, including zip code)

**(914) 524-6810**

(Registrant's telephone number, including area code)

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

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

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Large accelerated filer

Accelerated filer

Non-accelerated filer

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

Yes  No

As of October 31, 2007, there were 50,003,321 shares of common stock outstanding.

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**PART I****FINANCIAL INFORMATION****Item 1.****FINANCIAL STATEMENTS**

**Prestige Brands Holdings, Inc.**  
**Consolidated Statements of Operations**  
*(Unaudited)*

| <i>(In thousands, except per share data)</i> | <b>Three Months</b>       |             | <b>Six Months</b>         |             |
|--|---------------------------|-------------|---------------------------|-------------|
|  | <b>Ended September 30</b> |             | <b>Ended September 30</b> |             |
|  | <b>2007</b>               | <b>2006</b> | <b>2007</b>               | <b>2006</b> |
| <b>Revenues</b>                              |                           |             |                           |             |
| Net sales                                    | \$ 86,840                 | \$ 84,033   | \$ 164,881                | \$ 159,600  |
| Other revenues                               | 497                       | 518         | 1,067                     | 874         |
| Total revenues                               | 87,337                    | 84,551      | 165,948                   | 160,474     |
| <b>Cost of Sales</b>                         |                           |             |                           |             |
| Costs of sales                               | 42,770                    | 41,259      | 80,092                    | 77,584      |
| Gross profit                                 | 44,567                    | 43,292      | 85,856                    | 82,890      |
| <b>Operating Expenses</b>                    |                           |             |                           |             |
| Advertising and promotion                    | 11,017                    | 9,455       | 18,803                    | 16,857      |
| General and administrative                   | 10,184                    | 7,259       | 17,830                    | 13,693      |
| Depreciation                                 | 129                       | 219         | 253                       | 439         |
| Amortization of intangible assets            | 2,627                     | 2,193       | 5,254                     | 4,386       |
| Total operating expenses                     | 23,957                    | 19,126      | 42,140                    | 35,375      |
| Operating income                             | 20,610                    | 24,166      | 43,716                    | 47,515      |
| <b>Other income (expense)</b>                |                           |             |                           |             |
| Interest income                              | 173                       | 403         | 360                       | 588         |
| Interest expense                             | (9,768)                   | (10,146)    | (19,642)                  | (20,123)    |
| Total other income (expense)                 | (9,595)                   | (9,743)     | (19,282)                  | (19,535)    |
| Income before provision for income taxes     | 11,015                    | 14,423      | 24,434                    | 27,980      |
| Provision for income taxes                   | 4,186                     | 5,639       | 9,285                     | 10,940      |
| Net income                                   | \$ 6,829                  | \$ 8,784    | \$ 15,149                 | \$ 17,040   |
| <b>Basic earnings per share</b>              |                           |             |                           |             |
| Basic earnings per share                     | \$ 0.14                   | \$ 0.18     | \$ 0.30                   | \$ 0.35     |
| <b>Diluted earnings per share</b>            |                           |             |                           |             |
| Diluted earnings per share                   | \$ 0.14                   | \$ 0.18     | \$ 0.30                   | \$ 0.34     |
| <b>Weighted average shares outstanding:</b>  |                           |             |                           |             |
| Basic  | 49,710                    | 49,451      | 49,686                    | 49,389      |
| Diluted                                      | 50,046                    | 49,994      | 50,042                    | 49,991      |

*See accompanying notes.*



**Prestige Brands Holdings, Inc.**  
**Consolidated Balance Sheets**  
*(Unaudited)*

*(In thousands)*

|   | September 30,<br>2007 | March 31,<br>2007 |
|---|-----------------------|-------------------|
| <b>Assets</b>                             |                       |                   |
| Current assets                            |                       |                   |
| Cash and cash equivalents                 | \$ 8,799              | \$ 13,758         |
| Accounts receivable                       | 46,512                | 35,167            |
| Inventories                               | 27,783                | 30,173            |
| Deferred income tax assets                | 3,337                 | 2,735             |
| Prepaid expenses and other current assets | 3,628                 | 1,935             |
| Total current assets                      | 90,059                | 83,768            |
| Property and equipment                    |                       |                   |
| Property and equipment                    | 1,391                 | 1,449             |
| Goodwill                                  | 308,915               | 310,947           |
| Intangible assets                         | 651,903               | 657,157           |
| Other long-term assets                    | 8,310                 | 10,095            |
| Total Assets                              | \$ 1,060,578          | \$ 1,063,416      |

**Liabilities and Stockholders' Equity**

|                                   |           |           |
|-----------------------------------|-----------|-----------|
| Current liabilities               |           |           |
| Accounts payable                  | \$ 21,318 | \$ 19,303 |
| Accrued interest payable          | 7,556     | 7,552     |
| Other accrued liabilities         | 12,771    | 10,505    |
| Current portion of long-term debt | 3,550     | 3,550     |
| Total current liabilities         | 45,195    | 40,910    |
| Long-term debt                    |           |           |
| Long-term debt                    | 433,563   | 459,800   |
| Other long-term liabilities       | 2,801     | 2,801     |
| Deferred income tax liabilities   | 117,609   | 114,571   |
| Total Liabilities                 | 599,168   | 618,082   |

**Commitments and Contingencies – Note 13****Stockholders' Equity**

|  |         |         |
|--|---------|---------|
| Preferred stock - \$0.01 par value   |         |         |
| Authorized – 5,000 shares  |         |         |
| Issued and outstanding – None  | --      | --      |
| Common stock - \$0.01 par value  |         |         |
| Authorized – 250,000 shares  |         |         |
| Issued – 50,060 shares   | 501     | 501     |
| Additional paid-in capital   | 380,371 | 379,225 |
| Treasury stock, at cost – 57 shares at September 30, 2007<br>and 55 shares at March 31, 2007 | (44)    | (40)    |
| Accumulated other comprehensive income   | 98      | 313     |
| Retained earnings  | 80,484  | 65,335  |
| Total stockholders' equity   | 461,410 | 445,334 |

|  |    |           |    |           |
|--|----|-----------|----|-----------|
| Total Liabilities and Stockholders' Equity | \$ | 1,060,578 | \$ | 1,063,416 |
|--|----|-----------|----|-----------|

*See accompanying notes.*



**Prestige Brands Holdings, Inc.**  
**Consolidated Statement of Changes in Stockholders' Equity**  
**and Comprehensive Income**  
**Six Months Ended September 30, 2007**  
*(Unaudited)*

|   | <u>Common Stock</u> |        |            | <u>Treasury Stock</u> |         | Accumulated   | Retained  | Totals     |  |
|---|---------------------|--------|------------|-----------------------|---------|---------------|-----------|------------|--|
|   | Par                 |        | Additional | Shares                |         | Other         | Earnings  |            |  |
|   | Shares              |        | Paid-in    | Amount                |         | Comprehensive |           |            |  |
|   | Value               |        | Capital    |                       |         | Income        |           |            |  |
| <i>(In thousands)</i>   |                     |        |            |                       |         |               |           |            |  |
| Balances - March 31, 2007   | 50,060              | \$ 501 | \$ 379,225 | 55                    | \$ (40) | \$ 313        | \$ 65,335 | \$ 445,334 |  |
| Stock-based compensation  | --                  | --     | 1,146      | --                    | --      | --            | --        | 1,146      |  |
| Purchase of common stock for treasury   | --                  | --     | --         | 2                     | (4)     | --            | --        | (4)        |  |
| Components of comprehensive income:   |                     |        |            |                       |         |               |           |            |  |
| Net income  | --                  | --     | --         | --                    | --      | --            | 15,149    | 15,149     |  |
| Amortization of interest rate caps reclassified into earnings, net of income tax expense of \$139 | --                  | --     | --         | --                    | --      | 218           | --        | 218        |  |
| Unrealized loss on interest rate caps, net of income tax benefit of \$277                         | --                  | --     | --         | --                    | --      | (433)         | --        | (433)      |  |
| Total comprehensive income  | --                  | --     | --         | --                    | --      | --            | --        | 14,934     |  |
| Balances – September 30, 2007   | 50,060              | \$ 501 | \$ 380,371 | 57                    | \$ (44) | \$ 98         | \$ 80,484 | \$ 461,410 |  |

See accompanying notes.

**Prestige Brands Holdings, Inc.**  
**Consolidated Statements of Cash Flows**  
*(Unaudited)*

| <i>(In thousands)</i>   | <b>Six Months Ended<br/>September 30</b> |             |
|---|--|-------------|
|   | <b>2007</b>                              | <b>2006</b> |
| <b>Operating Activities</b>   |  |             |
| Net income  | \$ 15,149                                | \$ 17,040   |
| Adjustments to reconcile net income to net cash provided by operating activities: |  |             |
| Depreciation and amortization   | 5,507                                    | 4,825       |
| Deferred income taxes   | 4,622                                    | 6,197       |
| Amortization of deferred financing costs  | 1,561                                    | 1,609       |
| Stock-based compensation  | 1,146                                    | 224         |
| Changes in operating assets and liabilities                                       |  |             |
| Accounts receivable   | (11,345)                                 | 2,595       |
| Inventories   | 2,390                                    | 5,202       |
| Prepaid expenses and other current assets   | (1,692)                                  | (1,047)     |
| Accounts payable  | 1,884                                    | 4,494       |
| Income taxes payable  | --                                       | (1,731)     |
| Accrued liabilities   | 2,270                                    | 3,326       |
| Net cash provided by operating activities   | 21,492                                   | 42,734      |
| <b>Investing Activities</b>   |  |             |
| Purchases of equipment  | (194)                                    | (313)       |
| Purchase of business  | (16)                                     | (31,242)    |
| Net cash used for investing activities  | (210)                                    | (31,555)    |
| <b>Financing Activities</b>   |  |             |
| Repayment of long-term debt   | (26,237)                                 | (8,865)     |
| Purchase of common stock for treasury   | (4)                                      | (6)         |
| Net cash used for financing activities  | (26,241)                                 | (8,871)     |
| Increase (decrease) in cash   | (4,959)                                  | 2,308       |
| Cash - beginning of period  | 13,758                                   | 8,200       |
| Cash - end of period  | \$ 8,799                                 | \$ 10,508   |
| Interest paid   | \$ 18,078                                | \$ 18,306   |
| Income taxes paid   | \$ 5,664                                 | \$ 6,287    |

*See accompanying notes.*

**Prestige Brands Holdings, Inc.**  
**Notes to Consolidated Financial Statements**  
*(Unaudited)*

**1. Business and Basis of Presentation**

***Nature of Business***

Prestige Brands Holdings, Inc. (referred to herein as the “Company” which reference shall, unless the context requires otherwise, be deemed to refer to Prestige Brands Holdings, Inc. and all of its direct or indirect wholly-owned subsidiaries on a consolidated basis) is engaged in the marketing, sales and distribution of over-the-counter healthcare, personal care and household cleaning brands to mass merchandisers, drug stores, supermarkets and club stores primarily in the United States, Canada and certain international markets. Prestige Brands Holdings, Inc. is a holding company with no assets or operations and is also the parent guarantor of the senior secured credit facility and the senior subordinated notes more fully described in Note 8 to the consolidated financial statements.

***Basis of Presentation***

The unaudited consolidated financial statements presented herein have been prepared in accordance with generally accepted accounting principles for interim financial reporting and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by United States generally accepted accounting principles (“GAAP”) for complete financial statements. All significant intercompany transactions and balances have been eliminated. In the opinion of management, the financial statements include all adjustments, consisting of normal recurring adjustments that are considered necessary for a fair presentation of the Company’s consolidated financial position, results of operations and cash flows for the interim periods. Operating results for the three and six month periods ended September 30, 2007 are not necessarily indicative of results that may be expected for the year ending March 31, 2008. This financial information should be read in conjunction with the Company’s financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended March 31, 2007.

***Use of Estimates***

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, as well as the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on the Company’s knowledge of current events and actions that the Company may undertake in the future, actual results could differ materially from those estimates. As discussed below, the Company’s most significant estimates include those made in connection with the valuation of intangible assets, sales returns and allowances, trade promotional allowances and inventory obsolescence.

***Cash and Cash Equivalents***

The Company considers all short-term deposits and investments with original maturities of three months or less to be cash equivalents. Substantially all of the Company’s cash is held by one bank located in Wyoming. The Company does not believe that, as a result of this concentration, it is subject to any unusual financial risk beyond the normal risk associated with commercial banking relationships.

***Accounts Receivable***

The Company extends non-interest bearing trade credit to its customers in the ordinary course of business. The Company maintains an allowance for doubtful accounts receivable based upon historical collection experience and expected collectibility of the accounts receivable. In an effort to reduce credit risk, the Company (i) has established credit limits for all of its customer relationships, (ii) performs ongoing credit evaluations of customers’ financial condition, (iii) monitors the payment history and aging of customers’ receivables, and (iv) monitors open orders

against an individual customer's outstanding receivable balance.

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***Inventories***

Inventories are stated at the lower of cost or fair value, where cost is determined by using the first-in, first-out method. The Company provides an allowance for slow moving and obsolete inventory, whereby it reduces inventories for the diminution of value, resulting from product obsolescence, damage or other issues affecting marketability, equal to the difference between the cost of the inventory and its estimated market value. Factors utilized in the determination of estimated market value include (i) current sales data and historical return rates, (ii) estimates of future demand, (iii) competitive pricing pressures, (iv) new product introductions, (v) product expiration dates, and (vi) component and packaging obsolescence.

***Property and Equipment***

Property and equipment are stated at cost and are depreciated using the straight-line method based on the following estimated useful lives:

|                        | <b>Years</b> |
|------------------------|--------------|
| Machinery              | 5            |
| Computer equipment     | 3            |
| Furniture and fixtures | 7            |
| Leasehold improvements | 5            |

Expenditures for maintenance and repairs are charged to expense as incurred. When an asset is sold or otherwise disposed of, the cost and associated accumulated depreciation are removed from the accounts and the resulting gain or loss is recognized in the consolidated statement of operations.

Property and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. An impairment loss is recognized if the carrying amount of the asset exceeds its fair value.

***Goodwill***

The excess of the purchase price over the fair market value of assets acquired and liabilities assumed in purchase business combinations is classified as goodwill. In accordance with Financial Accounting Standards Board (“FASB”) Statement of Financial Accounting Standards (“Statement”) No. 142, “Goodwill and Other Intangible Assets,” the Company does not amortize goodwill, but performs impairment tests of the carrying value at least annually. The Company tests goodwill for impairment at the “brand” level which is one level below the operating segment level.

***Intangible Assets***

Intangible assets, which are composed primarily of trademarks, are stated at cost less accumulated amortization. For intangible assets with finite lives, amortization is computed on the straight-line method over estimated useful lives ranging from five to 20 years.

Indefinite lived intangible assets are tested for impairment at least annually, while intangible assets with finite lives are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. An impairment loss is recognized if the carrying amount of the asset exceeds its fair value.

***Deferred Financing Costs***

The Company has incurred debt issuance costs in connection with its long-term debt. These costs are capitalized as deferred financing costs and amortized using the straight-line method, which approximates the effective interest method, over the term of the related debt.

### ***Revenue Recognition***

Revenues are recognized in accordance with Securities and Exchange Commission (“SEC”) Staff Accounting Bulletin 104, “Revenue Recognition,” when the following criteria are met: (1) persuasive evidence of an arrangement exists; (2) the product has been shipped and the customer takes ownership and assumes risk of loss; (3) the selling price is fixed or determinable; and (4) collection of the resulting receivable is reasonably assured. The Company has determined that the transfer of risk of loss occurs when product is received by the customer and, accordingly, recognizes revenue at that time. Provision is made for estimated discounts related to customer payment terms and estimated product returns at the time of sale based on the Company’s historical experience.

As is customary in the consumer products industry, the Company participates in the promotional programs of its customers to enhance the sale of its products. The cost of these promotional programs varies based on the actual number of units sold during a finite period of time. The Company estimates the cost of such promotional programs at their inception based on historical experience and current market conditions and reduces sales by such estimates. These promotional programs consist of direct to consumer incentives such as coupons and temporary price reductions, as well as incentives to the Company’s customers, such as slotting fees and cooperative advertising. Estimates of the costs of these promotional programs are based on (i) historical sales experience, (ii) the current offering, (iii) forecasted data, (iv) current market conditions, and (v) communication with customer purchasing/marketing personnel. At the completion of the promotional program, the estimated amounts are adjusted to actual results.

Due to the nature of the consumer products industry, the Company is required to estimate future product returns. Accordingly, the Company records an estimate of product returns concurrent with recording sales which is made after analyzing (i) historical return rates, (ii) current economic trends, (iii) changes in customer demand, (iv) product acceptance, (v) seasonality of the Company’s product offerings, and (vi) the impact of changes in product formulation, packaging and advertising.

### ***Costs of Sales***

Costs of sales include product costs, warehousing costs, inbound and outbound shipping costs, and handling and storage costs. Shipping, warehousing and handling costs were \$6.6 million and \$6.5 million for the three month periods ended September 30, 2007 and 2006, respectively, and \$12.2 million for each of the six month periods ended September 30, 2007 and 2006, respectively.

### ***Advertising and Promotion Costs***

Advertising and promotion costs are expensed as incurred. Slotting fees associated with products are recognized as a reduction of sales. Under slotting arrangements, the retailers allow the Company’s products to be placed on the stores’ shelves in exchange for such fees. Direct reimbursements of advertising costs are reflected as a reduction of advertising costs in the period earned.

### ***Stock-based Compensation***

During fiscal 2006, the Company adopted FASB, Statement No. 123(R), “Share-Based Payment” (“Statement No. 123(R)”) with the grants of restricted stock and options to purchase common stock to employees and directors in accordance with the provisions of the Company’s 2005 Long-Term Equity Incentive Plan (the “Plan”). Statement No. 123(R) requires the Company to measure the cost of services to be rendered based on the grant-date fair value of the equity award. Compensation expense is to be recognized over the period an employee is required to provide service in exchange for the award, generally referred to as the requisite service period, and is included as a component of general and administrative expenses. The Company recorded stock-based compensation costs of \$685,000 and \$1.1 million during the three and six month periods ended September 30, 2007, respectively. During the three and six month periods ended September 30, 2006, the Company recorded stock-based compensation costs of \$233,000 and \$224,000, respectively. During the three month period ended June 30, 2006, the Company recorded a net stock-based compensation credit of \$9,000 due to the reversal of stock-based compensation costs in the amount of \$142,000

associated with the departure of a former member of management.

***Income Taxes***

Income taxes are recorded in accordance with the provisions of FASB Statement No. 109, "Accounting for Income Taxes" ("Statement No. 109"). Pursuant to Statement No. 109, deferred tax assets and liabilities are

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determined based on the differences between the financial reporting and tax bases of assets and liabilities using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. A valuation allowance is established when necessary to reduce deferred tax assets to the amounts expected to be realized.

In June 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes--an interpretation of FASB Statement 109" ("FIN 48"), which clarifies the accounting for uncertainty in income taxes recognized in a company's financial statements in accordance with Statement No. 109. FIN 48 prescribes a recognition threshold and measurement attributes for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. As a result, the Company has applied a more-likely-than-not recognition threshold for all tax uncertainties. FIN 48 allows the recognition of only those tax benefits that have a greater than 50% likelihood of being sustained upon examination by the various taxing authorities. The adoption of FIN 48, effective April 1, 2007, did not result in a cumulative effect adjustment to the opening balance of retained earnings or adjustment to any of the components of assets, liabilities or equity in the consolidated balance sheet.

The Company is subject to federal and state taxation in the US, as well as in various foreign jurisdictions. The Company remains subject to examination by tax authorities for years after 2003.

The Company classifies penalties and interest related to unrecognized tax benefits as income tax expense in the Statement of Operations.

#### ***Derivative Instruments***

FASB Statement No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("Statement No. 133"), requires companies to recognize derivative instruments as either assets or liabilities in the balance sheet at fair value. The accounting for changes in the fair value of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship and further, on the type of hedging relationship. For those derivative instruments that are designated and qualify as hedging instruments, a company must designate the hedging instrument, based upon the exposure being hedged, as a fair value hedge, a cash flow hedge or a hedge of a net investment in a foreign operation.

The Company has designated its derivative financial instruments as cash flow hedges because they hedge exposure to variability in expected future cash flows that are attributable to interest rate risk. For these hedges, the effective portion of the gain or loss on the derivative instrument is reported as a component of other comprehensive income (loss) and reclassified into earnings in the same line item associated with the forecasted transaction in the same period or periods during which the hedged transaction affects earnings. Any ineffective portion of the gain or loss on the derivative instruments is recorded in results of operations immediately.

#### ***Earnings Per Share***

Basic earnings per share is calculated based on income available to common stockholders and the weighted-average number of shares outstanding during the reporting period. Diluted earnings per share is calculated based on income available to common stockholders and the weighted-average number of common and potential common shares outstanding during the reporting period. Potential common shares, composed of the incremental common shares issuable upon the exercise of stock options, stock appreciation rights and unvested restricted shares, are included in the earnings per share calculation to the extent that they are dilutive.

#### ***Fair Value of Financial Instruments***

The carrying value of cash, accounts receivable and accounts payable at both September 30, 2007 and March 31, 2007 approximates fair value due to the short-term nature of these instruments. The carrying value of long-term debt at both September 30, 2007 and March 31, 2007 approximates fair value based on interest rates for instruments with similar terms and maturities.

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



In February 2007, the FASB issued SFAS No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities - Including an amendment of FASB Statement No. 115” (“Statement No. 159”). Statement No. 159 permits companies to choose to measure certain financial instruments and certain other items at fair value.

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Unrealized gains and losses on items for which the fair value option has been elected will be recognized in earnings at each subsequent reporting date. Statement No. 159 is effective for the Company's interim financial statements issued after April 1, 2008. The Company is evaluating the impact that the adoption of Statement No. 159 will have on its consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("Statement No. 157") to address inconsistencies in the definition and determination of fair value pursuant to GAAP. Statement No. 157 provides a single definition of fair value, establishes a framework for measuring fair value in GAAP and expands disclosures about fair value measurements in an effort to increase comparability related to the recognition of market-based assets and liabilities and their impact on earnings. Statement No. 157 is effective for the Company's interim financial statements issued after April 1, 2008. The Company is evaluating the impact that the adoption of Statement No. 157 will have on its consolidated financial statements.

Management has reviewed and continues to monitor the actions of the various financial and regulatory reporting agencies and is currently not aware of any other pronouncement that could have a material impact on the Company's consolidated financial position, results of operations or cash flows.

## 2. Accounts Receivable

Accounts receivable consist of the following (in thousands):

|   | <b>September<br/>30,<br/>2007</b> | <b>March 31,<br/>2007</b> |
|---|-----------------------------------|---------------------------|
| Accounts receivable   | \$ 48,679                         | \$ 35,274                 |
| Other receivables   | 1,286                             | 1,681                     |
|   | <b>49,965</b>                     | <b>36,955</b>             |
| Less allowances for discounts, returns and uncollectible accounts | (3,453)                           | (1,788)                   |
|   | <b>\$ 46,512</b>                  | <b>\$ 35,167</b>          |

## 3. Inventories

Inventories consist of the following (in thousands):

|                             | <b>September<br/>30,<br/>2007</b> | <b>March 31,<br/>2007</b> |
|-----------------------------|-----------------------------------|---------------------------|
| Packaging and raw materials | \$ 2,281                          | \$ 2,842                  |
| Finished goods              | 25,502                            | 27,331                    |
|                             | <b>\$ 27,783</b>                  | <b>\$ 30,173</b>          |

Inventories are shown net of allowances for obsolete and slow moving inventory of \$1.3 million and \$1.8 million at September 30, 2007 and March 31, 2007, respectively.

#### 4. Property and Equipment

Property and equipment consist of the following (in thousands):

|                          | September 30,<br>2007 | March 31,<br>2007 |
|--------------------------|-----------------------|-------------------|
| Machinery                | \$ 1,397              | \$ 1,480          |
| Computer equipment       | 477                   | 566               |
| Furniture and fixtures   | 205                   | 247               |
| Leasehold improvements   | 319                   | 372               |
|                          | 2,398                 | 2,665             |
| Accumulated depreciation | (1,007)               | (1,216)           |
|                          | \$ 1,391              | \$ 1,449          |

#### 5. Goodwill

A reconciliation of the activity affecting goodwill by operating segment is as follows (in thousands):

|  | Over-the-Counter<br>Healthcare | Household<br>Cleaning | Personal<br>Care | Consolidated |
|--|--------------------------------|-----------------------|------------------|--------------|
| Balance – March 31, 2007               | \$ 235,647                     | \$ 72,549             | \$ 2,751         | \$ 310,947   |
| Acquisition purchase price adjustments | (2,032)                        | --                    | --               | (2,032)      |
| Balance – September 30, 2007           | \$ 233,615                     | \$ 72,549             | \$ 2,751         | \$ 308,915   |

#### 6. Intangible Assets

A reconciliation of the activity affecting intangible assets is as follows (in thousands):

|                                 | Indefinite<br>Lived<br>Trademarks | Finite<br>Lived<br>Trademarks | Non<br>Compete<br>Agreement | Totals     |
|---------------------------------|-----------------------------------|-------------------------------|-----------------------------|------------|
| <b>Carrying Amounts</b>         |                                   |                               |                             |            |
| Balance – March 31, 2007        | \$ 544,963                        | \$ 139,470                    | \$ 196                      | \$ 684,629 |
| Additions                       | --                                | --                            | --                          | --         |
| Balance – September 30, 2007    | \$ 544,963                        | \$ 139,470                    | \$ 196                      | \$ 684,629 |
| <b>Accumulated Amortization</b> |                                   |                               |                             |            |
| Balance – March 31, 2007        | \$ --                             | \$ 27,375                     | \$ 97                       | \$ 27,472  |
| Additions                       | --                                | 5,232                         | 22                          | 5,254      |

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|                              |    |    |    |        |    |     |    |        |
|------------------------------|----|----|----|--------|----|-----|----|--------|
| Balance – September 30, 2007 | \$ | -- | \$ | 32,607 | \$ | 119 | \$ | 32,726 |
|------------------------------|----|----|----|--------|----|-----|----|--------|

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At September 30, 2007, intangible assets are expected to be amortized over a period of five to 30 years as follows (in thousands):

| <b>Year Ending September 30</b> |            |
|---------------------------------|------------|
| 2008                            | \$ 10,507  |
| 2009                            | 9,799      |
| 2010                            | 9,071      |
| 2011                            | 9,071      |
| 2012                            | 9,071      |
| Thereafter                      | 59,421     |
|                                 | \$ 106,940 |

**7. Other Accrued Liabilities**

Other accrued liabilities consist of the following (in thousands):

|                         | <b>September</b> |                  |
|-------------------------|------------------|------------------|
|                         | <b>30,</b>       | <b>March 31,</b> |
|                         | <b>2007</b>      | <b>2007</b>      |
| Accrued marketing costs | \$ 7,820         | \$ 5,687         |
| Accrued payroll         | 3,100            | 3,721            |
| Accrued commissions     | 357              | 335              |
| Other                   | 1,494            | 762              |
|                         | \$ 12,771        | \$ 10,505        |

## 8. Long-Term Debt

Long-term debt consists of the following (in thousands):

|  | September<br>30,<br>2007 | March 31,<br>2007 |
|--|--------------------------|-------------------|
| Senior revolving credit facility (“Revolving Credit Facility”), which expires on April 6, 2009 and is available for maximum borrowings of up to \$60.0 million. The Revolving Credit Facility bears interest at the Company’s option at either the prime rate plus a variable margin or LIBOR plus a variable margin. The variable margins range from 0.75% to 2.50% and at September 30, 2007, the interest rate on the Revolving Credit Facility was 8.75% per annum. The Company is also required to pay a variable commitment fee on the unused portion of the Revolving Credit Facility. At September 30, 2007, the commitment fee was 0.50% of the unused line. The Revolving Credit Facility is collateralized by substantially all of the Company’s assets.  | \$ --                    | \$ --             |
| Senior secured term loan facility (“Tranche B Term Loan Facility” and together with the Revolving Credit Facility, the “Senior Credit Facility”) that bears interest at the Company’s option at either the prime rate plus a margin of 1.25% or LIBOR plus a margin of 2.25%. At September 30, 2007, the average interest rate on the Tranche B Term Loan Facility was 7.74%. Principal payments of \$887,500 plus accrued interest are payable quarterly. At September 30, 2007, the Company may borrow up to a maximum amount of \$200.0 million under the Tranche B Term Loan Facility. Current amounts outstanding under the Tranche B Term Loan Facility mature on April 6, 2011, while any additional amounts borrowed will mature on October 6, 2011. The Tranche B Term Loan Facility is collateralized by substantially all of the Company’s assets.  | 311,113                  | 337,350           |
| Senior Subordinated Notes that bear interest at 9.25% which is payable on April 15 <sup>th</sup> and October 15 <sup>th</sup> of each year. The Senior Subordinated Notes mature on April 15, 2012; however, the Company may redeem some or all of the Senior Subordinated Notes on or prior to April 15, 2008 at a redemption price equal to 100% plus a make-whole premium, and after April 15, 2008, at redemption prices set forth in the Indenture governing the Senior Subordinated Notes. The Senior Subordinated Notes are unconditionally guaranteed by Prestige Brands Holdings, Inc. and its domestic wholly-owned subsidiaries other than Prestige Brands, Inc., the issuer. Each of these guarantees is joint and several. There are no significant restrictions on the ability of any of the guarantors to obtain funds from their subsidiaries. | 126,000                  | 126,000           |
|  | 437,113                  | 463,350           |
| Current portion of long-term debt  | (3,550)                  | (3,550)           |
|  | \$ 433,563               | \$ 459,800        |

Effective as of December 19, 2006: (i) a Second Supplemental Indenture (“Second Supplemental Indenture”), and (ii) a Guaranty Supplement (“Indenture Guaranty Supplement”) were entered into with the trustee for the holders

of the Senior Subordinated Notes. The Second Supplemental Indenture supplements and amends the Indenture, dated as of April 6, 2004, as supplemented on October 6, 2004 (“Indenture”). Pursuant to the terms of the Second Supplemental Indenture and the Indenture Guaranty Supplement, the Company agreed to guaranty all of the obligations of Prestige Brands, Inc., an indirect wholly-owned subsidiary of the Company (“PBI”), set forth in the Indenture governing PBI’s Senior Subordinated Notes. The Second Supplemental Indenture also amended the covenant requiring Prestige Brands International, LLC (“Prestige Brands International”), an indirect wholly-owned subsidiary of the Company, to file periodic reports with the SEC pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended (“Exchange Act”). So long as the Company or any other guarantor is required to file periodic reports under Section 13 or 15(d) of the Exchange Act that are substantially the same as the periodic reports that Prestige Brands International would otherwise be required to file with the SEC pursuant to the Indenture, Prestige Brands International is not required to file such reports.

Also effective as of December 19, 2006, a Joinder Agreement (“Joinder Agreement”) and a Guaranty Supplement (“Credit Agreement Guaranty Supplement”) were entered into with the administrative agent for the lenders under the Senior Credit Facility. Pursuant to the terms of the Joinder Agreement and the Credit Agreement Guaranty Supplement, the Company agreed to become a party to the Pledge and Security Agreement (“Security Agreement”) and the Guaranty (“Credit Agreement Guaranty”), each dated as of April 6, 2004, by PBI and certain of its affiliates in favor of the lenders. The Security Agreement and the Credit Agreement Guaranty secure the performance by PBI of its obligations under the Credit Agreement, dated as of April 6, 2004, as amended (“Credit Agreement”), by granting security interests to PBI’s lenders in collateral owned by the Company and certain of its subsidiaries and providing guaranties of such obligations by certain of PBI’s affiliates.

The Senior Credit Facility contains various financial covenants, including provisions that require the Company to maintain certain leverage ratios, interest coverage ratios and fixed charge coverage ratios. The Senior Credit Facility and the Senior Subordinated Notes also contain provisions that restrict the Company from undertaking specified corporate actions, such as asset dispositions, acquisitions, dividend payments, repurchase of common shares outstanding, changes of control, incurrence of indebtedness, creation of liens, making of loans and transactions with affiliates. Additionally, the Senior Credit Facility and the Senior Subordinated Notes contain cross-default provisions whereby a default pursuant to the terms and conditions of either indebtedness will cause a default on the remaining indebtedness. At September 30, 2007, the Company was in compliance with its applicable financial and other covenants under the Senior Credit Facility and the Indenture.

Future principal payments required in accordance with the terms of the Senior Credit Facility and the Senior Subordinated Notes are as follows (in thousands):

| <b><u>Year Ending September 30</u></b> |            |
|--|------------|
| 2008                                   | \$ 3,550   |
| 2009                                   | 3,550      |
| 2010                                   | 3,550      |
| 2011                                   | 300,463    |
| 2012                                   | 126,000    |
|  | \$ 437,113 |

In an effort to mitigate the impact of changing interest rates, the Company entered into interest rate cap agreements with various financial institutions. In June 2004, the Company purchased a 5% interest rate cap with a notional amount of \$20.0 million which expired in June 2006. In March 2005, the Company purchased interest rate cap agreements with a total notional amount of \$180.0 million and cap rates ranging from 3.25% to 3.75%. On May 31, 2006, an interest rate cap agreement with a notional amount of \$50.0 million and a 3.25% cap rate expired. Additionally, an interest rate cap agreement with a notional amount of \$80.0 million and a 3.50% cap rate expired on May 30, 2007. The remaining agreement, with a notional amount of \$50.0 million and a cap rate of 3.75%,

terminates on May 30, 2008. The Company is accounting for the interest rate cap agreements as cash flow hedges. The fair values of the interest rate cap agreements, which are included in other long-term assets, were \$486,000 and \$1.2 million at September 30, 2007 and March 31, 2007, respectively.

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## 9. Stockholders' Equity

The Company is authorized to issue 250.0 million shares of common stock, \$0.01 par value per share, and 5.0 million shares of preferred stock, \$0.01 par value per share. The Board of Directors may direct the issuance of the undesignated preferred stock in one or more series and determine preferences, privileges and restrictions thereof.

Each share of common stock has the right to one vote on all matters submitted to a vote of stockholders. The holders of common stock are also entitled to receive dividends whenever funds are legally available and when declared by the Board of Directors, subject to prior rights of holders of all classes of stock outstanding having priority rights as to dividends. No dividends have been declared or paid on the Company's common stock through September 30, 2007.

## 10. Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share (in thousands):

|  | Three Months Ended<br>September 30 |          | Six Months Ended<br>September 30 |           |
|--|------------------------------------|----------|----------------------------------|-----------|
|  | 2007                               | 2006     | 2007                             | 2006      |
| <b>Numerator</b>   |                                    |          |                                  |           |
| Net income   | \$ 6,829                           | \$ 8,784 | \$ 15,149                        | \$ 17,040 |
| <b>Denominator</b>   |                                    |          |                                  |           |
| Denominator for basic earnings per share – weighted average shares | 49,710                             | 49,451   | 49,686                           | 49,389    |
| Dilutive effect of unvested restricted common stock                | 336                                | 543      | 356                              | 602       |
| Denominator for diluted earnings per share                         | 50,046                             | 49,994   | 50,042                           | 49,991    |
| <b>Earnings per Common Share:</b>                                  |                                    |          |                                  |           |
| Basic  | \$ 0.14                            | \$ 0.18  | \$ 0.30                          | \$ 0.35   |
| Diluted  | \$ 0.14                            | \$ 0.18  | \$ 0.30                          | \$ 0.34   |

At September 30, 2007, 243,000 shares of restricted stock issued to management and employees prior to the Company's initial public offering are unvested and excluded from the calculation of basic earnings per share; however, such shares are included in the calculation of diluted earnings per share. At September 30, 2007, 160,000 shares of restricted stock granted to management, directors and employees, subject only to time vesting requirements, have been excluded from basic earnings per share; however, such shares are included in the calculation of diluted earnings per share. Additionally, 378,000 shares of restricted stock granted to management and employees, as well as 16,000 stock appreciation rights have been excluded from the calculation of both basic and diluted earnings per share since vesting of such shares is subject to contingencies, while options to purchase 255,000 shares of common stock have been excluded from diluted earnings per shares because their inclusion would be anti-dilutive.

At September 30, 2006, 522,000 shares of restricted stock issued to management and employees prior to the Company's initial public offering were unvested and excluded from the calculation of basic earnings per share; however, such shares are included in the calculation of diluted earnings per share. Additionally, at September 30, 2006, 278,000 shares of restricted stock granted to management and employees have been excluded from the calculation of both basic and diluted earnings per share since vesting of such shares is subject to contingencies.



## 11. Share-Based Compensation

In connection with the Company's initial public offering, the Board of Directors adopted the Plan which provides for the grant, to a maximum of 5.0 million shares, of stock options, restricted stock units, deferred stock units and other equity-based awards. Directors, officers and other employees of the Company and its subsidiaries, as well as others performing services for the Company, are eligible for grants under the Plan. The Company believes that such awards better align the interests of its employees with those of its stockholders.

During 2006, the Company adopted Statement No. 123(R) with the initial grants of restricted stock and options to purchase common stock to employees and directors in accordance with the provisions of the Plan. During the six month period ended September 30, 2007, the Company recorded compensation costs and related tax benefits of \$1.1 million and \$418,000, respectively, while during the six month period ended September 30, 2006, the Company recorded compensation costs and related tax benefits of \$225,000 and \$88,000, respectively.

### Restricted Shares

Restricted shares granted under the Plan generally vest in 3 years, contingent on attainment of Company performance goals, including both revenue and earnings per share growth targets, or time vesting, as determined by the Compensation Committee of the Board of Directors. Certain restricted share awards provide for accelerated vesting if there is a change of control. The fair value of nonvested restricted shares is determined as the closing price of the Company's common stock on the day preceding the grant date. The weighted-average grant-date fair value of restricted shares granted during 2007 was \$12.52.

A summary of the Company's restricted shares granted under the Plan is presented below:

| <b>Restricted Shares</b>           | <b>Shares<br/>(000)</b> | <b>Weighted-Average<br/>Grant-Date<br/>Fair Value</b> |
|------------------------------------|-------------------------|---|
| Nonvested at March 31, 2006        | 198.0                   | \$ 12.32  |
| Granted                            | 156.5                   | 9.83  |
| Vested                             | (13.1)                  | 10.67   |
| Forfeited                          | (39.0)                  | 12.82   |
| Nonvested at September 30,<br>2006 | 302.4                   | \$ 11.04  |
| Nonvested at March 31, 2007        | 294.4                   | \$ 11.05  |
| Granted                            | 292.0                   | 12.52   |
| Vested                             | (24.8)                  | 10.09   |
| Forfeited                          | (23.2)                  | 11.39   |
| Nonvested at September 30,<br>2007 | 538.4                   | \$ 11.88  |

## Options

The Plan provides that the exercise price of the option granted shall be no less than the fair market value of the Company's common stock on the date the option is granted. Options granted have a term of no greater than 10 years from the date of grant and vest in accordance with a schedule determined at the time the option is granted, generally 3 years.

The fair value of each option award is estimated on the date of grant using the Black-Scholes Option Pricing Model ("Black-Scholes Model") that uses the assumptions noted in the following table. Expected volatilities are based on the historical volatility of the Company's common stock and other factors, including the historical volatilities of comparable companies. The Company uses appropriate historical data, as well as current data, to estimate option exercise and employee termination behaviors. Employees that are expected to exhibit similar exercise or termination behaviors are grouped together for the purposes of valuation. The expected terms of the options granted are derived from management's estimates and information derived from the public filings of companies similar to the Company and represent the period of time that options granted are expected to be outstanding. The risk-free rate represents the yield on U.S. Treasury bonds with a maturity equal to the expected term of the granted option. The weighted-average grant-date fair value of the options granted during the six month period ended September 30, 2007 was \$5.30. There were no options granted during 2006.

|                        | 2007  | 2006 |
|------------------------|-------|------|
| Expected volatility    | 33.2% | --   |
| Expected dividends     | --    | --   |
| Expected term in years | 6.0   | --   |
| Risk-free rate         | 4.5%  | --   |

A summary of option activity under the Plan is as follows:

| Options                           | Shares<br>(000) | Weighted-Average<br>Exercise<br>Price | Weighted-<br>Average<br>Remaining<br>Contractual<br>Term |
|-----------------------------------|-----------------|---------------------------------------|--|
| Outstanding at March 31, 2006     | 61.8            | \$ 12.95                              | 4.3  |
| Granted                           | --              | --                                    | --   |
| Exercised                         | --              | --                                    | --   |
| Forfeited or expired              | (61.8)          | 12.95                                 | --   |
| Outstanding at September 30, 2006 | --              | \$ --                                 | --   |
| Outstanding at March 31, 2007     | --              | \$ --                                 | --   |
| Granted                           | 255.1           | 12.86                                 | 10.0   |
| Exercised                         | --              | --                                    | --   |
| Forfeited or expired              | --              | --                                    | --   |
| Outstanding at September 30, 2007 | 255.1           | \$ 12.86                              | 10.0   |
| Exercisable at September 30, 2007 | --              | \$ --                                 | --   |

## Stock Appreciation Rights ("SARS")

The Plan provides that the issuance price of a SAR shall be no less than the market price of the Company's common stock on the date the SAR is granted. SARS may be granted with a term of no greater than 10 years from the date of grant and will vest in accordance with a schedule determined at the time the SAR is granted, generally 3 years. The

Board of Directors, in its sole discretion, may settle the Company's obligation to the executive in shares of the Company's common stock, cash, other securities of the Company or any combination thereof. The weighted-average grant date fair value of the SARS granted during the six month period ended September 30, 2006 was \$3.68. There were no SARS granted during the six month period ended September 30,

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2007. The fair value of each SAR award was estimated on the date of grant using the Black-Scholes Model using the assumptions noted in the following table.

|                        | 2007 | 2006  |
|------------------------|------|-------|
| Expected volatility    | --   | 50.0% |
| Expected dividends     | --   | --    |
| Expected term in years | --   | 2.8   |
| Risk-free rate         | --   | 5.0%  |

A summary of SARS activity under the Plan is as follows:

| SARS                              | Shares<br>(000) | Grant<br>Date<br>Stock<br>Price | Weighted-<br>Average<br>Remaining<br>Contractual<br>Term |
|-----------------------------------|-----------------|---------------------------------|--|
| Outstanding at March 31, 2006     | --              | \$ --                           | --   |
| Granted                           | 16.1            | 9.97                            | 2.75   |
| Forfeited or expired              | --              | --                              | --   |
| Outstanding at September 30, 2006 | 16.1            | \$ 9.97                         | 2.5  |
| Exercisable at September 30, 2006 | --              | \$ --                           | --   |
| Outstanding at March 31, 2007     | 16.1            | \$ 9.97                         | 2.00   |
| Granted                           | --              | --                              | --   |
| Forfeited or expired              | --              | --                              | --   |
| Outstanding at September 30, 2007 | 16.1            | \$ 9.97                         | 1.50   |
| Exercisable at September 30, 2007 | --              | \$ --                           | --   |

At September 30, 2007 and March 31, 2007, there were \$4.9 million and \$1.4 million, respectively, of unrecognized compensation costs related to nonvested share-based compensation arrangements under the Plan based on management's estimate of the shares that will ultimately vest. The Company expects to recognize such costs over the next 3.0 years. However, certain of the restricted shares vest upon the attainment of Company performance goals and if such goals are not met, no compensation costs would ultimately be recognized and any previously recognized compensation cost would be reversed. At September 30, 2007, there were 4.1 million shares available for issuance under the Plan.

## 12. Income Taxes

Income taxes are recorded in the Company's quarterly financial statements based on the Company's estimated annual effective income tax rate. The effective tax rates used in the calculation of income taxes were 38.0% and 39.1% for the periods ended September 30, 2007 and 2006, respectively. The reduction in the income tax rates results from the implementation of initiatives to obtain operational, as well as tax, efficiencies during the fiscal year ended March 31, 2007.

At September 30, 2007, Medtech Products Inc., a wholly-owned subsidiary of the Company, had a net operating loss carryforward of approximately \$2.6 million which may be used to offset future taxable income of the consolidated group and which begins to expire in 2020. The net operating loss carryforward is subject to an annual limitation as to usage under Internal Revenue Code Section 382 of approximately \$240,000.



### 13. Commitments and Contingencies

The legal proceedings in which we are involved have been disclosed previously in our Annual Report on Form 10-K for the fiscal year ended March 31, 2007, our Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2007 and our Current Report on Form 8-K filed with the SEC on October 24, 2007. The following disclosure contains recent developments in our pending legal proceedings and should be read in conjunction with the legal proceedings disclosure contained in Part I, Item 3 of our Annual Report on Form 10-K for the fiscal year ended March 31, 2007, Part II, Item 1 of our Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2007 and our Current Report on Form 8-K filed with the SEC on October 24, 2007.

#### Securities Class Action Litigation

On September 4, 2007, the United States District Court for the Southern District of New York issued an Order certifying a class consisting of all persons who purchased the common stock of the Company pursuant to, or traceable to, the Company's initial public offering on or about February 9, 2005 through November 15, 2005 and were damaged thereby. The Company's management continues to believe that the remaining claims in the case are legally deficient and that it has meritorious defenses to the claims that remain. The Company intends to vigorously defend against the claims remaining in the case; however, the Company cannot reasonably estimate the potential range of loss, if any.

#### OraSure Technologies Arbitration

At the end of August 2007, the Company and OraSure Technologies, Inc. ("OraSure") participated in an arbitration hearing at which each party presented its case to the arbitration panel. On October 22, 2007, the Company received notification from the arbitrators that they had issued a Partial Final Award (the "Award") in the pending arbitration with OraSure. The arbitrators acknowledged that there was a technical breach of the non-compete clause in the Distribution Agreement between the parties but OraSure's proof of damages was speculative and not supported by credible evidence. Therefore, the arbitrators awarded nominal damages to OraSure in the amount of One Dollar (\$1.00). In addition, the arbitrators awarded to OraSure counsel fees and arbitrator compensation in an amount to be determined pursuant to further proceedings. The Company will vigorously contest the award of fees to OraSure as the Company believes that OraSure should only be entitled to a modest award in light of the arbitrators' rejection of OraSure's asserted damages and claims beyond the One Dollar (\$1.00) nominal award.

The arbitration panel also dismissed with prejudice OraSure's remaining claims for breach of the Distribution Agreement, OraSure's request for injunctive relief and the Company's counterclaims, respectively. Furthermore, the arbitrators confirmed the Company's position that the Distribution Agreement will terminate on December 31, 2007. The Company does not expect any interruptions in supply of its Compound W Freeze Off® branded cryosurgical wart remover as it transitions to a new supplier after December 31, 2007.

#### DenTek Oral Care, Inc. Litigation

In April 2007, the Company filed a lawsuit in the U.S. District Court in the Southern District of New York against DenTek Oral Care, Inc. ("DenTek") alleging (i) infringement of intellectual property associated with The Doctor's® NightGuard™ dental protector which is used for the protection of teeth from nighttime teeth grinding; and (ii) the violation of unfair competition and consumer protection laws. On October 4, 2007, the Company filed a Second Amended Complaint in which it named Kelly M. Kaplan, Raymond Duane and C.D.S. Associates, Inc. as additional defendants in the action against DenTek and added other claims to the previously filed complaint. Ms. Kaplan and Mr. Duane were formerly employed by the Company and C.D.S. Associates, Inc. is a corporation controlled by Mr. Duane. In the Second Amended Complaint, the Company has alleged patent, trademark and copyright infringement, unfair competition, unjust enrichment, violation of New York's Consumer Protection Act, breach of contract, tortious interference with contractual and business relations, civil conspiracy and trade secret misappropriation. On October 19, 2007, the Company filed a motion for preliminary injunction with the Court in which the Company has asked the Court to enjoin the defendants from (i) continuing to improperly use the Company's trade secrets; (ii) continuing to breach any contractual agreements with the Company; and (iii) marketing and selling any dental protector products or other products in which Ray Duane or Kelly Kaplan has had any involvement or provided any assistance to



DenTek. A hearing date for the motion for preliminary injunction has not yet been set by the Court. Discovery requests have been served by the parties and discovery is ongoing.

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In addition to the matters described above, the Company is involved from time to time in other routine legal matters and other claims incidental to its business. The Company reviews outstanding claims and proceedings internally and with external counsel as necessary to assess probability and amount of potential loss. These assessments are re-evaluated at each reporting period and as new information becomes available to determine whether a reserve should be established or if any existing reserve should be adjusted. The actual cost of resolving a claim or proceeding ultimately may be substantially different than the amount of the recorded reserve. In addition, because it is not permissible under GAAP to establish a litigation reserve until the loss is both probable and estimable, in some cases there may be insufficient time to establish a reserve prior to the actual incurrence of the loss (upon verdict and judgment at trial, for example, or in the case of a quickly negotiated settlement). The Company believes the resolution of routine matters and other incidental claims, taking into account reserves and insurance, will not have a material adverse effect on its business, financial condition or results from operations.

#### *Lease Commitments*

The Company has operating leases for office facilities and equipment in New York, New Jersey and Wyoming, which expire at various dates through 2011.

The following summarizes future minimum lease payments for the Company's operating leases (in thousands):

|                                  | Facilities | Equipment | Total    |
|----------------------------------|------------|-----------|----------|
| <b>Year Ending September 30,</b> |            |           |          |
| 2008                             | \$ 650     | \$ 122    | \$ 772   |
| 2009                             | 362        | 98        | 460      |
| 2010                             | --         | 67        | 67       |
| 2011                             | --         | 4         | 4        |
|                                  | \$ 1,012   | \$ 291    | \$ 1,303 |

Rent expense for the three month periods ended September 30, 2007 and 2006 was \$145,000 and \$136,000, respectively; while during the six month periods ended September 30, 2007 and 2006, rent expense was \$298,000 and \$275,000, respectively.

#### **14. Concentrations of Risk**

The Company's sales are concentrated in the areas of over-the-counter healthcare, household cleaning and personal care products. The Company sells its products to mass merchandisers, food and drug accounts, and dollar and club stores. During the three and six month periods ended September 30, 2007 approximately 56.4% and 56.5%, respectively, of the Company's total sales were derived from its four major brands, while during the three and six month periods ended September 30, 2006, approximately 61.1% and 60.2%, respectively, of the Company's total sales were derived from these four major brands. During the three and six month periods ended September 30, 2007, approximately 22.8% and 23.8%, respectively, of the Company's sales were made to one customer, while during the three and six month periods ended September 30, 2006, 24.1% and 24.6% of sales were to this customer. At September 30, 2007, approximately 19.5% of accounts receivable were owed by the same customer.

The Company manages product distribution in the continental United States through a main distribution center in St. Louis, Missouri. A serious disruption, such as a flood or fire, to the main distribution center could damage the Company's inventories and could materially impair the Company's ability to distribute its products to customers in a timely manner or at a reasonable cost. The Company could incur significantly higher costs and experience longer lead times associated with the distribution of its products to its customers during the time that it takes the Company to reopen or replace its distribution center. As a result, any such disruption could have a material adverse affect on the Company's sales and profitability.



The Company has relationships with over 40 third-party manufacturers. Of those, the top 10 manufacturers produced items that accounted for approximately 79% of the Company's gross sales during the six months ended September 30, 2007. The Company does not have long-term contracts with 4 of these manufacturers and certain manufacturers of various smaller brands, which collectively, represented approximately 35% of the Company's gross sales for 2007. The lack of manufacturing agreements for these products exposes the Company to the risk that a manufacturer could stop producing the Company's products at any time, for any reason or fail to provide the Company with the level of products the Company needs to meet its customers' demands. Without adequate supplies of merchandise to sell to the Company's customers, sales would decrease materially and the Company's business would suffer.

## 15. Business Segments

Segment information has been prepared in accordance with FASB Statement No. 131, "Disclosures about Segments of an Enterprise and Related Information." The Company's operating and reportable segments consist of (i) Over-the-Counter Healthcare, (ii) Household Cleaning and (iii) Personal Care.

There were no inter-segment sales or transfers during any of the periods presented. The Company evaluates the performance of its operating segments and allocates resources to them based primarily on contribution margin.

The table below summarizes information about the Company's operating and reportable segments (in thousands).

|                            | Three Months Ended September 30, 2007 |                       |                  |              |
|----------------------------|---------------------------------------|-----------------------|------------------|--------------|
|                            | Over-the-Counter<br>Healthcare        | Household<br>Cleaning | Personal<br>Care | Consolidated |
| Net sales                  | \$ 50,003                             | 30,925                | \$ 5,912         | \$ 86,840    |
| Other revenues             | --                                    | 497                   | --               | 497          |
| Total revenues             | 50,003                                | 31,422                | 5,912            | 87,337       |
| Cost of sales              | 19,688                                | 19,587                | 3,495            | 42,770       |
| Gross profit               | 30,315                                | 11,835                | 2,417            | 44,567       |
| Advertising and promotion  | 8,154                                 | 2,575                 | 288              | 11,017       |
| Contribution margin        | \$ 22,161                             | \$ 9,260              | \$ 2,129         | 33,550       |
| Other operating expenses   |                                       |                       |                  | 12,940       |
| Operating income           |                                       |                       |                  | 20,610       |
| Other (income) expense     |                                       |                       |                  | 9,595        |
| Provision for income taxes |                                       |                       |                  | 4,186        |
| Net income                 |                                       |                       |                  | \$ 6,829     |

|                            | <b>Six Months Ended September 30, 2007</b> |                  |                 |                     |
|----------------------------|--|------------------|-----------------|---------------------|
|                            | <b>Over-the-Counter</b>                    | <b>Household</b> | <b>Personal</b> | <b>Consolidated</b> |
|                            | <b>Healthcare</b>                          | <b>Cleaning</b>  | <b>Care</b>     |                     |
| Net sales                  | \$ 92,429                                  | \$ 60,270        | \$ 12,182       | \$ 164,881          |
| Other revenues             | --   | 1,039            | 28              | 1,067               |
| Total revenues             | 92,429                                     | 61,309           | 12,210          | 165,948             |
| Cost of sales              | 35,074                                     | 37,980           | 7,038           | 80,092              |
| Gross profit               | 57,355                                     | 23,329           | 5,172           | 85,856              |
| Advertising and promotion  | 14,035                                     | 4,203            | 565             | 18,803              |
| Contribution margin        | \$ 43,320                                  | \$ 19,126        | \$ 4,607        | 67,053              |
| Other operating expenses   |  |                  |                 | 23,337              |
| Operating income           |  |                  |                 | 43,716              |
| Other (income) expense     |  |                  |                 | 19,282              |
| Provision for income taxes |  |                  |                 | 9,285               |
| Net income                 |  |                  |                 | \$ 15,149           |

|                            | <b>Three Months Ended September 30, 2006</b> |                  |                 |                     |
|----------------------------|--|------------------|-----------------|---------------------|
|                            | <b>Over-the-Counter</b>                      | <b>Household</b> | <b>Personal</b> | <b>Consolidated</b> |
|                            | <b>Healthcare</b>                            | <b>Cleaning</b>  | <b>Care</b>     |                     |
| Net sales                  | \$ 46,255                                    | \$ 30,732        | \$ 7,046        | \$ 84,033           |
| Other revenues             | --   | 518              | --              | 518                 |
| Total revenues             | 46,255                                       | 31,250           | 7,046           | 84,551              |
| Cost of sales              | 18,001                                       | 18,941           | 4,317           | 41,259              |
| Gross profit               | 28,254                                       | 12,309           | 2,729           | 43,292              |
| Advertising and promotion  | 7,058  | 2,020            | 377             | 9,455               |
| Contribution margin        | \$ 21,196                                    | \$ 10,289        | \$ 2,352        | 33,837              |
| Other operating expenses   |  |                  |                 | 9,671               |
| Operating income           |  |                  |                 | 24,166              |
| Other (income) expense     |  |                  |                 | 9,743               |
| Provision for income taxes |  |                  |                 | 5,639               |
| Net income                 |  |                  |                 | \$ 8,784            |

|                            | Six Months Ended September 30, 2006 |                       |                  |              |
|----------------------------|-------------------------------------|-----------------------|------------------|--------------|
|                            | Over-the-Counter<br>Healthcare      | Household<br>Cleaning | Personal<br>Care | Consolidated |
| Net sales                  | \$ 85,853                           | \$ 60,470             | \$ 13,277        | \$ 159,600   |
| Other revenues             | --                                  | 874                   | --               | 874          |
| Total revenues             | 85,853                              | 61,344                | 13,277           | 160,474      |
| Cost of sales              | 32,398                              | 37,095                | 8,091            | 77,584       |
| Gross profit               | 53,455                              | 24,249                | 5,186            | 82,890       |
| Advertising and promotion  | 12,483                              | 3,710                 | 664              | 16,857       |
| Contribution margin        | \$ 40,972                           | \$ 20,539             | \$ 4,522         | 66,033       |
| Other operating expenses   |                                     |                       |                  | 18,518       |
| Operating income           |                                     |                       |                  | 47,515       |
| Other (income) expense     |                                     |                       |                  | 19,535       |
| Provision for income taxes |                                     |                       |                  | 10,940       |
| Net income                 |                                     |                       |                  | \$ 17,040    |

During the three month periods ended September 30, 2007 and 2006, approximately 96.6% and 96.4%, respectively, of the Company's sales were made to customers in the United States and Canada while during the six month periods ended September 30, 2007 and 2006, approximately 95.7% and 96.2%, respectively, of sales were made to customers in the US and Canada. At September 30, 2007, substantially all of the Company's long-term assets were located in the United States of America and have been allocated to the operating segments as follows:

|                   | Over-the-Counter | Household  | Personal  | Consolidated |
|-------------------|------------------|------------|-----------|--------------|
|                   | Healthcare       | Cleaning   | Care      |              |
| Goodwill          | \$ 233,615       | \$ 72,549  | \$ 2,751  | \$ 308,915   |
| Intangible assets |                  |            |           |              |
| Indefinite lived  | 374,070          | 170,893    | --        | 544,963      |
| Finite lived      | 90,986           | 15         | 15,939    | 106,940      |
|                   | 465,056          | 170,908    | 15,939    | 651,903      |
|                   | \$ 698,671       | \$ 243,457 | \$ 18,690 | \$ 960,818   |

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

The following discussion of our financial condition and results of operations should be read together with the consolidated financial statements and the related notes included in our Annual Report on Form 10-K for the fiscal year ended March 31, 2007. This discussion and analysis may contain forward-looking statements that involve certain risks, assumptions and uncertainties. Future results could differ materially from the discussion that follows for many reasons, including the factors described in Part I, Item 1A., "Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended March 31, 2007, as well as those described in future reports filed with the SEC. See also "Cautionary Statements Regarding Forward Looking Statements" on page 40 of this Quarterly Report on Form 10-Q.

***General***

We are engaged in the marketing, sales and distribution of brand name over-the-counter healthcare, household cleaning and personal care products to mass merchandisers, drug stores, supermarkets and club stores primarily in the United States and Canada. We operate in niche segments of these categories where we can use the strength of our brands, our established retail distribution network, a low-cost operating model and our experienced management team as a competitive advantage to grow our presence in these categories and, as a result, grow our sales and profits.

We have grown our brand portfolio by acquiring strong and well-recognized brands from larger consumer products and pharmaceutical companies, as well as other brands from smaller private companies. While the brands we have purchased from larger consumer products and pharmaceutical companies have long histories of support and brand development, we believe that at the time we acquired them they were considered "non-core" by their previous owners and did not benefit from the focus of senior level management or strong marketing support. We believe that the brands we have purchased from smaller private companies have been constrained by the limited resources of their prior owners. After acquiring a brand, we seek to increase its sales, market share and distribution in both existing and new channels. We pursue this growth through increased spending on advertising and promotion, new marketing strategies, improved packaging and formulations and innovative new products.

In October 2005, we completed the acquisition of the "Chore Boy®" brand of cleaning pads and sponges. The purchase price of this acquisition was \$22.6 million, including direct costs of \$400,000. We purchased the Chore Boy brand with funds generated from operations.

In November 2005, we completed the acquisition of Dental Concepts LLC, a marketer of therapeutic oral care products sold under "The Doctor's®" brand. The purchase price of the ownership interests was approximately \$30.2 million, including fees and expenses of the acquisition of \$1.3 million. We financed the acquisition price through the utilization of our Revolving Credit Facility in the amount of \$30.0 million and cash on hand.

In September 2006, we completed the acquisition of Wartner USA B.V., a privately held Netherlands limited liability company, which owned the intellectual property associated with the "Wartner®" brand of over-the-counter wart treatment products. The purchase price of this acquisition was \$31.2 million, inclusive of direct costs of the acquisition of \$216,000. We purchased the Wartner brand with funds generated from operations and the assumption of approximately \$5.0 million of contingent payments to the former owner of the Wartner brand.

**Three Month Period Ended September 30, 2007 compared to the  
Three Month Period Ended September 30, 2006**

**Revenues**

|                    | 2007      |       | 2006      |       | Increase<br>(Decrease) |        |
|--------------------|-----------|-------|-----------|-------|------------------------|--------|
|                    | Revenues  | %     | Revenues  | %     |                        | %      |
| OTC Healthcare     | \$ 50,003 | 57.2  | \$ 46,255 | 54.7  | \$ 3,748               | 8.1    |
| Household Cleaning | 31,422    | 36.0  | 31,250    | 37.0  | 172                    | 0.6    |
| Personal Care      | 5,912     | 6.8   | 7,046     | 8.3   | (1,134)                | (16.1) |
|                    | \$ 87,337 | 100.0 | \$ 84,551 | 100.0 | \$ 2,786               | 3.3    |

Revenues for the three month period ended September 30, 2007 increased \$2.8 million, or 3.3%, versus the comparable period in 2006, primarily as a result of the acquisition of the Wartner brand in September of 2006. Excluding the impact of the Wartner acquisition, revenues increased 0.6% versus the comparable period in 2006. Revenues to customers outside of North America, which represents 3.4% of total revenues, decreased 18% in 2007 versus the comparable period in 2006.

During the three month period ended September 30, 2007, the Company increased its allowance for returns by \$1.1 million as a result of the voluntary withdrawal from the marketplace of two medicated pediatric cough and cold products marketed under the Little Remedies brand. This action was part of an industry wide voluntary withdrawal of these items pending the final results of an FDA safety and efficacy review. Excluding the impact of the withdrawal, total revenues for the Company would have been \$88.4 million, or 4.6% greater than the comparable period in 2006, and up 1.8% excluding the Wartner acquisition.

***Over-the-Counter Healthcare Segment***

Revenues of the Over-the-Counter Healthcare segment increased by \$3.7 million, or 8.1%, for 2007 versus the comparable period in 2006. The increase was primarily due to the acquisition of the Wartner brand in September 2006 and the launch of Murine™ Earigate™, a new product that helps prevent earwax build-up with its patented reverse spray technology. Excluding the impact of the Wartner acquisition, revenues increased by 3.2% for the period. In addition to Murine, Clear eyes®, New Skin and Dermoplast® revenues increased for the period. Clear eyes and New Skin revenue increased as a result of increased consumption, and Dermoplast revenue increased as a result of strong shipments to wholesale distributors of the institutional size item. These revenue increases were partially offset by an increase in the allowance for returns of \$1.1 million in connection with the voluntary withdrawal of Little Remedies medicated pediatric cough and cold products, lower shipments to the trade of Chloraseptic cough and cold products in advance of the flu season, softer consumption of Compound W Freeze-off® as a result of a contraction in the cryogenic sub-segment of the wart removal category and lower consumption of The Doctor's® NightGuard™ dental protector as a result of increased competition in the bruxism category.

***Household Cleaning Segment***

Revenues of the Household Cleaning segment were substantially unchanged at \$31.4 million, increasing only 0.6% during the quarter versus the comparable period in 2006. Revenues of the Comet® brand were essentially flat for the period and declines in Spic and Span were offset by increased revenue of Chore Boy. Revenue of Comet Mildew SprayGel, which was launched in the last quarter of fiscal 2007, was mostly offset by weak factory sales of Comet powder due to inventory reductions taken at a key mass merchandiser customer. The decline in Spic and Span's revenue reflected a decline in consumer sales. The increase of Chore Boy sales were a result of strong shipments to small grocer wholesale accounts; however, consumption declined during the period.

***Personal Care Segment***



Revenues of the Personal Care segment declined \$1.1 million or 16.1% for the period versus the comparable period in 2006. All major brands in this segment, except for Prell, experienced revenue declines during the period. The decrease in revenue of Cutex® and Denorex® were a result of declining consumption. Prell's revenue increased slightly for the period, in line with consumption.

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**Gross Profit**

|                    | 2007         |      | 2006         |      | Increase<br>(Decrease) |        |
|--------------------|--------------|------|--------------|------|------------------------|--------|
|                    | Gross Profit | %    | Gross Profit | %    |                        | %      |
| OTC Healthcare     | \$ 30,315    | 60.6 | \$ 28,254    | 61.1 | \$ 2,061               | 7.3    |
| Household Cleaning | 11,835       | 37.7 | 12,309       | 39.4 | (474)                  | (3.9)  |
| Personal Care      | 2,417        | 40.9 | 2,729        | 38.7 | (312)                  | (11.4) |
|                    | \$ 44,567    | 51.0 | \$ 43,292    | 51.2 | \$ 1,275               | 2.9    |

Gross profit for 2007 increased by \$1.3 million, or 2.9%, versus the comparable period in 2006. As a percent of total revenue, gross profit decreased slightly from 51.2% in 2006 to 51.0% during 2007. The decrease in gross profit as a percent of revenues is a result of a \$1.1 million increase in the allowance for returns in connection with the voluntary withdrawal of the two Little Remedies medicated products discussed above and related obsolescence charges of \$800,000.

***Over-the-Counter Healthcare Segment***

Gross profit of the Over-the-Counter Healthcare segment increased \$2.1 million, or 7.3%, for 2007 versus the comparable period in 2006. As a percent of OTC revenue, gross profit decreased from 61.1% for 2006 to 60.6% during 2007. The decrease in gross profit as a percent of revenues is a result of the \$1.1 million increase in the allowance for returns for the voluntary withdrawal of the Little Remedies medicated products discussed above and related obsolescence charges of \$800,000.

***Household Cleaning Segment***

Gross profit of the Household Cleaning segment decreased by \$474,000, or 3.9%, for 2007 versus the comparable period in 2006. As a percent of household cleaning revenue, gross profit decreased from 39.4% for 2006 to 37.7% during 2007. The decrease in gross profit percentage is primarily a result of higher product costs partially offset by lower distribution costs.

***Personal Care Segment***

Gross profit of the Personal Care segment decreased \$312,000, or 11.4%, for 2007 versus the comparable period in 2006. As a percent of personal care revenue, gross profit increased from 38.7% for 2006 to 40.9% during 2007. The increase in gross profit percentage was primarily a result of the favorable product mix toward the higher margin shampoo businesses.

**Contribution Margin**

|                    | 2007                   |      | 2006                   |      | Increase<br>(Decrease) |        |
|--------------------|------------------------|------|------------------------|------|------------------------|--------|
|                    | Contribution<br>Margin | %    | Contribution<br>Margin | %    |                        | %      |
| OTC Healthcare     | \$ 22,161              | 44.3 | \$ 21,196              | 45.8 | \$ 965                 | 4.6    |
| Household Cleaning | 9,260                  | 29.5 | 10,289                 | 32.9 | (1,029)                | (10.0) |
| Personal Care      | 2,129                  | 36.0 | 2,352                  | 33.4 | (223)                  | (9.5)  |
|                    | \$ 33,550              | 38.4 | \$ 33,837              | 40.0 | \$ (287)               | (0.8)  |

Contribution margin, defined as gross profit less advertising and promotional expenses, decreased \$287,000, or 0.8%, for 2007 versus the comparable period in 2006. The contribution margin decrease was a result of the increase in sales and gross profit as previously discussed, offset by a \$1.6 million, or a 16.6% increase in advertising and promotional spending. The increased advertising and promotional spending was primarily attributable to support behind the

launches of Murine Earigate and Comet Mildew SprayGel.

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***Over-the-Counter Healthcare Segment***

Contribution margin for the Over-the-Counter Healthcare segment increased by \$1.0 million, or 4.6%, for 2007 versus the comparable period in 2006. The contribution margin increase was a result of the increase in sales and gross profit as previously discussed, partially offset by a \$1.1 million, or a 15.5% increase in advertising and promotional spending. The increase in advertising and promotional spending was primarily a result of television media support behind the launch of Murine Earigate.

***Household Cleaning Segment***

Contribution margin for the Household Cleaning segment decreased by \$1.0 million, or 10.0%, for 2007 versus the comparable period in 2006. The contribution margin decrease was a result of a decrease in gross profit as previously discussed and \$600,000, or a 27.4% increase of advertising and promotional spending. The increase was principally a result of increased television media support behind Comet Mildew SprayGel.

***Personal Care Segment***

Contribution margin for the Personal Care segment decreased \$223,000, or 9.5%, for 2007 versus the comparable period in 2006. The contribution margin decrease was primarily a result of the sales and gross profit decrease previously discussed.

**General and Administrative**

General and administrative expenses were \$10.2 million for 2007 versus \$7.3 million for 2006. The increase was primarily related to higher legal costs associated with the OraSure arbitration and four intellectual property legal actions initiated by the Company associated with The Doctor's® NightGuard™ dental protector.

**Depreciation and Amortization**

Depreciation and amortization expense was \$2.8 million for 2007 versus \$2.4 million for 2006. The increase in amortization of intangible assets is related to the Wartner acquisition, which was partially offset by a slight reduction in depreciation expense.

**Interest Expense**

Net interest expense was \$9.6 million for 2007 versus \$9.7 million for 2006. The reduction in interest expenses was the result of a lower level of indebtedness partially offset by higher interest rates on our variable rate indebtedness. The average cost of funds increased from 7.9% for 2006 to 8.7% for 2007.

**Income Taxes**

The income tax provision for 2007 was \$4.2 million, with an effective rate of 38.0%, compared to \$5.6 million, with an effective rate of 39.1% for 2006. During the fiscal year ended March 31, 2007, the Company implemented various initiatives to obtain operational, as well as tax, efficiencies.

**Six Month Period Ended September 30, 2007 compared to the  
Six Month Period Ended September 30, 2006**

**Revenues**

|                    | 2007       |       | 2006       |       | Increase   |       |
|--------------------|------------|-------|------------|-------|------------|-------|
|                    | Revenues   | %     | Revenues   | %     | (Decrease) | %     |
| OTC Healthcare     | \$ 92,429  | 55.7  | \$ 85,853  | 53.5  | \$ 6,576   | 7.7   |
| Household Cleaning | 61,309     | 36.9  | 61,344     | 38.2  | (35)       | (0.1) |
| Personal Care      | 12,210     | 7.4   | 13,277     | 8.3   | (1,067)    | (8.0) |
|                    | \$ 165,948 | 100.0 | \$ 160,474 | 100.0 | \$ 5,474   | 3.4   |

Revenues for the six month period ended September 30, 2007 increased \$5.5 million, or 3.4%, versus the comparable period in 2006, primarily as a result of the acquisition of the Wartner brand in September of 2006. Excluding the impact of the Wartner acquisition, revenues were essentially flat versus the comparable period in 2006. Revenues to customers outside of North America, which represented 4.3% of total revenues, were flat in 2007 versus the comparable period in 2006.

During the period the Company increased its allowance for returns by \$1.1 million in connection with the voluntary withdrawal from the marketplace of two medicated pediatric cough and cold products marketed under the Little Remedies brand. This action was part of an industry wide voluntary withdrawal of these items pending the final results of an FDA safety and efficacy review. Excluding the impact of the withdrawal, total revenues for the Company would have been \$167.0 million, or 4.0% greater than the same period last year and up 0.7% excluding the Wartner acquisition.

***Over-the-Counter Healthcare Segment***

Revenues of the Over-the-Counter Healthcare segment increased by \$6.6 million, or 7.7%, for 2007 versus the comparable period in 2006. The revenue increases were primarily due to the acquisition of the Wartner brand in September 2006 and the launch of Murine Earigate™, a new product that helps prevent earwax build-up with its patented reverse spray technology. Excluding the impact of the Wartner acquisition, revenues increased by 1.4% for the period. Revenue increases from Murine Earigate™, Dermoplast and New Skin were partially offset by decreases in Chloraseptic, Clear eyes®, The Doctor's® and Little Remedies. New Skin's revenue increased as a result of higher consumption and market share gains in the liquid bandage category. Dermoplast's revenue increased as a result of strong shipments of the institutional size to wholesale distributors. Chloraseptic's revenue decreased as a result of weaker consumption and lower shipments to the trade in advance of the flu season. The Clear eyes revenue declined as a result of comparisons to strong pipeline sales of new items during the six month period ended September 30, 2006. The Doctor's® revenue decreased as a result of increased competition in the bruxism category. Little Remedies' revenue declined due to a \$1.1 million increase in the allowance for returns in connection with the voluntary withdrawal from the marketplace of Little Remedies medicated pediatric cough and cold products. Compound W® revenues were down slightly primarily due to softer trends in the cryogenic sub-segment of the wart removal category.

***Household Cleaning Segment***

Revenues of the Household Cleaning segment were essentially flat during the period versus the comparable period in 2006. Revenues of the Comet® brand were flat for the period and declines in Spic and Span were offset by increased revenue from Chore Boy. Revenue of Comet Mildew SprayGel, which launched in the last quarter of fiscal 2007, was offset by weaker factory sales of Comet powder and bathroom sprays. Comet was negatively affected by inventory reductions taken at a key mass merchandiser customer while bathroom sprays reflect declining consumption trends. The decline in Spic and Span's revenue was a result weaker consumption and in line with overall declines in the all purpose cleaning category. Chore Boy's revenue increases were a result of strong shipments to small grocery

wholesale accounts; however, Chore Boy's consumption declined during the period.

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**Personal Care Segment**

Revenues of the Personal Care segment declined \$1.1 million or 8.0% for 2007 versus the comparable period in 2006. All major brands in this segment, except for Prell, experienced revenue declines during the period. The decrease in revenues of Cutex® and Denorex® were a result of declining consumption. Prell's revenue increased for the period primarily due to improved consumption.

**Gross Profit**

|                    | 2007         |      | 2006         |      | Increase   |       |
|--------------------|--------------|------|--------------|------|------------|-------|
|                    | Gross Profit | %    | Gross Profit | %    | (Decrease) | %     |
| OTC Healthcare     | \$ 57,355    | 62.1 | 53,455       | 62.3 | \$ 3,900   | 7.3   |
| Household Cleaning | 23,329       | 38.1 | 24,249       | 39.5 | (920)      | (3.8) |
| Personal Care      | 5,172        | 42.4 | 5,186        | 39.1 | (14)       | (0.3) |
|                    | \$ 85,856    | 51.7 | \$ 82,890    | 51.1 | \$ 2,966   | 3.6   |

Gross profit for 2007 increased by \$3.0 million, or 3.6%, versus the comparable period in 2006. As a percent of total revenue, gross profit increased from 51.1% in 2006 to 51.7% during 2007. The increase in gross profit as a percent of revenues was a result of favorable sales mix to higher margin products partially offset by a \$1.1 million increase in the allowance for returns in connection with the voluntary withdrawal of the two Little Remedies medicated products discussed above and related obsolescence charges of \$800,000.

**Over-the-Counter Healthcare Segment**

Gross profit of the Over-the-Counter Healthcare segment increased \$3.9 million, or 7.3%, for 2007 versus the comparable period in 2006. As a percent of OTC revenue, gross profit decreased from 62.3% for 2006 to 62.1% during 2007. The decrease in gross profit as a percent of revenues was a result of a \$1.1 million increase in the allowance for returns in connection with the voluntary withdrawal of Little Remedies medicated product discussed above and related obsolescence charges of \$800,000.

**Household Cleaning Segment**

Gross profit of the Household Cleaning segment decreased by \$920,000, or 3.8%, for 2007 versus the comparable period in 2006. As a percent of household cleaning revenue, gross profit decreased from 39.5% for 2006 to 38.1% during 2007. The decrease in gross profit percentage was primarily a result of higher product costs partially offset by lower distribution costs. The product cost increases were a result of higher raw material costs.

**Personal Care Segment**

Gross profit of the Personal Care segment was flat for 2007 versus the comparable period in 2006. As a percent of personal care revenue, gross profit increased from 39.1% for 2006 to 42.4% during 2007. The increase in gross profit percentage was primarily a result of favorable product mix, lower returns and a reduction in promotional pricing allowances.

**Contribution Margin**

|                    | 2007                |      | 2006                |      | Increase   |       |
|--------------------|---------------------|------|---------------------|------|------------|-------|
|                    | Contribution Margin | %    | Contribution Margin | %    | (Decrease) | %     |
| OTC Healthcare     | \$ 43,320           | 46.9 | \$ 40,972           | 47.7 | \$ 2,348   | 5.7   |
| Household Cleaning | 19,126              | 31.2 | 20,539              | 32.5 | (1,413)    | (6.9) |

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|               |           |      |           |      |          |     |
|---------------|-----------|------|-----------|------|----------|-----|
| Personal Care | 4,607     | 37.7 | 4,522     | 34.1 | 85       | 1.9 |
|               | \$ 67,053 | 40.4 | \$ 66,033 | 41.1 | \$ 1,020 | 1.5 |

Contribution margin, defined as gross profit less advertising and promotional expenses, increased \$1.0 million, or 1.5%, for 2007 versus the comparable period in 2006. The contribution margin increase was a result of the

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increase in sales and gross profit as previously discussed, offset by a \$1.9 million or 11.5% increase in advertising and promotional spending. The increase in advertising and promotional spending was primarily attributable to support behind the launches of Murine Earigate and Comet Mildew SprayGel, and increased television media support of The Doctor's® NightGuard™ dental protector.

#### ***Over-the-Counter Healthcare Segment***

Contribution margin for the Over-the-Counter Healthcare segment increased by \$2.3 million, or 5.7%, for 2007 versus the comparable period in 2006. The contribution margin increase was a result of the increase in sales and gross profit as previously discussed, partially offset by a \$1.6 million, or a 5.7% increase in advertising and promotional spending. The increase in advertising and promotional spending was primarily a result of television media support behind the launch of Murine Earigate and The Doctor's® NightGuard™ dental protector.

#### ***Household Cleaning Segment***

Contribution margin for the Household Cleaning segment decreased by \$1.4 million, or 6.9%, for 2007 versus the comparable period in 2006. The contribution margin decrease was a result of flat sales and a decrease in gross profit as previously discussed and \$500,000, or a 13.3% increase of advertising and promotional spending. The increase was a result of an increase in television media support behind Comet Mildew SprayGel.

#### ***Personal Care Segment***

Contribution margin for the Personal Care segment increased \$85,000, or 1.9%, for 2007 versus the comparable period in 2006. The contribution margin increase was primarily the result of the sales and gross profit decrease previously discussed offset by a \$99,000 reduction in advertising and promotional spending.

#### **General and Administrative**

General and administrative expenses were \$17.8 million for 2007 versus \$13.7 million for 2006. The increase was primarily related to higher legal and stock-based compensation costs.

#### **Depreciation and Amortization**

Depreciation and amortization expense was \$5.5 million for 2007 versus \$4.8 million for 2006. The increase in amortization of intangible assets is related to the Wartner acquisition, which was partially offset by a slight reduction in depreciation expense.

#### **Interest Expense**

Net interest expense was \$19.3 million for 2007 versus \$19.5 million for 2006. The reduction in interest expenses was the result of a lower level of indebtedness partially offset by higher interest rates on our variable rate indebtedness. The average cost of funds increased from 7.9% for 2006 to 8.7% for 2007.

#### **Income Taxes**

The income tax provision for 2007 was \$9.3 million, with an effective rate of 38.0%, compared to \$10.9 million, with an effective rate of 39.1% for 2006. During the fiscal year ended March 31, 2007, the Company implemented various initiatives to obtain operational, as well as tax, efficiencies.

## Liquidity and Capital Resources

### Liquidity

We have financed and expect to continue to finance our operations with a combination of internally generated funds and borrowings. Pursuant to the terms of the Senior Credit Facility, we may borrow an additional \$200.0 million under our Tranche B Term Loan Facility and up to a maximum of \$60.0 million under our Revolving Credit Facility. Our principal uses of cash are for operating expenses, debt service, acquisitions, working capital and capital expenditures.

| <i>(In thousands)</i>        | Six Months Ended September 30 |           |
|------------------------------|-------------------------------|-----------|
|                              | 2007                          | 2006      |
| Cash provided by (used for): |                               |           |
| Operating Activities         | \$ 21,492                     | \$ 42,734 |
| Investing Activities         | (210)                         | (31,555)  |
| Financing Activities         | (26,241)                      | (8,871)   |

### Operating Activities

Net cash provided by operating activities was \$21.5 million for 2007 compared to \$42.7 million 2006. The \$21.2 million decrease in net cash provided by operating activities was primarily the result of the following:

- A decrease of net income of \$1.9 million from \$17.0 million for 2006 to \$15.1 million for 2007, and
- An increase in the components of working capital caused primarily by an increase in accounts receivable resulting from the timing of sales in advance of the cough/cold season, as well as an increase in accrued liabilities resulting from the recognition of costs associated with the voluntary withdrawal from the marketplace of two medicated pediatric cough and cold products marketed under the Little Remedies brand.

### Investing Activities

Net cash used for investing activities was \$210,000 for 2007 compared to \$31.6 million for 2006. The net cash used for investing activities for 2007 was primarily for the acquisition of machinery, computers and office equipment, while for 2006, net cash was used primarily for the acquisition of Wartner USA B.V.

### Financing Activities

Net cash used for financing activities was \$26.2 million for 2007 compared to \$8.9 million for 2006. During 2007, the Company repaid \$24.5 million of indebtedness in excess of normal maturities with cash generated from operations. This reduced our outstanding indebtedness to \$437.1 million from \$463.4 million at March 31, 2007. During 2006, the Company repaid the remaining \$7.0 million indebtedness related to our Revolving Credit Facility which was drawn upon in connection with the November 2005 acquisition of Dental Concepts LLC.

The Company's cash flow from operations is normally expected to exceed net income due to the substantial non-cash charges related to depreciation and amortization of intangibles, increases in deferred income tax liabilities resulting from differences in the amortization of intangible assets and goodwill for income tax and financial reporting purposes, the amortization of certain deferred financing costs and stock-based compensation.

### Capital Resources

As of September 30, 2007, we had an aggregate of \$437.1 million of outstanding indebtedness, which consisted of the following:

- \$311.1 million of borrowings under the Tranche B Term Loan Facility, and
- \$126.0 million of 9.25% Senior Subordinated Notes due 2012.



We had \$60.0 million of borrowing capacity available under the Revolving Credit Facility at September 30, 2007, as well as \$200.0 million available under the Tranche B Term Loan Facility.

All loans under the Senior Credit Facility bear interest at floating rates, based on either the prime rate, or at our option, the LIBOR rate, plus an applicable margin. As of September 30, 2007, an aggregate of \$311.1 million was outstanding under the Senior Credit Facility at a weighted average interest rate of 7.74%.

In June 2004, we purchased a 5% interest rate cap agreement with a notional amount of \$20.0 million which expired in June 2006. In March 2005, we purchased interest rate cap agreements that became effective August 30, 2005, with a total notional amount of \$180.0 million and LIBOR cap rates ranging from 3.25% to 3.75%. On May 31, 2006, an interest rate cap agreement with a notional amount of \$50.0 million and a 3.25% cap rate expired. Additionally, an interest rate cap agreement with a notional amount of \$80.0 million and a 3.50% cap rate expired on May 30, 2007. The remaining agreement, with a notional amount of \$50.0 million and a cap rate of 3.75%, terminates on May 30, 2008. The fair value of the interest rate cap agreement was \$486,000 at September 30, 2007.

The Tranche B Term Loan Facility matures in October 2011. We must make quarterly principal payments on the Tranche B Term Loan Facility equal to \$887,500, representing 0.25% of the initial principal amount of the term loan. The Revolving Credit Facility matures and the commitments relating to the Revolving Credit Facility terminate in April 2009.

The Senior Credit Facility contains various financial covenants, including provisions that require us to maintain certain leverage ratios, interest coverage ratios and fixed charge coverage ratios. In addition, the Senior Credit Facility, as well as the Indenture governing the Senior Subordinated Notes, contain provisions that accelerate our indebtedness on certain changes in control and restrict us from undertaking specified corporate actions, including asset dispositions, acquisitions, payment of dividends and other specified payments, repurchasing the Company's equity securities in the public markets, incurrence of indebtedness, creation of liens, making loans and investments and transactions with affiliates. Specifically, we must:

- Have a leverage ratio of less than 4.5 to 1.0 for the quarter ended September 30, 2007, decreasing over time to 3.75 to 1.0 for the quarter ending September 30, 2010, and remaining level thereafter,
- Have an interest coverage ratio of greater than 2.75 to 1.0 for the quarter ended September 30, 2007, increasing over time to 3.25 to 1.0 for the quarter ending March 31, 2010, and
- Have a fixed charge coverage ratio of greater than 1.5 to 1.0 for the quarter ended September 30, 2007, and for each quarter thereafter until the quarter ending March 31, 2011.

At September 30, 2007, we were in compliance with the applicable financial and restrictive covenants under the Senior Credit Facility and the Indenture governing the Senior Subordinated Notes.

Our principal sources of funds are anticipated to be cash flows from operating activities and available borrowings under the Senior Credit Facility. We believe that these funds will provide us with sufficient liquidity and capital resources for us to meet our current and future financial obligations, as well as to provide funds for working capital, capital expenditures and other needs for at least the next 12 months. As part of our growth strategy, we regularly review acquisition opportunities and other potential strategic transactions, which may require additional debt or equity financing. If additional financing is required, there are no assurances that it will be available, or if available, that it can be obtained on terms favorable to us or on a basis that is not dilutive to our stockholders.

### **Off-Balance Sheet Arrangements**

We do not have any off-balance sheet arrangements or financing activities with special-purpose entities.

### **Inflation**

Inflationary factors such as increases in the costs of raw materials, packaging materials, purchased product and overhead may adversely affect our operating results. Although we do not believe that inflation has had a material impact on our financial condition or results from operations for the periods referred to above, a high rate of inflation in the future could have a material adverse effect on our business, financial condition or results from operations. The current volatility of the crude oil markets will continue to impact, at times favorably and at times unfavorably, our transportation costs, as well as, certain petroleum based raw materials and packaging materials. Although the Company takes efforts to minimize the impact of inflationary factors, including raising prices to our customers, a sustained rate of pricing increases associated with crude oil supplies may have an adverse effect on our operating results.

### **Seasonality**

The first quarter of our fiscal year typically has the lowest level of revenue due to the seasonal nature of certain of our brands relative to the summer and winter months. In addition, the first quarter is the least profitable quarter due to the increased advertising and promotional spending to support those brands with a summer selling season, such as Compound W, Wartner, Cutex and New Skin. The Company's advertising and promotional campaign in the third quarter influence sales in the fourth quarter winter months. Additionally, the fourth quarter typically has the lowest level of advertising and promotional spending as a percent of revenue.

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## Critical Accounting Policies and Estimates

The Company's significant accounting policies are described in the notes to the unaudited financial statements included elsewhere in this Quarterly Report on Form 10-Q, as well as in our Annual Report on Form 10-K for the year ended March 31, 2007. While all significant accounting policies are important to our consolidated financial statements, certain of these policies may be viewed as being critical. Such policies are those that are both most important to the portrayal of our financial condition and results from operations and require our most difficult, subjective and complex estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses or the related disclosure of contingent assets and liabilities. These estimates are based upon our historical experience and on various other assumptions that we believe to be reasonable under the circumstances. Actual results may differ materially from these estimates under different conditions. The most critical accounting policies are as follows:

### *Revenue Recognition*

We comply with the provisions of Securities and Exchange Commission Staff Accounting Bulletin 104 "Revenue Recognition," which states that revenue should be recognized when the following revenue recognition criteria are met: (1) persuasive evidence of an arrangement exists; (2) the product has been shipped and the customer takes ownership and assumes the risk of loss; (3) the selling price is fixed or determinable; and (4) collection of the resulting receivable is reasonably assured. We have determined that the transfer of risk of loss occurs when product is received by the customer, and, accordingly recognize revenue at that time. Provision is made for estimated discounts related to customer payment terms and estimated product returns at the time of sale based on our historical experience.

As is customary in the consumer products industry, we participate in the promotional programs of our customers to enhance the sale of our products. The cost of these promotional programs is recorded in accordance with Emerging Issues Task Force 01-09, "*Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)*" as either advertising and promotional expenses or as a reduction of sales. Such costs vary from period-to-period based on the actual number of units sold during a finite period of time. We estimate the cost of such promotional programs at their inception based on historical experience and current market conditions and reduce sales by such estimates. These promotional programs consist of direct to consumer incentives such as coupons and temporary price reductions, as well as incentives to our customers, such as slotting fees and cooperative advertising. We do not provide incentives to customers for the acquisition of product in excess of normal inventory quantities since such incentives increase the potential for future returns, as well as reduce sales in the subsequent fiscal periods.

Estimates of costs of promotional programs are based on (i) historical sales experience, (ii) the current offering, (iii) forecasted data, (iv) current market conditions, and (v) communication with customer purchasing/marketing personnel. At the completion of the promotional program, the estimated amounts are adjusted to actual results. While our promotional expense for the year ended March 31, 2007 was \$16.5 million, we participated in 5,900 promotional campaigns, resulting in an average cost of \$2,800 per campaign. Of such amount, only 582 payments were in excess of \$5,000. We believe that the estimation methodologies employed, combined with the nature of the promotional campaigns, makes the likelihood remote that our obligation would be misstated by a material amount. However, for illustrative purposes, had we underestimated the promotional program rate by 10% for the three and six month periods ended September 30, 2007, our sales and operating income would have been adversely affected by approximately \$529,00 and \$993,000, respectively.

We also periodically run coupon programs in Sunday newspaper inserts or as on-package instant redeemable coupons. We utilize a national clearing house to process coupons redeemed by customers. At the time a coupon is distributed, a provision is made based upon historical redemption rates for that particular product, information provided as a result of the clearing house's experience with coupons of similar dollar value, the length of time the coupon is valid, and the seasonality of the coupon drop, among other factors. During the year ended March 31, 2007, we had 17 coupon events. The amount recorded against revenues and accrued for these events during the year was

\$2.7 million, of which \$2.3 million was redeemed during the year. During the six month period ended September 30, 2007, we had 16 coupon events. The amount recorded against revenues and accrued for these events during the three and six month periods ended September 30, 2007 was \$602,000 and \$1.1 million,

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respectively. Redemptions during the three and six month periods ended September 30, 2007 were \$696,000 and \$1.1 million, respectively.

#### ***Allowances for Product Returns***

Due to the nature of the consumer products industry, we are required to estimate future product returns. Accordingly, we record an estimate of product returns concurrent with the recording of sales. Such estimates are made after analyzing (i) historical return rates, (ii) current economic trends, (iii) changes in customer demand, (iv) product acceptance, (v) seasonality of our product offerings, and (vi) the impact of changes in product formulation, packaging and advertising.

We construct our returns analysis by looking at the previous year's return history for each brand. Subsequently, each month, we estimate our current return rate based upon an average of the previous six months' return rate and review that calculated rate for reasonableness giving consideration to the other factors described above. Our historical return rate has been relatively stable; for example, for the years ended March 31, 2007, 2006 and 2005, returns represented 3.7%, 3.5%, and 3.6%, respectively, of gross sales. At September 30, 2007 and March 31, 2007, the allowances for sales returns were \$2.1 million and \$1.8 million, respectively.

While we utilize the methodology described above to estimate product returns, actual results may differ materially from our estimates, causing our future financial results to be adversely affected. Among the factors that could cause a material change in the estimated return rate would be significant unexpected returns with respect to a product or products that comprise a significant portion of our revenues. Based upon the methodology described above and our actual returns' experience, management believes the likelihood of such a material occurrence is remote. As noted, over the last three years, our actual product return rate has stayed within a range of 3.5% to 3.7% of gross sales. An increase of 0.1% in our estimated return rate as a percentage of gross sales would have adversely affected our reported sales and operating income for the three and six month periods ended September 30, 2007 by approximately \$102,000 and \$193,000, respectively.

#### ***Allowances for Obsolete and Damaged Inventory***

We value our inventory at the lower of cost or market value. Accordingly, we reduce our inventories for the diminution of value resulting from product obsolescence, damage or other issues affecting marketability equal to the difference between the cost of the inventory and its estimated market value. Factors utilized in the determination of estimated market value include (i) current sales data and historical return rates, (ii) estimates of future demand, (iii) competitive pricing pressures, (iv) new product introductions, (v) product expiration dates, and (vi) component and packaging obsolescence.

Many of our products are subject to expiration dating. As a general rule our customers will not accept goods with expiration dating of less than 12 months from the date of delivery. To monitor this risk, management utilizes a detailed compilation of inventory with expiration dating between zero and 15 months and reserves for 100% of the cost of any item with expiration dating of 12 months or less. At September 30, 2007 and March 31, 2007, the allowance for obsolete and slow moving inventory represented 4.4% and 5.8%, respectively, of total inventory. Inventory obsolescence costs charged to operations for the three and six month periods ended September 30, 2007 were \$872,000 and \$583,000, respectively. During the three month period ended June 30, 2007, the Company recorded a credit of \$289,000 to operations for obsolescence due to the settlement of a claim from a vendor. A 1.0% increase in our allowance for obsolescence at September 30, 2007 would have adversely affected our reported operating income for the three and six month periods ended September 30, 2007 by approximately \$291,000.

#### ***Allowance for Doubtful Accounts***

In the ordinary course of business, we grant non-interest bearing trade credit to our customers on normal credit terms. We maintain an allowance for doubtful accounts receivable which is based upon our historical collection experience and expected collectibility of the accounts receivable. In an effort to reduce our credit risk, we (i) establish credit limits for all of our customer relationships, (ii) perform ongoing credit evaluations of our customers' financial



condition, (iii) monitor the payment history and aging of our customers' receivables, and (iv) monitor open orders against an individual customer's outstanding receivable balance.

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We establish specific reserves for those accounts which file for bankruptcy, have no payment activity for 180 days or have reported major negative changes to their financial condition. The allowance for bad debts at September 30, 2007 and March 31, 2007 amounted to 0.12% and 0.10%, respectively, of accounts receivable. For the three and six months ended September 30, 2007 we recorded bad debt expense of \$15,000 and \$99,000, respectively, while during the three and six month periods ended September 30, 2006 we recorded bad debt recoveries of \$67,000 and \$12,000, respectively.

While management believes that it is diligent in its evaluation of the adequacy of the allowance for doubtful accounts, an unexpected event, such as the bankruptcy filing of a major customer, could have an adverse effect on our future financial results. A 0.1% increase in our bad debt expense as a percentage of net sales would have resulted in a decrease in operating income for the three and six month periods ended September 30, 2007 of approximately \$87,000 and \$165,000, respectively.

### ***Valuation of Intangible Assets and Goodwill***

Goodwill and intangible assets amounted to \$960.8 million and \$968.1 million at September 30, 2007 and March 31, 2007, respectively. As of September 30, 2007, goodwill and intangible assets were apportioned among our three operating segments as follows:

|                          | <b>Over-the-Counter<br/>Healthcare</b> | <b>Household<br/>Cleaning</b> | <b>Personal<br/>Care</b> | <b>Consolidated</b> |
|--------------------------|--|-------------------------------|--------------------------|---------------------|
| Goodwill                 | \$ 233,615                             | \$ 72,549                     | \$ 2,751                 | \$ 308,915          |
| <b>Intangible assets</b> |  |                               |                          |                     |
| Indefinite lived         | 374,070                                | 170,893                       | --                       | 544,963             |
| Finite lived             | 90,986                                 | 15                            | 15,939                   | 106,940             |
|                          | 465,056                                | 170,908                       | 15,939                   | 651,903             |
|                          | \$ 698,671                             | \$ 243,457                    | \$ 18,690                | \$ 960,818          |

Our Clear Eyes, New-Skin, Chloraseptic, Compound W and Wartner brands comprise the majority of the value of the intangible assets within the Over-The-Counter Healthcare segment. The Comet, Spic and Span and Chore Boy brands comprise substantially all of the intangible asset value within the Household Cleaning segment. Denorex, Cutex and Prell comprised substantially all of the intangible asset value within the Personal Care segment.

Goodwill and intangible assets comprise substantially all of our assets. Goodwill represents the excess of the purchase price over the fair value of assets acquired and liabilities assumed in a purchase business combination. Intangible assets generally represent our trademarks, brand names and patents. When we acquire a brand, we are required to make judgments regarding the value assigned to the associated intangible assets, as well as their respective useful lives. Management considers many factors, both prior to and after, the acquisition of an intangible asset in determining the value, as well as the useful life, assigned to each intangible asset that the Company acquires or continues to own and promote. The most significant factors are:

- **Brand History**

A brand that has been in existence for a long period of time (*e.g.*, 25, 50 or 100 years) generally warrants a higher valuation and longer life (sometimes indefinite) than a brand that has been in existence for a very short period of time. A brand that has been in existence for an extended period of time generally has been the subject of considerable investment by its previous owner(s) to support product innovation and advertising and promotion.



• **Market Position**

Consumer products that rank number one or two in their respective market generally have greater name recognition and are known as quality product offerings, which warrant a higher valuation and longer life than products that lag in the marketplace.

• **Recent and Projected Sales Growth**

Recent sales results present a snapshot as to how the brand has performed in the most recent time periods and represent another factor in the determination of brand value. In addition, projected sales growth provides information about the strength and potential longevity of the brand. A brand that has both strong current and projected sales generally warrants a higher valuation and a longer life than a brand that has weak or declining sales. Similarly, consideration is given to the potential investment, in the form of advertising and promotion, that is required to reinvigorate a brand that has fallen from favor.

• **History of and Potential for Product Extensions**

Consideration also is given to the product innovation that has occurred during the brand's history and the potential for continued product innovation that will determine the brand's future. Brands that can be continually enhanced by new product offerings generally warrant a higher valuation and longer life than a brand that has always "followed the leader".

After consideration of the factors described above, as well as current economic conditions and changing consumer behavior, management prepares a determination of the intangible's value and useful life based on its analysis of the requirements of Statements No. 141 and No. 142. Under Statement No. 142, goodwill and indefinite-lived intangible assets are no longer amortized, but must be tested for impairment at least annually. Intangible assets with finite lives are amortized over their respective estimated useful lives and must also be tested for impairment.

On an annual basis, or more frequently if conditions indicate that the carrying value of the asset may not be recovered, management performs a review of both the values and useful lives assigned to goodwill and intangible assets and tests for impairment.

*Finite-Lived Intangible Assets*

As mentioned above, management performs an annual review or more frequently if necessary, to ascertain the impact of events and circumstances on the estimated useful lives and carrying values of our trademarks and trade names. In connection with this analysis, management:

- Reviews period-to-period sales and profitability by brand,
- Analyzes industry trends and projects brand growth rates,
  - Prepares annual sales forecasts,
  - Evaluates advertising effectiveness,
    - Analyzes gross margins,
  - Reviews contractual benefits or limitations,
- Monitors competitors' advertising spend and product innovation,
- Prepares projections to measure brand viability over the estimated useful life of the intangible asset, and
  - Considers the regulatory environment, as well as industry litigation.

Should analysis of any of the aforementioned factors warrant a change in the estimated useful life of the intangible asset, management will reduce the estimated useful life and amortize the carrying value prospectively over the shorter remaining useful life. Management's projections are utilized to assimilate all of the facts, circumstances and expectations related to the trademark or trade name and estimate the cash flows over its useful life. In the event that the long-term projections indicate that the carrying value is in excess of the undiscounted cash flows expected to result from the use of the intangible assets, management is required to record an impairment charge. Once that analysis is completed, a discount rate is applied to the cash flows to estimate fair value. The impairment charge is measured as the excess of the carrying amount of the intangible asset over fair



value as calculated using the discounted cash flow analysis. Future events, such as competition, technological advances and reductions in advertising support for our trademarks and trade names could cause subsequent evaluations to utilize different assumptions.

#### *Indefinite-Lived Intangible Assets*

In a manner similar to finite-lived intangible assets, on an annual basis, or more frequently if necessary, management analyzes current events and circumstances to determine whether the indefinite life classification for a trademark or trade name continues to be valid. Should circumstance warrant a finite life, the carrying value of the intangible asset would then be amortized prospectively over the estimated remaining useful life.

In connection with this analysis, management also tests the indefinite-lived intangible assets for impairment by comparing the carrying value of the intangible asset to its estimated fair value. Since quoted market prices are seldom available for trademarks and trade names such as ours, we utilize present value techniques to estimate fair value. Accordingly, management's projections are utilized to assimilate all of the facts, circumstances and expectations related to the trademark or trade name and estimate the cash flows over its useful life. In performing this analysis, management considers the same types of information as listed above in regards to finite-lived intangible assets. Once that analysis is completed, a discount rate is applied to the cash flows to estimate fair value. Future events, such as competition, technological advances and reductions in advertising support for our trademarks and trade names could cause subsequent evaluations to utilize different assumptions.

#### *Goodwill*

As part of its annual test for impairment of goodwill, management estimates the discounted cash flows of each reporting unit, which is at the brand level, and one level below the operating segment level, to estimate their respective fair values. In performing this analysis, management considers the same types of information as listed above in regards to finite-lived intangible assets. In the event that the carrying amount of the reporting unit exceeds the fair value, management would then be required to allocate the estimated fair value of the assets and liabilities of the reporting unit as if the unit was acquired in a business combination, thereby revaluing the carrying amount of goodwill. In a manner similar to indefinite-lived assets, future events, such as competition, technological advances and reductions in advertising support for our trademarks and trade names could cause subsequent evaluations to utilize different assumptions.

In estimating the value of trademarks and trade names, as well as goodwill, at March 31, 2007, management applied a discount rate of 9.5%, the Company's then current weighted-average cost of funds, to the estimated cash flows; however that rate, as well as future cash flows may be influenced by such factors, including (i) changes in interest rates, (ii) rates of inflation, or (iii) sales or contribution margin reductions. In the event that the carrying value exceeded the estimated fair value of either intangible assets or goodwill, we would be required to recognize an impairment charge. Additionally, continued decline of the fair value ascribed to an intangible asset or a reporting unit caused by external factors may require future impairment charges.

During the three month period ended March 31, 2006, we recorded non-cash charges related to the impairment of intangible assets and goodwill of the Personal Care segment of \$7.4 million and \$1.9 million, respectively, because the carrying amounts of these "branded" assets exceeded their fair market values primarily as a result of declining sales caused by product competition. Should the related fair values of goodwill and intangible assets continue to be adversely affected as a result of declining sales or margins caused by competition, technological advances or reductions in advertising and promotional expenses, the Company may be required to record additional impairment charges.

#### *Stock-Based Compensation*

During 2006, we adopted FASB Statement No. 123(R), "Share-Based Payment" ("Statement No. 123(R)") with the initial grants of restricted stock and options to purchase common stock to employees and directors in accordance with the provisions of the Plan. Statement No. 123(R) requires us to measure the cost of services to be rendered based on the

grant-date fair value of the equity award. Compensation expense is to be recognized over the period which an employee is required to provide service in exchange for the award, generally referred to

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as the requisite service period. Information utilized in the determination of fair value includes the following:

- Type of instrument (i.e.: restricted shares vs. an option, warrant or performance shares),
  - Strike price of the instrument,
- Market price of the Company's common stock on the date of grant,
  - Discount rates,
  - Duration of the instrument, and
- Volatility of the Company's common stock in the public market.

Additionally, management must estimate the expected attrition rate of the recipients to enable it to estimate the amount of non-cash compensation expense to be recorded in our financial statements. While management uses diligent analysis to estimate the respective variables, a change in assumptions or market conditions, as well as changes in the anticipated attrition rates, could have a significant impact on the future amounts recorded as non-cash compensation expense. The Company recorded stock-based compensation costs of \$655,000 and \$383,000 during the fiscal years ended March 31, 2007 and 2006, respectively. During the three and six month periods ended September 30, 2007, the Company recorded stock-based compensation costs of \$685,000 and \$1.1 million, respectively. During the three and six month periods ended September 30, 2006, the Company recorded stock-based compensation costs of \$233,000 and \$224,000, respectively. The period-to-period decrease resulted from the recording of a net stock-based compensation credit of \$9,000 during the three month period ended June 30, 2006 due to the reversal of stock-based compensation costs in the amount of \$142,000 associated with the departure of a former member of management.

#### ***Loss Contingencies***

Loss contingencies are recorded as liabilities when it is probable that a liability has been incurred and the amount of such loss is reasonable estimable. Contingent losses are often resolved over longer periods of time and involve many factors including:

- Rules and regulations promulgated by regulatory agencies,
  - Sufficiency of the evidence in support of our position,
    - Anticipated costs to support our position, and
    - Likelihood of a positive outcome.

#### ***Recent Accounting Pronouncements***

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities - Including an amendment of FASB Statement No. 115" ("Statement No. 159"). Statement No. 159 permits companies to choose to measure certain financial instruments and certain other items at fair value. Unrealized gains and losses on items for which the fair value option has been elected will be recognized in earnings at each subsequent reporting date. Statement No. 159 is effective for interim financial statements issued during the fiscal year beginning after November 15, 2007. The Company is evaluating the impact that the adoption of Statement No. 159 will have on its consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("Statement No. 157") to address inconsistencies in the definition and determination of fair value pursuant to generally accepted accounting principles ("GAAP"). Statement No. 157 provides a single definition of fair value, establishes a framework for measuring fair value in GAAP and expands disclosures about fair value measurements in an effort to increase comparability related to the recognition of market-based assets and liabilities and their impact on earnings. Statement No. 157 is effective for interim financial statements issued during the fiscal year beginning after November 15, 2007.

Management has reviewed and continues to monitor the actions of the various financial and regulatory reporting agencies and is currently not aware of any other pronouncement that could have a material impact on the Company's consolidated financial position, results of operations or cash flows.





## CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995 (the “PSLR Act”), including, without limitation, information within Management’s Discussion and Analysis of Financial Condition and Results of Operations. The following cautionary statements are being made pursuant to the provisions of the PSLR Act and with the intention of obtaining the benefits of the “safe harbor” provisions of the PSLR Act. Although we believe that our expectations are based on reasonable assumptions, actual results may differ materially from those in our forward-looking statements.

Forward-looking statements speak only as of the date of this Quarterly Report on Form 10-Q. Except as required under federal securities laws and the rules and regulations of the SEC, we do not have any intention to update any forward-looking statements to reflect events or circumstances arising after the date of this Quarterly Report on Form 10-Q, whether as a result of new information, future events or otherwise.

Our forward-looking statements generally can be identified by the use of words or phrases such as “believe,” “anticipate,” “expect,” “estimate,” “project,” “will be,” “will continue,” “will likely result,” or other similar words or phrases. Forward-looking statements and our plans and expectations are subject to a number of risks and uncertainties that could cause actual results to differ materially from those anticipated, and our business in general is subject to such risks. As a result of these risks and uncertainties, readers are cautioned not to place undue reliance on forward-looking statements included in this Quarterly Report on Form 10-Q or that may be made elsewhere from time to time by, or on behalf of, us. All forward-looking statements attributable to us are expressly qualified by these cautionary statements. For more information, see “Risk Factors” contained in Part I, Item 1A of our Annual Report on Form 10-K for the year ended March 31, 2007. In addition, our expectations or beliefs concerning future events involve risks and uncertainties, including, without limitation:

- General economic conditions affecting our products and their respective markets,
  - The high level of competition in our industry and markets,
- Our dependence on a limited number of customers for a large portion of our sales,
  - Disruptions in our distribution center,
- Acquisitions or other strategic transactions diverting managerial resources, or incurrence of additional liabilities or integration problems associated with such transactions,
  - Changing consumer trends or pricing pressures which may cause us to lower our prices,
    - Increases in supplier prices,
      - Increases in transportation fees and fuel charges,
      - Changes in our senior management team,
    - Our ability to protect our intellectual property rights,
    - Our dependency on the reputation of our brand names,
  - Shortages of supply of sourced goods or interruptions in the manufacturing of our products,
    - Our level of debt, and ability to service our debt,

- Any adverse judgment rendered in any pending litigation or arbitration,
  - Our ability to obtain additional financing, and
- The restrictions imposed by our financing agreements on our operations.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We are exposed to changes in interest rates because our Senior Credit Facility is variable rate debt. Interest rate changes, therefore, generally do not affect the market value of our senior secured financing, but do impact the amount of our interest payments and, therefore, our future earnings and cash flows, assuming other factors are held constant. At September 30, 2007, we had variable rate debt of approximately \$311.1 million related to our Tranche B term loan.

In an effort to protect the Company from the adverse impact that rising interest rates would have on our variable rate debt, we have entered into various interest rate cap agreements to hedge this exposure. In June 2004, we purchased a 5% interest rate cap agreement with a notional amount of \$20.0 million which terminated in June 2006. In March 2005, we purchased interest rate cap agreements that became effective August 30, 2005, with a total notional amount of \$180.0 million and LIBOR cap rates ranging from 3.25% to 3.75%. On May 31, 2006, an interest rate cap agreement with a notional amount of \$50.0 million and a 3.25% cap rate expired. Additionally, an interest rate cap agreement with a notional amount of \$80.0 million and a 3.5% cap rate expired on May 31, 2007. The remaining agreement, with a notional amount of \$50.0 million and a cap rate of 3.75% terminates on May 31, 2008.

Holding other variables constant, including levels of indebtedness, a one percentage point increase in interest rates on our variable rate debt would have an adverse impact on pre-tax earnings and cash flows for fiscal 2008 of approximately \$3.1 million. However, given the protection afforded by the interest rate cap agreements, the impact of a one percentage point increase would be limited to \$2.8 million. The fair value of the interest rate cap agreement was \$486,000 at September 30, 2007.

### **ITEM 4. CONTROLS AND PROCEDURES**

#### **Disclosure Controls and Procedures**

The Company's management, with the participation of its Chief Executive Officer and the Chief Financial Officer, evaluated the effectiveness of the Company's disclosure controls and procedures, as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934 ("Exchange Act"), as of September 30, 2007. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that, as of September 30, 2007, the Company's disclosure controls and procedures were effective to ensure that information required to be disclosed by the Company in the reports the Company files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

#### **Changes in Internal Control over Financial Reporting**

There have been no changes during the quarter ended September 30, 2007 in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## **PART OTHER INFORMATION**

### **II.**

#### **ITEM LEGAL PROCEEDINGS**

##### **1.**

The legal proceedings in which we are involved have been disclosed previously in our Annual Report on Form 10-K for the fiscal year ended March 31, 2007, our Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2007 and our Current Report on Form 8-K filed with the SEC on October 24, 2007. The following disclosure contains recent developments in our pending legal proceedings and should be read in conjunction with the legal proceedings disclosure contained in Part I, Item 3 of our Annual Report on Form 10-K for the fiscal year ended March 31, 2007, Part II, Item 1 of our Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2007 and our Current Report on Form 8-K filed with the SEC on October 24, 2007.

##### *Securities Class Action Litigation*

On September 4, 2007, the United States District Court for the Southern District of New York issued an Order certifying a class consisting of all persons who purchased the common stock of the Company pursuant to, or traceable to, the Company's initial public offering on or about February 9, 2005 through November 15, 2005 and were damaged thereby. The Company's management continues to believe that the remaining claims in the case are legally deficient and that it has meritorious defenses to the claims that remain. The Company intends to vigorously defend against the claims remaining in the case; however, the Company cannot reasonably estimate the potential range of loss, if any.

##### *OraSure Technologies Arbitration*

At the end of August 2007, the Company and OraSure Technologies, Inc. ("OraSure") participated in an arbitration hearing at which each party presented its case to the arbitration panel. On October 22, 2007, the Company received notification from the arbitrators that they had issued a Partial Final Award (the "Award") in the pending arbitration with OraSure. The arbitrators acknowledged that there was a technical breach of the non-compete clause in the Distribution Agreement between the parties but OraSure's proof of damages was speculative and not supported by credible evidence. Therefore, the arbitrators awarded nominal damages to OraSure in the amount of One Dollar (\$1.00). In addition, the arbitrators awarded to OraSure counsel fees and arbitrator compensation in an amount to be determined pursuant to further proceedings. The Company will vigorously contest the award of fees to OraSure as the Company believes that OraSure should only be entitled to a modest award in light of the arbitrators' rejection of OraSure's asserted damages and claims beyond the One Dollar (\$1.00) nominal award.

The arbitration panel also dismissed with prejudice OraSure's remaining claims for breach of the Distribution Agreement, OraSure's request for injunctive relief and the Company's counterclaims, respectively. Furthermore, the arbitrators confirmed the Company's position that the Distribution Agreement will terminate on December 31, 2007. The Company does not expect any interruptions in supply of its Compound W Freeze Off® branded cryosurgical wart remover as it transitions to a new supplier after December 31, 2007.

##### *DenTek Oral Care, Inc. Litigation*

In April 2007, the Company filed a lawsuit in the U.S. District Court in the Southern District of New York against DenTek Oral Care, Inc. ("DenTek") alleging (i) infringement of intellectual property associated with The Doctor's® NightGuard™ dental protector which is used for the protection of teeth from nighttime teeth grinding; and (ii) the violation of unfair competition and consumer protection laws. On October 4, 2007, the Company filed a Second Amended Complaint in which it named Kelly M. Kaplan, Raymond Duane and C.D.S. Associates, Inc. as additional defendants in the action against DenTek and added other claims to the previously filed complaint. Ms. Kaplan and Mr. Duane were formerly employed by the Company and C.D.S. Associates, Inc. is a corporation controlled by Mr. Duane. In the Second Amended Complaint, the Company has alleged patent, trademark and copyright infringement, unfair competition, unjust enrichment, violation of New York's Consumer Protection Act, breach of contract, tortious interference with contractual and business relations, civil conspiracy and trade secret misappropriation. On October

19, 2007, the Company filed a motion for preliminary injunction with the Court in which the Company has asked the Court to enjoin the defendants from (i) continuing to improperly use the Company's trade secrets; (ii) continuing to breach any contractual agreements with the Company; and (iii) marketing and selling any dental protector products or other products in which Ray Duane or Kelly Kaplan has had any involvement or provided any assistance to DenTek. A hearing date for the motion for preliminary

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injunction has not yet been set by the Court. Discovery requests have been served by the parties and discovery is ongoing.

In addition to the matters described above, the Company is involved from time to time in other routine legal matters and other claims incidental to its business. The Company reviews outstanding claims and proceedings internally and with external counsel as necessary to assess probability and amount of potential loss. These assessments are re-evaluated at each reporting period and as new information becomes available to determine whether a reserve should be established or if any existing reserve should be adjusted. The actual cost of resolving a claim or proceeding ultimately may be substantially different than the amount of the recorded reserve. In addition, because it is not permissible under GAAP to establish a litigation reserve until the loss is both probable and estimable, in some cases there may be insufficient time to establish a reserve prior to the actual incurrence of the loss (upon verdict and judgment at trial, for example, or in the case of a quickly negotiated settlement). The Company believes the resolution of routine matters and other incidental claims, taking into account reserves and insurance, will not have a material adverse effect on its business, financial condition or results from operations.

#### **ITEM 1A. RISK FACTORS**

There have been no material changes to the risk factors previously disclosed in Part I, Item 1A, of our Annual Report on Form 10-K for the year ended March 31, 2007, which is incorporated herein by reference.

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

There were no purchases of shares of the Company's common stock during the quarter ended September 30, 2007, by or on behalf of the Company or any "affiliated purchaser," as defined by Rule 10b-18(a)(3) of the Exchange Act.

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

The Company's 2007 Annual Meeting of Stockholders was held on July 31, 2007 (the "Annual Meeting"). Proxies for the Annual Meeting were solicited in accordance with Regulation 14 of the Exchange Act to elect directors to serve until the 2008 Annual Meeting of Stockholders or until their earlier removal or resignation and to ratify the appointment of PricewaterhouseCoopers LLP as the independent registered public accounting firm for the fiscal year ending March 31, 2008. The following nominees were elected to the Company's Board of Directors to serve until the 2008 Annual Meeting of Stockholders or until their respective successors have been elected and qualified, or until their earlier death, resignation or retirement. The voting information for each elected nominee

is set forth below:

|                    | <b>For</b> | <b>Withheld</b> |
|--------------------|------------|-----------------|
| Mark Pettie        | 47,678,543 | 428,426         |
| L. Dick Buell      | 47,813,986 | 292,983         |
| John E. Byom       | 47,723,268 | 383,701         |
| Gary E. Costley    | 47,783,333 | 323,636         |
| David A. Donnini   | 26,036,225 | 22,070,744      |
| Ronald Gordon      | 47,659,068 | 447,901         |
| Vincent J. Hemmer  | 47,609,448 | 497,521         |
| Patrick Lonergan   | 47,723,173 | 383,796         |
| Peter C. Mann      | 47,609,948 | 497,021         |
| Raymond P. Silcock | 47,701,121 | 405,848         |

The votes for the ratification of the appointment of PricewaterhouseCoopers LLP as the Company's independent registered public accounting firm for the audit of the Company's financial statements for the fiscal year ending March 31, 2008 were as follows:

| <b>For</b> | <b>Against</b> | <b>Withheld</b> |
|------------|----------------|-----------------|
| 47,598,174 | 506,149        | 2,646           |

## **ITEM 6. EXHIBITS**

See Exhibit Index immediately following signature page.



**SIGNATURES**

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

**Prestige Brands Holdings, Inc.**  
Registrant

Date: November 8, 2007

By: **/s/ PETER J. ANDERSON**  
Peter J. Anderson  
Chief Financial Officer  
(Principal Financial  
Officer and  
Duly Authorized Officer)

**Exhibit Index**

- 31.1 Certification of Principal Executive Officer of Prestige Brands Holdings, Inc. pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934.
- 31.2 Certification of Principal Financial Officer of Prestige Brands Holdings, Inc. pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934.
- 32.1 Certification of Principal Executive Officer of Prestige Brands Holdings, Inc. pursuant to Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code.
- 32.2 Certification of Principal Financial Officer of Prestige Brands Holdings, Inc. pursuant to Rule 13a-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code.