

ECOLAB INC
Form 10-Q
August 01, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2008

OR

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

For the transition period from to

Commission File No. 1-9328

ECOLAB INC.

(Exact name of registrant as specified in its charter)

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Delaware
(State or other jurisdiction of
incorporation or organization)

41-0231510
(I.R.S. Employer
Identification No.)

370 Wabasha Street N., St. Paul, Minnesota 55102

(Address of principal executive offices)(Zip Code)

1-800-232-6522

(Registrant's telephone number, including area code)

(Not Applicable)

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

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

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

Large accelerated filer

Accelerated filer

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

Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of June 30, 2008.

247,266,546 shares of common stock, par value \$1.00 per share.

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements.

ECOLAB INC.

CONSOLIDATED STATEMENT OF INCOME

(millions, except per share)	Second Quarter Ended June 30	
	2008	2007
	(unaudited)	
Net sales	\$ 1,570.0	\$ 1,362.4
Cost of sales	798.8	669.5
Selling, general and administrative expenses	580.0	519.9
Special (gains) and charges	(19.3)	
Operating income	210.5	173.0
Interest expense, net	15.3	13.4
Income before income taxes	195.2	159.6
Provision for income taxes	56.2	49.3
Net income	\$ 139.0	\$ 110.3
Net income per common share		
Basic	\$ 0.56	\$ 0.45
Diluted	\$ 0.55	\$ 0.44
Dividends declared per common share	\$ 0.1300	\$ 0.1150
Weighted-average common shares outstanding		
Basic	247.1	246.0
Diluted	251.4	250.7

The accompanying notes are an integral part of the consolidated financial information.

ECOLAB INC.

CONSOLIDATED STATEMENT OF INCOME

(millions, except per share)	2008	Six Months Ended June 30 (unaudited)	2007
Net sales	\$	3,027.9	\$ 2,616.6
Cost of sales		1,537.1	1,285.2
Selling, general and administrative expenses		1,137.2	1,010.0
Special (gains) and charges		(17.4)	
Operating income		371.0	321.4
Interest expense, net		30.1	25.1
Income before income taxes		340.9	296.3
Provision for income taxes		99.0	96.5
Net income	\$	241.9	\$ 199.8
Net income per common share			
Basic	\$	0.98	\$ 0.81
Diluted	\$	0.96	\$ 0.79
Dividends declared per common share	\$	0.2600	\$ 0.2300
Weighted-average common shares outstanding			
Basic		247.1	247.8
Diluted		251.5	252.6

The accompanying notes are an integral part of the consolidated financial information.

ECOLAB INC.

CONSOLIDATED BALANCE SHEET

(millions)	June 30 2008	December 31 2007
	(unaudited)	
ASSETS		
Current assets		
Cash and cash equivalents	\$ 222.0	\$ 137.4
Accounts receivable (net of allowance of \$43.9 at June 30, 2008 and \$42.7 at December 31, 2007)	1,082.1	974.0
Inventories	499.1	450.8
Deferred income taxes	96.2	89.4
Other current assets	93.1	65.7
Total current assets	1,992.5	1,717.3
Property, plant and equipment, net	1,157.3	1,083.4
Goodwill	1,439.6	1,279.2
Other intangible assets, net	374.8	328.9
Other assets	391.3	314.0
Total assets	\$ 5,355.5	\$ 4,722.8

The accompanying notes are an integral part of the consolidated financial information.

(Continued)

ECOLAB INC.

CONSOLIDATED BALANCE SHEET (Continued)

(millions, except per share)	June 30 2008	December 31 2007 (unaudited)
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Short-term debt	\$ 376.1	\$ 403.5
Accounts payable	399.1	343.7
Compensation and benefits	237.3	280.2
Income taxes	31.2	27.7
Other current liabilities	518.0	463.2
Total current liabilities	1,561.7	1,518.3
Long-term debt	876.0	599.9
Postretirement health care and pension benefits	443.8	418.5
Other liabilities	275.3	250.4
Shareholders' equity (a)		
Common stock	327.4	326.5
Additional paid-in capital	1,055.9	1,015.2
Retained earnings	2,476.1	2,298.4
Accumulated other comprehensive income	126.9	63.1
Treasury stock	(1,787.6)	(1,767.5)
Total shareholders' equity	2,198.7	1,935.7
Total liabilities and shareholders' equity	\$ 5,355.5	\$ 4,722.8

(a) Common stock, 400 million shares authorized, \$1.00 par value per share, 247.3 million shares outstanding at June 30, 2008, 246.8 million shares outstanding at December 31, 2007.

The accompanying notes are an integral part of the consolidated financial information.

ECOLAB INC.

CONSOLIDATED STATEMENT OF CASH FLOWS

(millions)	2008	Six Months Ended June 30 (unaudited)	2007
OPERATING ACTIVITIES			
Net income	\$	241.9	\$ 199.8
Adjustments to reconcile net income to cash provided by operating activities:			
Depreciation and amortization		170.0	142.5
Deferred income taxes		(4.8)	(3.8)
Share-based compensation expense		15.4	17.2
Excess tax benefits from share-based payment arrangements		(4.9)	(8.6)
Gain on sale of plant		(24.5)	
Other, net		6.8	(0.6)
Changes in operating assets and liabilities:			
Accounts receivable		(73.3)	(54.1)
Inventories		(30.8)	(24.1)
Other assets		(38.5)	6.3
Accounts payable		35.2	(3.4)
Other liabilities		18.2	36.1
Cash provided by operating activities	\$	310.7	\$ 307.3

The accompanying notes are an integral part of the consolidated financial information.

(Continued)

ECOLAB INC.

CONSOLIDATED STATEMENT OF CASH FLOWS (Continued)

(millions)	2008	Six Months Ended June 30 (unaudited)	2007
INVESTING ACTIVITIES			
Capital expenditures	\$ (164.5)		\$ (126.0)
Capitalized software expenditures	(35.7)		(23.0)
Property sold	34.5		5.6
Businesses acquired and investments in affiliates, net of cash acquired	(202.5)		(24.7)
Sale of businesses and assets	2.2		1.1
Deposit into indemnification escrow	(21.0)		
Cash used for investing activities	(387.0)		(167.0)
FINANCING ACTIVITIES			
Net issuances (repayment) of notes payable	(32.3)		182.8
Long-term debt borrowings	248.0		
Long-term debt repayments	(2.8)		(392.7)
Reacquired shares	(20.2)		(336.3)
Cash dividends on common stock	(64.2)		(57.6)
Exercise of employee stock options	21.8		42.3
Excess tax benefits from share-based payment arrangements	4.9		8.6
Other, net	(0.8)		
Cash provided by (used for) financing activities	154.4		(552.9)
Effect of exchange rate changes on cash	6.5		0.8
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	84.6		(411.8)
Cash and cash equivalents, beginning of period	137.4		484.0
Cash and cash equivalents, end of period	\$ 222.0		\$ 72.2

The accompanying notes are an integral part of the consolidated financial information.

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Consolidated Financial Information

The unaudited consolidated financial information for the second quarter and six months ended June 30, 2008 and 2007, reflect, in the opinion of management, all adjustments necessary for a fair statement of the financial position, results of operations and cash flows of Ecolab Inc. (the company) for the interim periods presented. The financial results for any interim period are not necessarily indicative of results for the full year. The consolidated balance sheet data as of December 31, 2007 was derived from the audited consolidated financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America. The unaudited consolidated financial information should be read in conjunction with the consolidated financial statements and notes thereto incorporated in the company s Annual Report on Form 10-K for the year ended December 31, 2007.

With respect to the unaudited financial information of the company for the three and six-month periods ended June 30, 2008 and 2007 included in this Form 10-Q, PricewaterhouseCoopers LLP reported that they have applied limited procedures in accordance with professional standards, which do not require an audit, for a review of such information. Therefore, their separate report dated July 24, 2008 appearing herein, states that they did not audit and they do not express an opinion on that unaudited financial information. Accordingly, the degree of reliance on their report on such information should be restricted in light of the limited nature of the review procedures applied. PricewaterhouseCoopers LLP is not subject to the liability provisions of Section 11 of the Securities Act of 1933, as amended (the Act) for their report on the unaudited financial information because that report is not a report or a part of a registration statement prepared or certified by PricewaterhouseCoopers LLP within the meaning of Sections 7 and 11 of the Act.

2. Special Gains and Charges

The company reported a net pre-tax gain in special gains and charges of \$19.3 million and \$17.4 million for the second quarter and six months ended June 30, 2008, respectively. The reported amounts include a gain of \$24.0 million recorded in the second quarter on the previously announced sale of a plant in Denmark and a \$1.7 million additional gain recorded in the first quarter of 2008 related to the sale of a business in the U.K. These gains were partially offset by costs to optimize the company s business structure including the establishment of a European headquarters in Zurich, Switzerland.

For segment reporting purposes, special gains and charges have been included in the company s corporate segment, which is consistent with the company s internal management reporting.

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

3. Share-Based Compensation

Statement of Financial Accounting Standards (SFAS) No. 123 (Revised 2004), *Share-Based Payment*, (SFAS 123R) requires the company to measure compensation expenses for share-based awards at fair value at the date of grant and recognize compensation expense over the service period for awards expected to vest. Total compensation expense related to share-based compensation plans was \$7.7 million (\$4.9 million net of tax benefit) and \$9.6 million (\$6.1 million net of tax benefit) for the second quarters ended June 30, 2008 and 2007, respectively. Total compensation expense related to share-based compensation plans was \$15.4 million (\$9.9 million net of tax benefit) and \$17.2 million (\$10.9 million net of tax benefit) for the six months ended June 30, 2008 and 2007, respectively.

4. Selected Balance Sheet Information

(millions)	June 30 2008	December 31 2007
	(unaudited)	
Inventories		
Finished goods	\$ 267.0	\$ 241.9
Raw materials and parts	249.2	224.9
Excess of FIFO cost over LIFO cost	(17.1)	(16.0)
Total	\$ 499.1	\$ 450.8
Property, plant and equipment, net		
Land	\$ 30.5	\$ 30.7
Buildings and leaseholds	342.9	331.9
Machinery and equipment	718.9	683.7
Merchandising equipment	1,427.9	1,330.1
Capitalized software	148.8	129.0
Construction in progress	136.3	113.0
	2,805.3	2,618.4
Accumulated depreciation	(1,648.0)	(1,535.0)
Total	\$ 1,157.3	\$ 1,083.4
Other intangible assets, gross		
Customer relationships	\$ 312.8	\$ 291.6
Intellectual property	78.8	52.2
Trademarks	115.7	102.5
Other intangibles	56.1	45.8
	563.4	492.1
Accumulated amortization		
Customer relationships	(130.0)	(108.5)
Intellectual property	(21.4)	(20.0)
Trademarks	(29.3)	(29.1)
Other intangibles	(7.9)	(5.6)
Other intangible assets, net	\$ 374.8	\$ 328.9

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

4. Selected Balance Sheet Information (continued)

(millions)	June 30 2008		December 31 2007	
			(unaudited)	
Other assets				
Deferred income taxes	\$	139.7	\$	137.6
Pension		22.4		23.2
Sole supply fees		56.7		56.3
Other		172.5		96.9
Total	\$	391.3	\$	314.0
Other current liabilities				
Discounts and rebates	\$	247.8	\$	223.7
Dividends payable		32.2		32.1
Other		238.0		207.4
Total	\$	518.0	\$	463.2
Other liabilities				
Deferred income taxes	\$	89.1	\$	86.1
Income taxes payable non-current		61.6		57.3
Other		124.6		107.0
Total	\$	275.3	\$	250.4
Accumulated other comprehensive income				
Unrealized loss on financial instruments	\$	(5.0)	\$	(5.4)
Pension and postretirement benefits		(161.9)		(162.7)
Cumulative translation		293.8		231.2
Total	\$	126.9	\$	63.1

5. Interest

(millions)	Second Quarter Ended June 30			Six Months Ended June 30				
	2008	2007		2008	2007			
	(unaudited)			(unaudited)				
Interest expense	\$	17.8	\$	14.3	\$	35.1	\$	29.5
Interest income		(2.5)		(0.9)		(5.0)		(4.4)
Interest expense, net	\$	15.3	\$	13.4	\$	30.1	\$	25.1

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

6. Financial Instruments

In December 2006, the company issued euro 300 million (\$467 million as of June 30, 2008) aggregate principal amount of the company's senior notes in two series: 4.355% Series A Senior Notes due 2013 in the aggregate principal amount of euro 125 million and 4.585% Series B Senior Notes due 2016 in the aggregate principal amount of euro 175 million. The company designated this debt and related accrued interest as a hedge of existing foreign currency exposures related to net investments the company has in certain European subsidiaries. Accordingly, the transaction gains and losses on all euro notes which are designated and are effective as hedges of the company's net investments have been included as a component of the cumulative translation account. Total transaction losses related to the euro notes charged to shareholders' equity were \$6.9 million, net of tax, and \$17.1 million, net of tax, in the second quarter and first six months of 2008, respectively. Total transaction losses related to the euro notes charged to shareholders' equity were \$4.1 million, net of tax, and \$3.7 million, net of tax, in the second quarter and first six months of 2007, respectively.

7. Comprehensive Income

Comprehensive income was as follows:

(millions)	Second Quarter Ended June 30		Six Months Ended June 30	
	2008 (unaudited)	2007	2008 (unaudited)	2007
Net income	\$ 139.0	\$ 110.3	\$ 241.9	\$ 199.8
Foreign currency translation	17.5	29.4	60.4	25.9
Derivative instruments	0.1	(0.8)	0.4	(0.3)
Pension and postretirement benefits	1.5	1.6	3.0	12.3
Comprehensive income	\$ 158.1	\$ 140.5	\$ 305.7	\$ 237.7

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

8. Business Acquisitions and Investments

In December 2007, subsequent to the company's year-end for International operations, the company purchased the Irish dairy hygiene business from Novartis Animal Health Ireland Ltd. The business, which has annual sales of approximately \$3 million, became part of the company's International operations during the first quarter of 2008.

In February 2008, the company acquired Ecovation, Inc., a Rochester, N.Y. area-based provider of renewable energy solutions and effluent management systems primarily for the food and beverage manufacturing industry in the U.S., including dairy, beverage, and meat and poultry producers. 2007 sales were approximately \$50 million. The total purchase price was approximately \$210 million, of which \$21 million remains payable and was placed in escrow for indemnification purposes. Ecovation became part of the company's U.S. Cleaning & Sanitizing operations during the first quarter of 2008.

Acquisitions in 2008 and 2007 are not material to the company's consolidated financial statements; therefore pro forma financial information is not presented. The aggregate purchase price of acquisitions and investments in affiliates has been reduced for any cash or cash equivalents acquired with the acquisitions.

Based upon purchase price allocations and subsequent adjustments thereto, the components of the aggregate purchase prices of the acquisitions and investments in affiliates made were as follows:

(millions)	Second Quarter Ended June 30		Six Months Ended June 30	
	2008 (unaudited)	2007	2008 (unaudited)	2007
Net tangible assets acquired (liabilities assumed)	\$ 5.9	\$ (0.3)	\$ 49.4	\$ (4.5)
Identifiable intangible assets				
Customer relationships	(1.7)	3.8	10.3	7.4
Intellectual property	(1.5)	0.2	26.8	0.3
Trademarks	0.1	0.3	16.0	0.3
Other intangibles			9.6	8.3
Total	(3.1)	4.3	62.7	16.3
Goodwill	0.4	10.1	111.4	12.9
Total aggregate purchase price	3.2	14.1	223.5	24.7
Liability for indemnification			(21.0)	
Net cash paid for acquisitions	\$ 3.2	\$ 14.1	\$ 202.5	\$ 24.7

Note: Amounts in table above include immaterial purchase accounting adjustments to prior period acquisitions.

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

8. Business Acquisitions and Investments (continued)

The changes in the carrying amount of goodwill for each of the company's reportable segments for the quarter and six months ended June 30, 2008 were as follows:

(unaudited) (millions)	Cleaning & Sanitizing	United States Other Services	Total	International	Consolidated
Balance as of December 31, 2007	\$ 318.7	\$ 50.5	\$ 369.2	\$ 910.0	\$ 1,279.2
Goodwill acquired during quarter	111.0		111.0		111.0
Goodwill allocated to business dispositions				(0.4)	(0.4)
Foreign currency translation				32.6	32.6
Balance as of March 31, 2008	429.7	50.5	480.2	942.2	1,422.4
Goodwill acquired during quarter	(0.9)		(0.9)	1.3	0.4
Foreign currency translation				16.8	16.8
Balance as of June 30, 2008	\$ 428.8	\$ 50.5	\$ 479.3	\$ 960.3	\$ 1,439.6

Goodwill acquired in 2008 includes immaterial adjustments to prior period acquisitions.

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

9. Net Income Per Common Share

The computations of the basic and diluted net income per share amounts were as follows:

(millions, except per share)	Second Quarter Ended June 30		Six Months Ended June 30	
	2008 (unaudited)	2007	2008 (unaudited)	2007
Net income	\$ 139.0	\$ 110.3	\$ 241.9	\$ 199.8
Weighted-average common shares outstanding				
Basic	247.1	246.0	247.1	247.8
Effect of diluted stock options and awards	4.3	4.7	4.4	4.8
Diluted	251.4	250.7	251.5	252.6
Net income per common share				
Basic	\$ 0.56	\$ 0.45	\$ 0.98	\$ 0.81
Diluted	\$ 0.55	\$ 0.44	\$ 0.96	\$ 0.79

Stock options to purchase approximately 5.4 million shares for the second quarter and six months ended June 30, 2008 and 2.8 million shares for the second quarter and six months ended June 30, 2007 were non-dilutive and, therefore, were not included in the computation of diluted common shares outstanding.

Restricted stock awards of 91,646 shares and 88,246 shares for the second quarter and six months ended June 30, 2008, respectively, and 39,987 shares and 34,340 shares for the second quarter and six months ended June 30, 2007, respectively, were excluded from the computation of basic weighted-average shares outstanding because such shares were not yet vested at these dates.

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

10. Pension and Postretirement Plans

The components of net periodic pension and postretirement health care benefit costs for the second quarter ended June 30 are as follows:

(unaudited) (millions)	U.S. Pension Benefits (qualified and non-qualified plans)		International Pension Benefits		U.S. Postretirement Health Care Benefits	
	2008	2007	2008	2007	2008	2007
Service cost	\$ 11.2	\$ 10.8	\$ 5.2	\$ 5.2	\$ 0.6	\$ 0.7
Interest cost on benefit obligation	13.0	11.9	6.8	5.5	2.4	2.4
Expected return on plan assets	(17.6)	(16.4)	(4.9)	(3.9)	(0.6)	(0.6)
Amortization of prior service cost (benefit)	0.3	0.5	0.1		(1.6)	(1.6)
Recognition of net actuarial loss	2.2	3.2	0.2	0.7	1.1	1.8
Total expense	\$ 9.1	\$ 10.0	\$ 7.4	\$ 7.5	\$ 1.9	\$ 2.7

The components of net periodic pension and postretirement health care benefit costs for the six months ended June 30 are as follows:

(unaudited) (millions)	U.S. Pension Benefits (qualified and non-qualified plans)		International Pension Benefits		U.S. Postretirement Health Care Benefits	
	2008	2007	2008	2007	2008	2007
Service cost	\$ 22.4	\$ 21.6	\$ 10.1	\$ 10.2	\$ 1.2	\$ 1.4
Interest cost on benefit obligation	26.0	23.8	13.4	10.9	4.8	4.8
Expected return on plan assets	(35.2)	(32.8)	(9.7)	(7.8)	(1.2)	(1.2)
Amortization of prior service cost (benefit)	0.6	1.0	0.1		(3.2)	(3.2)
Recognition of net actuarial loss	4.4	6.4	0.5	1.5	2.2	3.6
Total expense	\$ 18.2	\$ 20.0	\$ 14.4	\$ 14.8	\$ 3.8	\$ 5.4

The company is not required to make any contributions to its U.S. pension plan and postretirement health care benefits plans for 2008 based on plan asset values as of June 30, 2008. Certain international pension benefit plans are required to be funded in accordance with local government

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requirements. The company contributed approximately \$13 million to its international pension benefit plans during the first six months of 2008. The company currently estimates that it will contribute approximately \$13 million to the international pension benefit plans during the remainder of 2008.

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

11. Operating Segments

Financial information for each of the company's reportable segments is as follows:

(millions)	Second Quarter Ended June 30		Six Months Ended June 30	
	2008 (unaudited)	2007	2008 (unaudited)	2007
Net Sales				
United States				
Cleaning & Sanitizing	\$ 663.7	\$ 589.3	\$ 1,317.1	\$ 1,157.5
Other Services	120.9	113.7	231.3	215.8
Total	784.6	703.0	1,548.4	1,373.3
International				
Effect of foreign currency translation	44.7	(42.3)	55.4	(93.2)
Consolidated	\$ 1,570.0	\$ 1,362.4	\$ 3,027.9	\$ 2,616.6
Operating Income				
United States				
Cleaning & Sanitizing	\$ 107.5	\$ 99.8	\$ 213.0	\$ 199.0
Other Services	13.0	11.0	20.0	20.3
Total	120.5	110.8	233.0	219.3
International				
Corporate	9.9	(4.3)	3.1	(6.5)
Effect of foreign currency translation	6.4	(5.9)	7.3	(11.6)
Consolidated	\$ 210.5	\$ 173.0	\$ 371.0	\$ 321.4

The International amounts included above are based on translation into U.S. dollars at the fixed currency exchange rates used by management for 2008.

Consistent with the company's internal management reporting, the corporate segment includes special gains and charges reported on the Consolidated Statement of Income. The corporate segment also includes investments in the development of business systems and other corporate investments the company is making as part of ongoing efforts to improve efficiency and returns.

Total service revenue for the U.S. Other Services segment was \$100.7 million and \$191.1 million for the second quarter and six months ended June 30, 2008, respectively, and \$94.3 million and \$176.7 million for the second quarter and six months ended 2007, respectively. Total service revenue for the International segment at public currency exchange rates was \$48.2 million and \$92.9 million for the second quarter and six months ended June 30, 2008, respectively, and \$45.9 million and \$88.6 million for the second quarter and six months ended June 30, 2007, respectively.

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

12. Goodwill and Other Intangible Assets

Under SFAS 142, goodwill must be tested annually for impairment. The company performs its annual goodwill impairment test during the second quarter. If circumstances change significantly within a reporting unit, the company would also test a reporting unit for impairment prior to the annual test. As of June 30, 2008, the company has completed its annual test for goodwill impairment. Based on this testing, no adjustment to the carrying value of goodwill was necessary.

Goodwill and other intangible assets arise principally from business acquisitions. Goodwill represents the excess of the purchase price over the fair value of identifiable net assets acquired. Other intangible assets include primarily customer relationships, trademarks, patents and other technology. Other intangible assets are amortized on a straight-line basis over their estimated economic lives. The weighted-average useful life of other intangible assets was 13 years as of both June 30, 2008 and 2007.

The straight-line method of amortization reflects an appropriate allocation of the cost of the intangible assets to earnings in proportion to the amount of economic benefits obtained by the company in each reporting period. Total amortization expense related to other intangible assets during the second quarters ended June 30, 2008 and 2007 was \$11.1 million and \$7.1 million, respectively. Total amortization expense related to other intangible assets during the six months ended June 30, 2008 and 2007 was \$25.9 million and \$14.1 million, respectively. As of June 30, 2008, future estimated amortization expense related to amortizable other identifiable intangible assets will be:

(unaudited)		
(millions)		
2008 (Remainder: six-month period)	\$	22
2009		43
2010		43
2011		42
2012		41

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

13. New Accounting Pronouncements

In September 2006, the FASB issued SFAS 157, *Fair Value Measurement* (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurement. Additionally, in February 2008, the FASB announced it will defer for one year the effective date of SFAS 157 for nonfinancial assets and liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis. The FASB also amended SFAS 157 to add a scope exception for leasing transactions subject to SFAS 13 *Accounting for Leases* from its application. The company adopted SFAS 157 effective January 1, 2008 for financial assets and liabilities. The adoption did not have a material impact on the company's consolidated results of operations and financial condition. The company's financial liabilities as of June 30, 2008 include foreign exchange contracts with fair market value of approximately \$2 million, which are valued using foreign currency exchange rates as of the balance sheet date (level 2 - significant other observable inputs). In addition, the company has concluded that it does not have material amounts of assets and liabilities measured using the company's own assumptions of fair market value (level 3 - unobservable inputs).

In February 2007, the FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities - including an amendment of FASB Statement No. 115* (SFAS 159). SFAS 159 provides companies with an option to report selected financial assets and financial liabilities at fair value, which can be elected on an instrument-by-instrument basis. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings at each subsequent reporting date. The company adopted SFAS 159 effective January 1, 2008. The adoption did not have a material impact on the company's consolidated results of operations and financial condition.

In December 2007, the FASB issued SFAS 141 (revised 2007), *Business Combinations* (SFAS 141R). SFAS 141R establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any noncontrolling interest in the acquiree and the goodwill acquired. SFAS 141R also establishes disclosure requirements to enable the evaluation of the nature and financial effects of the business combination. SFAS 141R is effective for fiscal years beginning after December 15, 2008, and will be adopted by the company in the first quarter of 2009. The company is currently evaluating the potential impact of the adoption of SFAS 141R on its consolidated results of operations and financial condition including the impact on future acquisitions.

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

13. New Accounting Pronouncements (continued)

In December 2007, the FASB issued SFAS 160, *Noncontrolling Interests in Consolidated Financial Statements - an amendment of Accounting Research Bulletin No. 51* (SFAS 160). SFAS 160 establishes accounting and reporting standards for ownership interests in subsidiaries held by parties other than the parent, the amount of consolidated net income attributable to the parent and to the noncontrolling interest, changes in a parent's ownership interest, and the valuation of retained noncontrolling equity investments when a subsidiary is deconsolidated. SFA