CENTRAL GARDEN & PET CO
Form 10-Q
February 04, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended December 26, 2015

or

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

For the transition period from ______ to ______

Commission File Number: 001-33268

CENTRAL GARDEN & PET COMPANY

Delaware	**68-0275553**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

1340 Treat Blvd., Suite 600, Walnut Creek, California 94597

(Address of principal executive offices)

(925) 948-4000

(Registrant s telephone number, including area code)

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). x Yes ¨ No

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

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨	Smaller reporting company	¨

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

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

Common Stock Outstanding as of January 29, 2016	11,908,317
Class A Common Stock Outstanding as of January 29, 2016	36,592,397
Class B Stock Outstanding as of January 29, 2016	1,652,262

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PART I. FINANCIAL INFORMATION

PART II. OTHER INFORMATION

Safe Harbor Statement under the Private Securities Litigation Reform Act of 1995

This Form 10-Q includes forward-looking statements. Forward-looking statements include statements concerning our plans, objectives, goals, strategies, future events, future revenues or performance, projected cost savings, capital expenditures, financing needs, plans or intentions relating to acquisitions, our competitive strengths and weaknesses, our business strategy and the trends we anticipate in the industries in which we operate and other information that is not historical information. When used in this Form 10-Q, the words estimates, expects, anticipates, projects, plans intends, believes and variations of such words or similar expressions are intended to identify forward-looking statements. All forward-looking statements, including, without limitation, our examination of historical operating trends, are based upon our current expectations and various assumptions. Our expectations, beliefs and projections are expressed in good faith, and we believe there is a reasonable basis for them, but we cannot assure you that our expectations, beliefs and projections will be realized.

There are a number of risks and uncertainties that could cause our actual results to differ materially from the forward-looking statements contained in this Form 10-Q. Important factors that could cause our actual results to differ materially from the forward-looking statements we make in this Form 10-Q are set forth in the Form 10-K for the fiscal year ended September 26, 2015, including the factors described in the section entitled Item 1A Risk Factors. If any of these risks or uncertainties materializes, or if any of our underlying assumptions are incorrect, our actual results may differ significantly from the results that we express in, or imply by, any of our forward-looking statements. We do not undertake any obligation to revise these forward-looking statements to reflect future events or circumstances, except as required by law. Presently known risk factors include, but are not limited to, the following factors:

- seasonality and fluctuations in our operating results and cash flow;
- fluctuations in market prices for seeds and grains and other raw materials;
- our inability to pass through cost increases in a timely manner;
- the impending retirement of our CEO, dependence upon him and our other key executives and the ability to execute on our succession plan;

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risks associated with new product introductions, including the risk that our new products will not produce sufficient sales to recoup our investment;

declines in consumer spending during economic downturns;

inflation, deflation and other adverse macro-economic conditions;

supply shortages in small animals and pet birds;

adverse weather conditions;

risks associated with our acquisition strategy;

fluctuations in energy prices, fuel and related petrochemical costs;

access to and cost of additional capital;

dependence on a small number of customers for a significant portion of our business;

consolidation trends in the retail industry;

competition in our industries;

potential goodwill or intangible asset impairment;

continuing implementation of an enterprise resource planning information technology system;

our ability to protect our intellectual property rights;

potential environmental liabilities;

risk associated with international sourcing;

litigation and product liability claims;

regulatory issues;

the impact of product recalls;

potential costs and risks associated with actual or anticipated cyber attacks;

the voting power associated with our Class B stock; and

potential dilution from issuance of authorized shares.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

CENTRAL GARDEN & PET COMPANY

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share amounts)

(Unaudited)

	December 26, 2015	December 27, 2014	September 26, 2015
ASSETS			
Current assets:			
Cash and cash equivalents	$ 9,006	$ 79,588	$ 47,584
Restricted cash	11,939	19,690	13,157
Short term investments	0	9,992	0
Accounts receivable (less allowance for doubtful accounts of $21,213, $24,184 and $19,296)	195,357	142,877	207,402
Inventories	416,458	399,936	335,946
Prepaid expenses and other	59,873	64,280	49,731
Total current assets	692,633	716,363	653,820
Land, buildings, improvements and equipment net	163,948	163,546	162,809
Goodwill	209,089	208,233	209,089
Other intangible assets net	74,552	87,061	75,460
Other assets	70,987	9,104	30,419
Total	$ 1,211,209	$ 1,184,307	$ 1,131,597
LIABILITIES AND EQUITY			
Current liabilities:			
Accounts payable	$ 129,091	$ 128,485	$ 88,889
Accrued expenses	89,047	93,208	87,724
Current portion of long-term debt	292	50,289	291
Total current liabilities	218,430	271,982	176,904
Long-term debt	435,893	395,257	396,691
Other long-term obligations	58,005	42,212	51,622
Equity:			
Common stock, $.01 par value: 11,908,317, 12,220,627, and 11,908,317 shares outstanding at December 26, 2015, December 27, 2014 and September 26, 2015	119	122	119

Class A common stock, $.01 par value: 36,591,487, 36,445,726 and 36,462,299 shares outstanding at December 26, 2015, December 27, 2014 and September 26, 2015	366	364	364
Class B stock, $.01 par value: 1,652,262 shares outstanding	16	16	16
Additional paid-in capital	390,583	393,494	388,636
Accumulated earnings	107,385	80,136	115,987
Accumulated other comprehensive income (loss)	(69)	670	164
Total Central Garden & Pet Company shareholders equity	498,400	474,802	505,286
Noncontrolling interest	481	54	1,094
Total equity	498,881	474,856	506,380
Total	$ 1,211,209	$ 1,184,307	$ 1,131,597

See notes to condensed consolidated financial statements.

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CENTRAL GARDEN & PET COMPANY

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share amounts)

(Unaudited)

	Three Months Ended	
	December 26, 2015	**December 27 2014**
Net sales	$ 359,812	$ 307,320
Cost of goods sold and occupancy	260,026	219,339
Gross profit	99,786	87,981
Selling, general and administrative expenses	91,013	86,843
Income from operations	8,773	1,138
Interest expense	(22,145)	(10,503)
Interest income	22	71
Other expense	(473)	(368)
Loss before income taxes and noncontrolling interest	(13,823)	(9,662)
Income tax benefit	(5,200)	(3,969)
Loss including noncontrolling interest	(8,623)	(5,693)
Net income (loss) attributable to noncontrolling interest	(21)	4
Net loss attributable to Central Garden & Pet Company	$ (8,602)	$ (5,697)
Net loss per share attributable to Central Garden & Pet Company:		
Basic	$ (0.18)	$ (0.12)
Diluted	$ (0.18)	$ (0.12)
Weighted average shares used in the computation of net income per share:		
Basic	48,566	49,379
Diluted	48,566	49,379

See notes to condensed consolidated financial statements.

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CENTRAL GARDEN & PET COMPANY

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(in thousands, except per share amounts)

(Unaudited)

	Three Months Ended	
	December 26, 2015	December 27, 2014
Net loss	$ (8,623)	$ (5,693)
Other comprehensive loss:		
Unrealized loss on securities	0	(10)
Foreign currency translation	(233)	(552)
Total comprehensive loss	(8,856)	(6,255)
Comprehensive income (loss) attributable to noncontrolling interest	(21)	4
Comprehensive loss attributable to Central Garden & Pet Company	$ (8,835)	$ (6,259)

See notes to condensed consolidated financial statements.

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CENTRAL GARDEN & PET COMPANY

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(Unaudited)

	Three Months Ended December 26, 2015	Three Months Ended December 27, 2014
Cash flows from operating activities:		
Net loss	$ (8,623)	$ (5,693)
Adjustments to reconcile net loss to net cash (used) provided by operating activities:		
Depreciation and amortization	9,032	8,464
Amortization of deferred financing costs	417	524
Stock-based compensation	2,218	1,592
Excess tax benefits from stock-based awards	(900)	(40)
Deferred income taxes	3,997	2,500
Write-off of deferred financing costs	3,337	0
Loss (Gain) on sale of property and equipment	(14)	44
Change in assets and liabilities (excluding businesses acquired):		
Accounts receivable	33,736	50,650
Inventories	(61,101)	(73,868)
Prepaid expenses and other assets	(6,921)	(15,622)
Accounts payable	23,404	40,090
Accrued expenses	622	7,124
Other long-term obligations	315	87
Net cash (used) provided by operating activities	(481)	15,852
Cash flows from investing activities:		
Additions to property and equipment	(5,256)	(4,069)
Payments to acquire companies, net of cash acquired	(68,529)	0
Change in restricted cash	1,218	(5,407)
Investment in short-term investments	(0)	(12)
Other investing activities	(200)	0
Net cash used in investing activities	(72,767)	(9,488)
Cash flows from financing activities:		
Repayments of long-term debt	(400,072)	(72)
Proceeds from issuance of long-term debt	400,000	0
Borrowings under revolving line of credit	79,000	0
Repayments under revolving line of credit	(37,000)	(0)

Proceeds from issuance of common stock	0	188
Repurchase of common stock, including shares surrendered for tax withholding	(1,167)	(3,742)
Distribution to noncontrolling interest	(592)	(1,680)
Payment of financing costs	(6,324)	0
Excess tax benefits from stock-based awards	900	40
Net cash provided (used) by financing activities	34,745	(5,266)
Effect of exchange rate changes on cash and cash equivalents	(75)	(186)
Net increase (decrease) in cash and cash equivalents	(38,578)	912
Cash and equivalents at beginning of period	47,584	78,676
Cash and equivalents at end of period	$ 9,006	$ 79,588
Supplemental information:		
Cash paid for interest	$ 17,844	$ 848

See notes to condensed consolidated financial statements.

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CENTRAL GARDEN & PET COMPANY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Three Months Ended December 26, 2015

(Unaudited)

1. Basis of Presentation

The condensed consolidated balance sheets of Central Garden & Pet Company and subsidiaries (the Company or Central) as of December 26, 2015 and December 27, 2014, the condensed consolidated statements of operations for the three months ended December 26, 2015 and December 27, 2014, the condensed consolidated statements of comprehensive income for the three months ended December 26, 2015 and December 27, 2014 and the condensed consolidated statements of cash flows for the three months ended December 26, 2015 and December 27, 2014 have been prepared by the Company, without audit. In the opinion of management, the interim financial statements include all normal recurring adjustments necessary for a fair statement of the results for the interim periods presented.

For the Company s foreign business in the UK, the local currency is the functional currency. Assets and liabilities are translated using the exchange rate in effect at the balance sheet date. Income and expenses are translated at the average exchange rate for the period. Deferred taxes are not provided on translation gains and losses because the Company expects earnings of its foreign subsidiary to be permanently reinvested. Transaction gains and losses are included in results of operations. See Note 8, Supplemental Equity Information, for further detail.

Due to the seasonal nature of the Company s garden business, the results of operations for the three month periods ended December 26, 2015 are not indicative of the operating results that may be expected for the entire fiscal year. These interim financial statements should be read in conjunction with the annual audited financial statements, accounting policies and financial notes thereto, included in the Company s 2015 Annual Report on Form 10-K, which has previously been filed with the Securities and Exchange Commission. The September 26, 2015 balance sheet presented herein was derived from the audited financial statements.

Noncontrolling Interest

Noncontrolling interest in the Company s condensed consolidated financial statements represents the 20% interest not owned by Central in a consolidated subsidiary. Since the Company controls this subsidiary, its financial statements are consolidated with those of the Company, and the noncontrolling owner s 20% share of the subsidiary s net assets and results of operations is deducted and reported as noncontrolling interest on the consolidated balance sheets and as net income (loss) attributable to noncontrolling interest in the consolidated statements of operations. See Note 8, Supplemental Equity Information, for additional information.

Derivative Instruments

The Company principally uses a combination of purchase orders and various short and long-term supply arrangements in connection with the purchase of raw materials, including certain commodities. The Company may also enter into commodity futures, options and swap contracts to reduce the volatility of price fluctuations of corn, which impacts the cost of raw materials. The Company s primary objective when entering into these derivative contracts is to achieve greater certainty with regard to the future price of commodities purchased for use in its supply chain. These derivative contracts are entered into for periods consistent with the related underlying exposures and do not constitute positions independent of those exposures. The Company does not enter into derivative contracts for speculative purposes and does not use leveraged instruments.

The Company does not perform the assessments required to achieve hedge accounting for commodity derivative positions. Accordingly, the changes in the values of these derivatives are recorded currently in other income (expense) in its condensed consolidated statements of operations. As of December 26, 2015 and December 27, 2014, the Company had no outstanding derivative instruments.

Recent Accounting Pronouncements

Accounting Pronouncements Recently Adopted

Discontinued Operations

In April 2014, the FASB issued Accounting Standards Update No. 2014-08 (ASU 2014-08), *Presentation of Financial Statements (Topic 205) and Property, Plant and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*. ASU 2014-08 provides amended guidance for reporting discontinued operations and disclosures of disposals of components. The amended guidance raises the threshold for disposals to qualify as discontinued operations and permits significant continuing involvement and continuing cash flows with the discontinued operation. In addition, the amended guidance requires additional disclosures for discontinued operations and new disclosures for individually material disposal transactions that do not meet the definition of a discontinued operation. The amended guidance is effective for annual periods and interim periods within those annual periods beginning after December 15, 2014 and became effective for the Company September 27, 2015. The adoption of the applicable sections of this ASC will have an impact on the presentation of any future discontinued operations the Company may have.

Debt Issuance Costs

In April 2015, the FASB issued ASU No. 2015-03(ASU 2015-03*), Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs.* This standard amends the existing guidance to require that debt issuance costs be presented in the balance sheet as a deduction from the carrying amount of the related debt liability instead of as a deferred charge. In August 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2015-15, *Interest Imputation of Interest (Subtopic 835-30).* This ASU provides additional guidance on ASU 2015-03 with respect to line of credit arrangements, whereby specify debt issuance costs as part of line-of-credit arrangements may continue to be deferred and presented as an asset on the balance sheet. Recognition and measurement guidance for debt issuance costs are not affected. The Company adopted the guidance in ASU s 2015-03 and 2015-15 as of September 27, 2015. See Change in Accounting Principle below.

Business Combinations

In September 2015, the FASB issued ASU No. 2015-16 (ASU 2015-16), *Simplifying the Accounting for Measurement-Period Adjustments*. ASU 2015-16 requires that an acquirer recognize adjustments to provisional amounts that are identified during the measurement period after an acquisition within the reporting period they are determined. This is a change from the previous requirement that the adjustments be recorded retrospectively. The ASU also requires disclosure of the effect on earnings of changes in depreciation, amortization or other income effects, if any, as a result of the adjustment to the provisional amounts, calculated as if the accounting had been completed at the acquisition date. ASU 2015-16 is effective for annual reporting periods (including interim reporting periods within those periods) beginning after December 15, 2015; early adoption is permitted. The Company has early adopted the guidance prospectively as of September 27, 2015. The adoption of this standard will impact the Company s presentation of measurement period adjustments for any future business combinations.

Accounting Standards Not Yet Adopted

Revenue Recognition

In May 2014, the FASB issued Accounting Standards Update No. 2014-09 (ASU 2014-09), *Revenue from Contracts with Customers*. This update was issued as Accounting Standards Codification Topic 606. The core principle of this amendment is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. On July 9, 2015, the FASB deferred the effective date of ASU 2014-09 for one year. ASU 2014-09 is now effective for the Company in the first quarter of its fiscal year ending September 28, 2019. Early adoption is not permitted before the original effective date. The guidance permits two implementation approaches, one requiring retrospective application of the new standard with restatement of prior years and one requiring prospective application of the new standard with disclosure of results under old standards. The Company is currently evaluating the impact that the adoption of this standard will have on its consolidated financial statements.

Stock Based Compensation

In June 2014, the FASB issued ASU No. 2014-12 (ASU 2014-12), *Compensation - Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period.* ASU 2014-12 requires that a performance target that affects vesting and that could be achieved after the requisite service period should be treated as a performance condition. A reporting entity should apply existing guidance in Topic 718 as it relates to awards with performance conditions that affect vesting to account for such awards. As such, the performance target should not be reflected in estimating the grant-date fair value of the award. ASU 2014-12 is effective for annual periods and interim periods within those annual periods beginning after December 15, 2015, or the Company s first quarter of fiscal 2017. Earlier adoption is permitted. The Company is currently evaluating the impact that the adoption of this standard will have on its consolidated financial statements.

Consolidation

In February 2015, the FASB issued ASU 2015-02 (ASU 2015-02), *Amendments to the Consolidation Analysis to ASC Topic 810, Consolidation*. ASU 2015-02 modifies the evaluation of whether limited partnerships and similar legal entities are VIEs or voting interest entities, eliminates the presumption that a general partner should consolidate a limited partnership and affects the consolidation analysis of reporting entities that are involved with VIEs, particularly those that have fee arrangements and related party relationships. ASU 2015-02 is effective for fiscal years that begin after December 15, 2015, or the Company s first quarter of fiscal 2017. The Company is currently evaluating the impact the adoption of ASU 2015-02 will have on its consolidated financial statements.

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Cloud Computing Costs

In April 2015, the FASB issued ASU No. 2015-05(ASU 2015-05), *Intangibles Goodwill and Other Internal-Use Software (Subtopic 350-40): Customer s Accounting for Fees Paid in a Cloud Computing Arrangement*. This standard clarifies the circumstances under which a cloud computing customer would account for the arrangement as a license of internal-use software under ASC 350-40. ASU 2015-05 is effective for public entities for annual and interim periods therein beginning after December 15, 2015, or the Company s first quarter of fiscal 2017. Early adoption is permitted. Entities may adopt the guidance either retrospectively or prospectively to arrangements entered into, or materially modified after the effective date. The Company is currently evaluating the impact the adoption of ASU 2015-05 will have on its consolidated financial statements.

Inventory Measurement

In July 2015, the FASB issued ASU 2015-11 (ASU 2015-11), *Simplifying the Measurement of Inventory*. Under ASU 2015-11, inventory will be measured at the lower of cost and net realizable value and options that currently exist for market value will be eliminated. The standard defines net realizable value as the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. No other changes were made to the current guidance on inventory measurement. ASU 2015-11 is effective for interim and annual periods beginning after December 15, 2016, or the Company s first quarter of fiscal 2018. Early application is permitted and should be applied prospectively. The Company is currently evaluating the impact the adoption of ASU 2015-11 will have on its consolidated financial statements.

Balance Sheet Classification of Deferred Taxes.

In November 2015, the FASB issued ASU 2015-17, *Balance Sheet Classification of Deferred Taxes*. This ASU eliminates the current requirement for entities to present deferred tax liabilities and assets as current and noncurrent in a classified statement of financial position and instead requires that deferred income tax liabilities and assets be classified as noncurrent in a classified statement of financial position. The amendments in this update are effective for financial statements issued for annual periods beginning after December 15, 2016, and interim periods within those annual periods. Earlier application is permitted as of the beginning of an interim or annual reporting period. The Company is currently evaluating the impact the adoption of ASU 2015-17 will have on its consolidated financial statements.

Change in Accounting Principle

Prior to its early adoption of ASU 2015-03, the Company recorded issuance costs associated with its long term debt as a long-term asset on its consolidated balance sheet. The guidance in ASU 2015-03 requires the Company to present debt issuance costs in the consolidated balance sheet as a direct deduction from the carrying amount of the related debt liability. Changes in accounting principles are to be reported through retrospective application of the new principle to all prior financial statement periods presented. Accordingly, the condensed consolidated balance sheets have been adjusted to reflect the effects of reclassifying debt issuance costs from long-term assets to a direct deduction from the carrying amount of the related debt liability as follows.

Financial Statement Line Item	Previously Reported September 26, 2015	Reclassifications	As Adjusted September 26, 2015
Other assets	$ 33,576	$ (3,157)	$ 30,419

Total assets	1,134,754	(3,157)	1,131,597
Long term debt	399,848	(3,157)	396,691
Total liabilities and equity	1,134,754	(3,157)	1,131,597

Financial Statement Line Item	**Previously Reported December 27, 2014**	**Reclassifications**	**As Adjusted December 27, 2014**
Other assets	$ 13,760	$ (4,656)	$ 9,104
Total assets	1,188,963	(4,656)	1,184,307
Long term debt	399,913	(4,656)	395,257
Total liabilities and equity	1,188,963	(4,656)	1,184,307

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2. Fair Value Measurements

ASC 820 establishes a single authoritative definition of fair value, a framework for measuring fair value and expands disclosure of fair value measurements. ASC 820 requires financial assets and liabilities to be categorized based on the inputs used to calculate their fair values as follows:

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

Level 2 - Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 - Unobservable inputs for the asset or liability, which reflect the Company s own assumptions about the assumptions that market participants would use in pricing the asset or liability (including assumptions about risk).

The Company s financial instruments include cash and equivalents, short term investments consisting of bank certificates of deposit, accounts receivable and payable, derivative instruments, short-term borrowings, and accrued liabilities. The carrying amount of these instruments approximates fair value because of their short-term nature.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following table presents the Company s financial assets and liabilities measured at fair value on a recurring basis based upon the level within the fair value hierarchy in which the fair value measurements fall, as of December 26, 2015 (in thousands):

	Level 1	Level 2	Level 3	Total
Liabilities:				
Liability for contingent consideration [b]	$ 0	$ 0	$ 5,625	$ 5,625
Total liabilities	$ 0	$ 0	$ 5,625	$ 5,625

The following table presents the Company s financial assets and liabilities measured at fair value on a recurring basis based upon the level within the fair value hierarchy in which the fair value measurements fall, as of December 27, 2014 (in thousands):

	Level 1	Level 2	Level 3	Total
Assets:				
Short term investments [a]	$ 9,992	$ 0	$ 0	$ 9,992
Total assets	$ 9,992	$ 0	$ 0	$ 9,992
Liabilities:				
Liability for contingent consideration [b]	$ 0	$ 0	$ 4,414	$ 4,414
Total liabilities	$ 0	$ 0	$ 4,414	$ 4,414

The following table presents our financial assets and liabilities at fair value on a recurring basis based upon the level within the fair value hierarchy in which the fair value measurements fall, as of September 26, 2015:

	Level 1	Level 2	Level 3	Total
Liabilities:				
Liability for contingent consideration (b)	$ 0	$ 0	$ 3,625	$ 3,625
Total liabilities	$ 0	$ 0	$ 3,625	$ 3,625

(a) The fair value of short-term investments is based on quoted prices in active markets for identical assets.

(b) The liability for contingent consideration relates to an earn-out for B2E, acquired in December 2012 and future performance-based contingent payments for Hydro-Organics Wholesale, Inc., acquired in October 2015. The fair value of the estimated contingent consideration arrangement is determined based on the Company s evaluation as to the probability and amount of any earn-out that will be achieved based on expected future performance by the acquired entity. This is presented as part of long-term liabilities in our consolidated balance sheets.

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The following table provides a summary of changes in fair value of our Level 3 financial instruments for the periods ended December 26, 2015 and December 27, 2014 (in thousands):

	Amount
Balance as of September 26, 2015	$ 3,625
Estimated contingent performance-based consideration established at the time of acquisition	2,000
Changes in the fair value of contingent performance-based payments established at the time of acquisition	0
Balance as of December 26, 2015	$ 5,625

	Amount
Balance as of September 27, 2014	$ 4,414
Changes in the fair value of contingent performance-based payments established at the time of acquisition	0
Balance as of December 27, 2014	$ 4,414

Assets and Liabilities Measured at Fair Value on a Non-Recurring Basis

The Company measures certain non-financial assets and liabilities, including long-lived assets, goodwill and intangible assets, at fair value on a non-recurring basis. Fair value measurements of non-financial assets and non-financial liabilities are used primarily in the impairment analyses of long-lived assets, goodwill and other intangible assets. During the periods ended December 26, 2015 and December 27, 2014, the Company was not required to measure any significant non-financial assets and liabilities at fair value.

Fair Value of Other Financial Instruments

In November 2015, the Company issued $400 million aggregate principal amount of 6.125% senior notes due November 2023 (the 2023 Notes). The estimated fair value of the Company s 2023 Notes as of December 26, 2015 was $404.0 million, compared to a carrying value of $393.8 million.

In January 2015, the Company called $50 million aggregate principal amount of the Company s senior subordinated notes due 2018 (the 2018 Notes) for redemption on March 1, 2015 at a price of 102.063%. In December 2015, the Company redeemed the remaining $400 million aggregate principal amount of the 2018 Notes at a price of 102.063%. The estimated fair value of the Company s $450 million principal amount of 2018 Notes as of December 27, 2014 was $461.9 million, compared to a carrying value of $444.9 million. The estimated fair value of the Company s $400 million aggregate principal amount of 2018 Notes as of September 26, 2015 was $410.5 million, compared to a carrying value of $396.5 million. The estimated fair value is based on quoted market prices for these notes, which are Level 1 inputs within the fair value hierarchy.

3. Acquisitions

IMS Trading Corp

On July 31, 2015, the Company purchased substantially all of the assets of IMS Trading Corp. for a purchase price of approximately $23 million. IMS Trading Corp was a manufacturer, importer and distributor of rawhide, natural dog treats and pet products throughout the United States and internationally. The purchase price exceeded the fair value of the net tangible assets acquired by approximately $4.9 million, which is included in other assets in our consolidated balance sheet as of December 26, 2015, as the Company has not yet finalized the allocation of the purchase price to the fair value of the intangible assets acquired. This acquisition is expected to complement the Company s existing dog and cat business.

Hydro-Organics Wholesale Inc.

On October 1, 2015, the Company purchased Hydro-Organics Wholesale, Inc., an organic fertilizer business, for a purchase price of approximately $7.8 million cash and approximately $2.0 million of estimated contingent future performance-based payments. The purchase price exceeded the estimated fair value of the tangible net assets acquired by approximately $6.0 million and is included in other assets in the Company s condensed consolidated balance sheet as of December 26, 2015, as the Company has not yet finalized the allocation of the purchase price to the fair value of the intangible assets acquired. This acquisition is expected to complement the Company s existing garden fertilizer category.

DMC

On December 1, 2015, the Company purchased the pet bedding business and certain other assets of National Consumers Outdoors Corp., formerly known as Dallas Manufacturing Company (DMC), for a cash purchase price of approximately $61 million. The purchase price exceeded the estimated fair value of the tangible net assets acquired by approximately $34.0 million and is included in other assets in the Company s condensed consolidated balance sheet as of December 26, 2015, as the Company has not yet finalized the allocation of the purchase price to the fair value of the intangible assets acquired. This acquisition is expected to complement the Company s existing dog and cat business.

4. Inventories, net

Inventories, net of allowance for obsolescence, consist of the following (in thousands):

	December 26, 2015	December 27, 2014	September 26, 2015
Raw materials	$ 118,827	$ 111,012	$ 94,969
Work in progress	15,086	13,006	15,268
Finished goods	271,134	260,314	215,673
Supplies	11,411	15,604	10,036
Total inventories, net	$ 416,458	$ 399,936	$ 335,946

5. Goodwill

The Company accounts for goodwill in accordance with ASC 350, Intangibles Goodwill and Other, and tests goodwill for impairment annually, or whenever events occur or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. This assessment involves the use of significant accounting judgments and estimates as to future operating results and discount rates. Changes in estimates or use of different assumptions could produce significantly different results. An impairment loss is generally recognized when the carrying amount of the reporting unit s net assets exceeds the estimated fair value of the reporting unit. The Company uses discounted cash flow analysis to estimate the fair value of our reporting units. The Company s goodwill impairment analysis also includes a comparison of the aggregate estimated fair value of its reporting units to the Company s total market capitalization.

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6. Other Intangible Assets

The following table summarizes the components of gross and net acquired intangible assets:

	Gross	Accumulated Amortization (in millions)	Accumulated Impairment	Net Carrying Value
December 26, 2015				
Marketing-related intangible assets amortizable	$ 14.1	$ (10.7)	$ 0	$ 3.4
Marketing-related intangible assets nonamortizable	59.6	0	(24.2)	35.4
Total	73.7	(10.7)	(24.2)	38.8
Customer-related intangible assets amortizable	43.3	(22.8)	0	20.5
Other acquired intangible assets amortizable	19.3	(10.7)	0	8.6
Other acquired intangible assets nonamortizable	7.8	0	(1.2)	6.6
Total	27.1	(10.7)	(1.2)	15.2
Total other intangible assets	$ 144.1	$ (44.2)	$ (25.4)	$ 74.5

	Gross	Accumulated Amortization (in millions)	Accumulated Impairment	Net Carrying Value
December 27, 2014				
Marketing-related intangible assets amortizable	$ 15.5	$ (10.1)	$ 0	$ 5.4
Marketing-related intangible assets nonamortizable	59.6	0	(16.9)	42.7
Total	75.1	(10.1)	(16.9)	48.1
Customer-related intangible assets amortizable	42.8	(20.7)	0	22.1
Other acquired intangible assets amortizable	19.4	(9.0)	0	10.4
Other acquired intangible assets nonamortizable	7.7	0	(1.2)	6.5
Total	27.1	(9.0)	(1.2)	16.9
Total other intangible assets	$ 145.0	$ (39.8)	$ (18.1)	$ 87.1

Gross

			Accumulated Amortization	Accumulated Impairment	Net Carrying Value
			(in millions)		
September 26, 2015					
Marketing-related intangible assets	amortizable	$ 14.1	$ (10.4)	$ 0	$ 3.7
Marketing-related intangible assets	nonamortizable	59.6	0	(24.2)	35.4
Total		73.7	(10.4)	(24.2)	39.1
Customer-related intangible assets	amortizable	43.3	(22.3)	0	21.0
Other acquired intangible assets	amortizable	19.3	(10.5)	0	8.8
Other acquired intangible assets	nonamortizable	7.8	0	(1.2)	6.6
Total		27.1	(10.5)	(1.2)	15.4
Total other intangible assets		$ 144.1	$ (43.2)	$ (25.4)	$ 75.5

Other acquired intangible assets include contract-based and technology-based intangible assets.

The Company evaluates long-lived assets, including amortizable and indefinite-lived intangible assets, for impairment whenever events or changes in circumstances indicate the carrying value may not be recoverable. The Company evaluates indefinite-lived intangible assets on an annual basis. In fiscal 2015, the Company recognized a non-cash $7.3 million impairment charge to certain indefinite-lived intangible assets as a result of increased competition in the marketplace and declining volume of sales. The fair value of the remaining $15.0 million of indefinite-lived intangible assets that were impaired exceeded their carrying value at September 26, 2015.

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Other factors indicating the carrying value of the Company s amortizable intangible assets may not be recoverable were not present in fiscal 2015 or during the three months ended December 26, 2015, and accordingly, no impairment testing was performed on these assets.

The Company amortizes its acquired intangible assets with definite lives over periods ranging from 1 to 25 years; over weighted average remaining lives of six years for marketing-related intangibles, 14 years for customer-related intangibles and 14 years for other acquired intangibles. Amortization expense for intangibles subject to amortization was approximately $1.0 million and $0.9 million for the three month periods ended December 26, 2015 and December 27, 2014, respectively, and is classified within operating expenses in the condensed consolidated statements of operations. Estimated annual amortization expense related to acquired intangible assets in each of the succeeding five years is estimated to be approximately $4 million per year from fiscal 2016 through fiscal 2020.

7. Long-Term Debt

Long-term debt consists of the following:

	December 26, 2015	December 27, 2014 (in thousands)	September 26, 2015
Senior notes, interest at 6.125%, payable semi-annually, principal due May 2023	$ 400,000	$ 0	$ 0
Senior subordinated notes, interest at 8.25%, payable semi-annually, repaid in December 2015	0	450,000	400,000
Unamortized discount	0	(440)	(309)
Unamortized debt issuance costs	(6,194)	(4,656)	(3,157)
Net carrying value	393,806	444,904	396,534
Asset-based revolving credit facility, interest at LIBOR plus a margin of 1.25% to 1.75% or Base Rate plus a margin of 0.25% to 0.75%, final maturity December 2018	42,000	0	0
Other notes payable	379	642	448
Total	436,185	445,546	396,982
Less current portion	(292)	(50,289)	(291)
Long-term portion	$ 435,893	$ 395,257	$ 396,691

Senior Notes and Redemption of Senior Subordinated Notes

On November 9, 2015, the Company issued $400 million aggregate principal amount of 6.125% senior notes due November 2023. In December 2015, the Company used the net proceeds from the offering, together with available cash, to redeem its $400 million aggregate principal amount of 8.25% senior subordinated notes due March 1, 2018 at a price of 102.063% of the principal amount and to pay fees and expenses related to the offering.

The Company incurred approximately $6.3 million of debt issuance costs in conjunction with these transactions, which included underwriter fees and legal, accounting and rating agency expenses. The debt issuance costs will be amortized over the term of the 2023 Notes.

As a result of the Company s redemption of the 2018 Notes, the Company incurred a call premium payment of $8.3 million, overlapping interest expense for 30 days of approximately $2.7 million and a $3.3 million non-cash charge for the write off of unamortized deferred financing costs and discount related to the 2018 Notes. These amounts are included in interest expense in the condensed consolidated statements of operations.

The 2023 Notes require semiannual interest payments, which commence on May 15, 2016. The 2023 Notes are unconditionally guaranteed on a senior basis by each of the Company s existing and future domestic restricted subsidiaries which are borrowers under or guarantors of Central s senior secured revolving credit facility. The 2023 Notes are unsecured senior obligations and are subordinated to all of the Company s existing and future secured debt, including the Company s Credit Facility, to the extent of the value of the collateral securing such indebtedness.

The Company may redeem some or all of the 2023 Notes at any time, at its option, prior to November 15, 2018 at the principal amount plus a make whole premium. At any time prior to November 15, 2018, the Company may also redeem, at its option, up to 35% of the original aggregate principal amount of the notes with the proceeds of certain equity offerings at a redemption price of 106.125% of the principal amount of the notes. The Company may redeem some or all of the 2023 Notes, at its option, at any time on or after November 15, 2018 for 104.594%, on or after November 15, 2019 for 103.063%, on or after November 15, 2020 for 101.531% and on or after November 15, 2021 for 100%, plus accrued and unpaid interest.

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The holders of the 2023 Notes have the right to require the Company to repurchase all or a portion of the 2023 Notes at a purchase price equal to 101% of the principal amount of the notes repurchased, plus accrued and unpaid interest upon the occurrence of a change of control.

The 2023 Notes contain customary high yield covenants, including covenants limiting debt incurrence and restricted payments, subject to certain baskets and exceptions. The Company was in compliance with all covenants as of December 26, 2015.

Asset Backed Loan Facility

On December 5, 2013, the Company entered into a credit agreement which provides up to a $390 million principal amount senior secured asset-based revolving credit facility, with up to an additional $200 million principal amount available with the consent of the Lenders if the Company exercises the accordion feature set forth therein (collectively, the Credit Facility). The Credit Facility matures on December 5, 2018 and replaced the Company s prior revolving credit facility. The Company may borrow, repay and reborrow amounts under the Credit Facility until its maturity date, at which time all amounts outstanding under the Credit Facility must be repaid in full. As of December 26, 2015, there were borrowings of $42.0 million outstanding and no letters of credit outstanding under the Credit Facility. There were other letters of credit of $6.0 million outstanding as of December 26, 2015.

The Credit Facility is subject to a borrowing base, calculated using a formula based upon eligible receivables and inventory, minus certain reserves and subject to restrictions. As of December 26, 2015, the borrowing availability was $293.0 million and the remaining borrowing availability, after taking into consideration $42.0 million of outstanding borrowings, was $251.0 million. Borrowings under the Credit Facility bear interest at an index based on LIBOR or, at the option of the Company, the Base Rate (defined as the highest of (a) the SunTrust prime rate, (b) the Federal Funds Rate plus 0.5% and (c) one-month LIBOR plus 1.00%), plus, in either case, an applicable margin based on the Company s total outstanding borrowings. Such applicable margin for LIBOR-based borrowings fluctuates between 1.25%-1.75% (and was 1.25% at December 26, 2015) and such applicable margin for Base Rate borrowings fluctuates between 0.25%-0.75% (and was 0.25% at December 26, 2015). As of December 26, 2015, the applicable interest rate related to Base Rate borrowings was 3.75%, and the applicable interest rate related to LIBOR-based borrowings was 1.49%.

The Credit Facility contains customary covenants, including financial covenants which require the Company to maintain a minimum fixed charge coverage ratio of 1.00:1.00 upon reaching certain borrowing levels. The Credit Facility is secured by substantially all assets of the Company. The Company was in compliance with all financial covenants under the Credit Facility during the period ended December 26, 2015.

8. Supplemental Equity Information

The following table provides a summary of the changes in the carrying amounts of equity attributable to controlling interest and noncontrolling interest for the three months ended December 26, 2015 and December 27, 2014:

	Controlling Interest								
(in thousands)	**Common Stock**	**Class A Common Stock**	**Class B Stock**	**Additional Paid In Capital**	**Retained Earnings**	**Accumulated Other Comprehensive**	**Total**	**Noncontrolling Interest**	**Total**

					Income				
Balance September 26, 2015	$ 119	$ 364	$ 16	$ 388,636	$ 115,987	$ 164	$ 505,286	$ 1,094	$ 506,380
Comprehensive loss					(8,602)	(233)	(8,835)	(21)	(8,856)
Amortization of share-based awards				1,625			1,625		1,625
Restricted share activity				(216)			(216)		(216)
Issuance of common stock		2		(360)			(358)		(358)
Tax benefit on stock option exercise, net of tax deficiency				898			898		898
Distribution to Noncontrolling interest								(592)	(592)
Balance December 26, 2015	$ 119	$ 366	$ 16	$ 390,583	$ 107,385	$ (69)	$ 498,400	$ 481	$ 498,881

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	Controlling Interest								
(in thousands)	Common Stock	Class A Common Stock	Class B Stock	Additional Paid In Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total	Noncontrolling Interest	Total
Balance September 27, 2014	$ 124	$ 369	$ 16	$ 396,586	$ 86,396	$ 1,232	$ 484,723	$ 1,730	$ 486,453
Comprehensive loss					(5,697)	(562)	(6,259)	4	(6,255)
Amortization of share-based awards				1,080			1,080		1,080
Restricted share activity		(1)		(144)			(145)		(145)
Issuance of common stock				470			470		470
Repurchase of common stock	(2)	(4)		(4,538)	(563)		(5,107)		(5,107)
Tax benefit on stock option exercise, net of tax deficiency				40			40		40
Distribution to Noncontrolling interest								(1,680)	(1,680)
Balance December 27, 2014	$ 122	$ 364	$ 16	$ 393,494	$ 80,136	$ 670	$ 474,802	$ 54	$ 474,856

9. Stock-Based Compensation

The Company recognized share-based compensation expense of $2.2 million and $1.6 million for the three month periods ended December 26, 2015 and December 27, 2014, respectively, as a component of selling, general and administrative expenses. The tax benefit associated with share-based compensation expense for the three month periods ended December 26, 2015 and December 27, 2014 was $0.8 million and $0.6 million, respectively.

10. Earnings Per Share

The potential effects of stock awards were excluded from the diluted earnings per share calculation for the three month periods ended December 26, 2015 and December 27, 2014 because their inclusion in a net loss period would be anti-dilutive to the earnings per share calculation.

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11. Segment Information

Management has determined that the Company has two operating segments which are also reportable segments based on the level at which the Chief Operating Decision Maker reviews the results of operations to make decisions regarding performance assessment and resource allocation. These operating segments are Pet segment and Garden segment and are presented in the table below (in thousands).

	Three Months Ended	
	December 26, 2015	December 27, 2014
Net sales:		
Pet segment	$ 248,662	$ 199,320
Garden segment	111,150	108,000
Total net sales	$ 359,812	$ 307,320
Income (loss) from operations:		
Pet segment	26,195	20,575
Garden segment	(3,254)	(3,535)
Corporate	(14,168)	(15,902)
Total income from operations	8,773	1,138
Interest expense - net	(22,123)	(10,432)
Other expense	(473)	(368)
Income tax benefit	(5,200)	(3,969)
Loss including noncontrolling interest	(8,623)	(5,693)
Net income (loss) attributable to noncontrolling interest	(21)	4
Net loss attributable to Central Garden & Pet Company	$ (8,602)	$ (5,697)
Depreciation and amortization:		
Pet segment	$ 4,464	3,941
Garden segment	1,685	1,566
Corporate	2,883	2,957
Total depreciation and amortization	$ 9,032	$ 8,464

	December 26, 2015	December 27, 2014	September 26, 2015
Assets:			
Pet segment	$ 540,218	$ 425,528	$ 465,171
Garden segment	342,811	350,835	310,981
Corporate	328,180	407,944	355,445

Total assets	$	1,211,209	$	1,184,307	$	1,131,597
Goodwill (included in corporate assets above):						
Pet segment	$	209,089	$	208,233	$	209,089

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12. Consolidating Condensed Financial Information of Guarantor Subsidiaries

Certain 100% wholly-owned subsidiaries of the Company (as listed below, collectively the Guarantor Subsidiaries) have guaranteed fully and unconditionally, on a joint and several basis, the obligation to pay principal and interest on the Company s 2023 Notes. Certain subsidiaries and operating divisions are not guarantors of the Notes. Those subsidiaries that are guarantors and co-obligors of the Notes are as follows:

Farnam Companies, Inc.

Four Paws Products Ltd.

Gulfstream Home & Garden, Inc.

Kaytee Products, Incorporated

Matson, LLC

New England Pottery, LLC

Pennington Seed, Inc. (including Gro Tec, Inc. and All-Glass Aquarium Co., Inc.)

Pets International, Ltd.

T.F.H. Publications, Inc.

Wellmark International (including B2E Corporation and B2E Biotech LLC)

In lieu of providing separate audited financial statements for the Guarantor Subsidiaries, the Company has included the accompanying consolidating condensed financial statements based on the Company s understanding of the Securities and Exchange Commission s interpretation and application of Rule 3-10 of the Securities and Exchange Commission s Regulation S-X.

CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS
Three Months Ended December 26, 2015
(in thousands)

	Parent	Non-Guarantor Subsidiaries	Guarantor Subsidiaries	Eliminations	Consolidated
Net sales	$ 137,027	$ 15,270	$ 222,164	$ (14,649)	$ 359,812
Cost of goods sold and occupancy	110,259	12,946	150,489	(13,668)	260,026
Gross profit	26,768	2,324	71,675	(981)	99,786
Selling, general and administrative expenses	32,954	3,779	55,261	(981)	91,013
Income (loss) from operations	(6,186)	(1,455)	16,414	0	8,773
Interest expense	(22,508)	(12)	375	0	(22,145)

Interest income	21	1	0	0	22
Other income (expense)	(835)	(66)	428	0	(473)
Income (loss) before taxes and equity in earnings (loss) of affiliates	(29,508)	(1,532)	17,217	0	(13,823)
Income tax expense (benefit)	(11,145)	(497)	6,442	0	(5,200)
Equity in earnings (loss) of affiliates	9,761	0	(762)	(8,999)	0
Net income (loss) including noncontrolling interest	(8,602)	(1,035)	10,013	(8,999)	(8,623)
Net loss attributable to noncontrolling interest	0	(21)	0	0	(21)
Net income (loss) attributable to Central Garden & Pet Company	$ (8,602)	$ (1,014)	$ 10,013	$ (8,999)	$ (8,602)

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CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS
Three Months Ended December 27, 2014
(in thousands)

	Parent	Non-Guarantor Subsidiaries	Guarantor Subsidiaries	Eliminations	Consolidated
Net sales	$ 96,962	$ 17,323	$ 207,125	$ (14,090)	$ 307,320
Cost of goods sold and occupancy	78,779	14,578	139,091	(13,109)	219,339
Gross profit	18,183	2,745	68,034	(981)	87,981
Selling, general and administrative expenses	27,851	3,999	55,974	(981)	86,843
Income (loss) from operations	(9,668)	(1,254)	12,060	0	1,138
Interest expense	(10,487)	(15)	(1)	0	(10,503)
Interest income	70	1	0	0	71
Other expense	(330)	0	(38)	0	(368)
Income (loss) before taxes and equity in earnings (loss) of affiliates	(20,415)	(1,268)	12,021	0	(9,662)
Income tax expense (benefit)	(8,457)	(444)	4,932	0	(3,969)
Equity in earnings (loss) of affiliates	6,261	0	(587)	(5,674)	0
Net income (loss) including noncontrolling interest	(5,697)	(824)	6,502	(5,674)	(5,693)
Net income attributable to noncontrolling interest	0	4	0	0	4
Net income (loss) attributable to Central Garden & Pet Company	$ (5,697)	$ (828)	$ 6,502	$ (5,674)	$ (5,697)

CONSOLIDATING CONDENSED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
Three Months Ended December 26, 2015
(in thousands)

	Parent	Non-Guarantor Subsidiaries	Guarantor Subsidiaries	Eliminations	Consolidated
Net income (loss)	$ (8,602)	$ (1,035)	$ 10,013	$ (8,999)	$ (8,623)
Other comprehensive loss:					
Foreign currency translation	(233)	(142)	(51)	193	(233)
Total comprehensive income (loss)	(8,835)	(1,177)	9,962	(8,806)	(8,856)
Comprehensive loss attributable to noncontrolling interests	0	(21)	0	0	(21)

Comprehensive income (loss) attributable to Central Garden & Pet Company	$ (8,835)	$ (1,156)	$ 9,962	$ (8,806)	$ (8,835)

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CONSOLIDATING CONDENSED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
Three Months Ended December 27, 2014
(in thousands)

	Parent	Non-Guarantor Subsidiaries	Guarantor Subsidiaries	Eliminations	Consolidated
Net income (loss)	$ (5,697)	$ (824)	$ 6,502	$ (5,674)	$ (5,693)
Other comprehensive loss:					
Foreign currency translation	(552)	(345)	(104)	449	(552)
Unrealized loss on securities	(10)	(0)	(0)	(0)	(10)
Total comprehensive income (loss)	(6,259)	(1,169)	6,398	(5,225)	(6,255)
Comprehensive income attributable to noncontrolling interests	0	4	0	0	4