SUN MICROSYSTEMS, INC.
Form DEF 14A
September 25, 2007
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SCHEDULE 14A INFORMATION

Proxy Statement Pursuant to Section 14(a) of the Securities

Exchange Act of 1934

Filed by the Registrant x

Filed by a Party other than the Registrant ¨

Check the appropriate box:

¨ Preliminary Proxy Statement

¨ Confidential, For Use of the Commission Only (as permitted by Rule 14a-6(e)(2))

x Definitive Proxy Statement

¨ Definitive Additional Materials

¨ Soliciting Material Pursuant to §240.14a-12

Sun Microsystems, Inc.

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

x No fee required.

¨ Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:

(2) Aggregate number of securities to which transaction applies:

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (Set forth the amount on which the filing fee is calculated and state how it was determined):

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¨ Fee paid previously with preliminary materials:

¨ Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

(1) Amount Previously Paid:

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(3) Filing Party:

(4) Date Filed:

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SUN MICROSYSTEMS, INC.

4150 Network Circle

Santa Clara, California 95054

NOTICE OF 2007 ANNUAL MEETING OF STOCKHOLDERS

November 8, 2007

10:00 a.m. Pacific Standard Time

Dear Stockholder:

You are cordially invited to attend Sun s 2007 Annual Meeting of Stockholders, which will be held on Thursday, November 8, 2007 at 10:00 a.m., Pacific Standard Time, at Sun s Auditorium, located at the Santa Clara Campus, 4030 George Sellon Circle, Santa Clara, California 95054, for the following purposes:

1. To elect ten members to the Board of Directors;

2. To ratify the appointment of Ernst & Young LLP as our independent registered public accounting firm for the fiscal year ending June 30, 2008;

3. To approve Sun s 2007 Omnibus Incentive Plan;

4. To approve an amendment to our Amended and Restated Certificate of Incorporation to effect a one-for-four reverse split of our common stock, together with a corresponding reduction in the number of authorized shares of our common stock;

5. To consider two stockholder proposals, if each is properly presented at the meeting; and

6. To transact such other business as may properly come before the meeting or any postponement or adjournment thereof.

The foregoing items of business are more fully described in the Proxy Statement accompanying this notice.

Only stockholders of record at the close of business on September 10, 2007 are entitled to vote at the Annual Meeting or any postponement or adjournment of the meeting. A list of those stockholders will be maintained and open for examination by any of our stockholders, for any purpose germane to the Annual Meeting, during regular business hours at the address listed above for ten days prior to the meeting.

We are pleased to be among the first companies to take advantage of new Securities and Exchange Commission rules that allow issuers to furnish proxy materials to their stockholders on the Internet. We believe the new rules will allow us to provide our stockholders with the information they need, while lowering the costs of delivery and reducing the environmental impact of our Annual Meeting.

As owners of Sun, your vote is important. Whether or not you are able to attend the Annual Meeting in person, it is important that your shares be represented. Please vote as soon as possible.

On behalf of our Board of Directors, thank you for your participation in this important annual process.

Sincerely,

MICHAEL A. DILLON

Executive Vice President, General Counsel and Secretary

Santa Clara, California

September 25, 2007

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SUN MICROSYSTEMS, INC.

PROXY STATEMENT

FOR

2007 ANNUAL MEETING OF STOCKHOLDERS

GENERAL INFORMATION

Why am I receiving these materials?

Our Board of Directors has made these materials available to you on the Internet or, upon your request, has delivered printed versions of these materials to you by mail, in connection with the Board s solicitation of proxies for use at our 2007 Annual Meeting of Stockholders, which will take place on November 8, 2007. Our stockholders are invited to attend the Annual Meeting and are requested to vote on the proposals described in this proxy statement.

What is included in these materials?

These materials include:

- Our proxy statement for the Annual Meeting; and
- Our 2007 Annual Report to Stockholders, which includes our audited consolidated financial statements.

If you requested printed versions of these materials by mail, these materials also include the proxy card for the Annual Meeting.

What items will be voted on at the Annual Meeting?

There are six items that will be voted on at the Annual Meeting:

1. The election of ten members to the Board of Directors;
2. The ratification of the appointment of Ernst & Young LLP as our independent registered public accounting firm for the fiscal year ending June 30, 2008;
3. A proposal regarding the approval of Sun s 2007 Omnibus Incentive Plan;
4. A proposal regarding an amendment to our Amended and Restated Certificate of Incorporation to effect a one-for-four reverse stock split of our common stock, together with a corresponding reduction in the number of authorized shares of our common stock;
5. A stockholder proposal regarding advisory vote on compensation, if properly presented at the meeting; and

6. A stockholder proposal regarding simple majority vote, if properly presented at the meeting.

What are our Board of Directors voting recommendations?

Our Board recommends that you vote your shares FOR each of the nominees to the Board, FOR the ratification of the appointment of Ernst & Young LLP, FOR the approval of our 2007 Omnibus Incentive Plan, FOR the reverse stock split, AGAINST the stockholder proposal regarding an advisory vote on compensation and AGAINST the stockholder proposal regarding a simple majority vote.

Where are Sun s principal executive offices located, and what is Sun s main telephone number?

Sun s principal executive offices are located at 4150 Network Circle, Santa Clara, California 95054. Sun s main telephone number is (650) 960-1300.

Why did I receive a one-page notice in the mail regarding the Internet availability of proxy materials this year instead of a full set of proxy materials?

Pursuant to the new rules recently adopted by the Securities and Exchange Commission, we have elected to provide access to our proxy materials over the Internet. Accordingly, we are sending a Notice of Internet Availability of Proxy Materials (the Notice) to our stockholders of record and beneficial owners. All stockholders will have the ability to access the proxy materials on a website referred to in the Notice or request to receive a printed set of the proxy materials. Instructions on how to access the proxy materials over the Internet or to request a printed copy may be found on the Notice. In addition, stockholders may request to receive proxy materials in printed form by mail or electronically by email on an ongoing basis.

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How can I get electronic access to the proxy materials?

The Notice will provide you with instructions regarding how to:

- View our proxy materials for the Annual Meeting on the Internet; and
- Instruct us to send our future proxy materials to you electronically by email.

Choosing to receive your future proxy materials by email will save us the cost of printing and mailing documents to you and will reduce the impact of our annual stockholders meetings on the environment. If you choose to receive future proxy materials by email, you will receive an email next year with instructions containing a link to those materials and a link to the proxy voting site. Your election to receive proxy materials by email will remain in effect until you terminate it.

Who may vote at the Annual Meeting?

If you owned Sun s common stock at the close of business on September 10, 2007 (the Record Date), then you may attend and vote at the meeting. At the close of business on the Record Date, we had approximately 3,414,725,566 shares of common stock issued and outstanding, of which 3,414,675,566 were entitled to vote.

What is the difference between holding shares as a stockholder of record and as a beneficial owner of shares held in street name?

Stockholder of Record. If your shares are registered directly in your name with our transfer agent, Computershare Trust Company, N.A., you are considered the stockholder of record with respect to those shares, and the Notice was sent directly to you by Sun.

Beneficial Owner of Shares Held in Street Name. If your shares are held in an account at a brokerage firm, bank, broker-dealer, or other similar organization, then you are the beneficial owner of shares held in street name, and the Notice was forwarded to you by that organization. The organization holding your account is considered the stockholder of record for purposes of voting at the Annual Meeting. As a beneficial owner, you have the right to direct that organization on how to vote the shares held in your account.

What is the quorum requirement for the Annual Meeting?

A majority of Sun s outstanding shares on the Record Date must be present at the meeting in order to hold the meeting and conduct business. This is called a quorum. Your shares will be counted for purposes of determining if there is a quorum, whether representing votes for, against, withheld or abstained, or broker non-votes, if you:

- Are present and vote in person at the meeting; or
- Have voted on the Internet, by telephone or by properly submitting a proxy card or voting instruction form by mail.

If I am a stockholder of record of Sun s shares, how do I vote?

If you are a stockholder of record, you may vote in person at the Annual Meeting. We will give you a ballot when you arrive.

If you do not wish to vote in person or if you will not be attending the Annual Meeting, you may vote by proxy. You can vote by proxy over the Internet by following the instructions provided in the Notice, or, if you request printed copies of the proxy materials by mail, you can also vote by mail or by telephone.

If I am a beneficial owner of shares held in street name, how do I vote?

If you are a beneficial owner of shares held in street name and you wish to vote in person at the Annual Meeting, you must obtain a valid proxy from the organization that holds your shares.

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If you do not wish to vote in person or you will not be attending the Annual Meeting, you may vote by proxy. You may vote by proxy over the Internet, or if you request printed copies of the proxy materials by mail, you can also vote by mail or by telephone by following the instructions provided in the Notice.

What happens if I do not give specific voting instructions?

Stockholders of Record. If you are a stockholder of record and you:

Indicate when voting on the Internet or by telephone that you wish to vote as recommended by our Board of Directors; or

If you sign and return a proxy card without giving specific voting instructions,
then the proxy holders will vote your shares in the manner recommended by our Board on all matters presented in this proxy statement and as the proxy holders may determine in their discretion with respect to any other matters properly presented for a vote at the meeting.

Beneficial Owners of Shares Held in Street Name. If you are a beneficial owner of shares held in street name and do not provide the organization that holds your shares with specific voting instructions, under the rules of various national and regional securities exchanges, the organization that holds your shares may generally vote on routine matters but cannot vote on non-routine matters. If the organization that holds your shares does not receive instructions from you on how to vote your shares on a non-routine matter, the organization that holds your shares will inform our Inspector of Election that it does not have the authority to vote on this matter with respect to your shares. This is generally referred to as a broker non-vote. When our Inspector of Election tabulates the votes for any particular matter, broker non-votes will be counted for purposes of determining whether a quorum is present, but will not otherwise be counted. We encourage you to provide voting instructions to the organization that holds your shares by carefully following the instructions provided in the Notice.

Which ballot measures are considered routine or non-routine ?

Proposal 1 (election of directors); Proposal 2 (approval of auditors) and Proposal 4 (approval of reverse stock split) involve matters that we believe will be considered routine.

Proposal 3 (approval of Sun s 2007 Omnibus Incentive Plan) and Proposals 5 and 6 (the stockholder proposals) involve matters that we believe will be considered non-routine.

How are abstentions treated?

Abstentions are counted for purposes of determining whether a quorum is present. For the purpose of determining whether the stockholders have approved a matter, abstentions are not treated as votes cast affirmatively or negatively, and therefore have no effect on the outcome of any matter being voted on at the Annual Meeting.

What is the voting requirement to approve each of the proposals?

The following table sets forth the voting requirement with respect to each of the proposals:

Proposal 1	Election of directors	Each director must be elected by a majority of the votes cast, meaning that the number of shares entitled to vote on the election of directors and represented in person or by proxy at the Annual Meeting casting their vote FOR a director must exceed the number of votes WITHHELD from that director. Please see Corporate Governance Majority Vote Standard and Director Resignation Policy for more information.
Proposal 2	Ratification of appointment of	

independent registered public accounting firm	To be approved by our stockholders, this proposal must receive the affirmative FOR vote of a majority of the votes cast affirmatively or negatively on this proposal at the Annual Meeting.

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Proposal 3 Approval of Sun s 2007 Omnibus Incentive Plan	To be approved by our stockholders, this proposal must receive the affirmative FOR vote of a majority of the votes cast affirmatively or negatively on this proposal at the Annual Meeting.
Proposal 4 Approval of amendment to Sun s Amended and Restated Certificate of Incorporation to effect a one-for-four reverse stock split of our common stock	To be approved by our stockholders, this proposal must receive the affirmative FOR vote of a majority of the outstanding shares of our common stock.
Proposal 5 Stockholder proposal regarding advisory vote on compensation	To be approved by stockholders, this proposal must receive the affirmative FOR vote of a majority of the votes cast affirmatively or negatively on this proposal at the Annual Meeting.
Proposal 6 Stockholder proposal regarding simple majority vote	To be approved by stockholders, this proposal must receive the affirmative FOR vote of a majority of the votes cast affirmatively or negatively on this proposal at the Annual Meeting.

Can I change my vote after I have voted?

You may revoke your proxy and change your vote at any time before the final vote at the meeting. You may vote again on a later date on the Internet or by telephone (only your latest Internet or telephone proxy submitted prior to the meeting will be counted), or by signing and returning a new proxy card with a later date, or by attending the meeting and voting in person. However, your attendance at the Annual Meeting will not automatically revoke your proxy unless you vote again at the meeting or specifically request in writing that your prior proxy be revoked.

Is cumulative voting permitted for the election of directors?

In the election of directors, you may elect to cumulate your votes. If you choose to cumulate your votes, you will need to notify the Secretary of Sun in writing at the address of Sun s principal executive offices prior to the Annual Meeting or notify the chairman of the meeting prior to the commencement of voting at the Annual Meeting of your intent to cumulate your votes. If you hold your shares beneficially in street name and wish to cumulate votes, you should contact the organization that holds your shares prior to the meeting to assist you with this process.

As provided in our Bylaws and Corporate Governance Guidelines, if cumulative voting is invoked, then majority voting will not apply with respect to the election of directors, and the ten director nominees receiving the highest number of votes will be elected. If cumulative voting is invoked, you will have a total number of votes equal to the number of director nominees, multiplied by the number of shares you hold. You may allocate these votes among the director nominees as you see fit. For example, if you hold 1,000 shares of stock, you could allocate 10,000 FOR votes (1,000 times 10 director nominees) among as few or as many of the ten director nominees as you choose.

The proxy holders intend to vote the shares represented by proxies to elect Sun s ten director nominees as set forth in Proposal 1. If cumulative voting is in effect at the Annual Meeting, the proxy holders will vote the shares represented by the proxies in order to elect as many of Sun s ten director nominees as possible or as they otherwise determine in their discretion. Cumulative voting applies only to the election of directors. For all other matters, each share of common stock outstanding as of the close of business on the Record Date is entitled to one vote.

Is my vote confidential?

Proxy instructions, ballots and voting tabulations that identify individual stockholders are handled in a manner that protects your voting privacy. Your vote will not be disclosed either within Sun or to third parties, except:

- As necessary to meet applicable legal requirements;
- To allow for the tabulation and certification of votes; and
- To facilitate a successful proxy solicitation.

Occasionally, stockholders provide written comments on their proxy cards, which may be forwarded to management and our Board of Directors.

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Where can I find the voting results of the Annual Meeting?

The preliminary voting results will be announced at the Annual Meeting. The final voting results will be tallied by the Inspector of Election and published in our quarterly report on Form 10-Q for the fiscal quarter ending on December 31, 2007, which we expect to file with the SEC by February 9, 2008.

Who is paying for the cost of this proxy solicitation?

Sun is paying the costs of the solicitation of proxies. We have engaged Morrow & Co., Inc. as our proxy solicitor to help us solicit proxies from brokers, bank nominees and other institutions for a fee of $30,000.00, plus reasonable out-of-pocket expenses. We must also pay brokerage firms and other persons representing beneficial owners of shares held in street name certain fees associated with:

- Forwarding the Notice to beneficial owners;
- Forwarding printed proxy materials by mail to beneficial owners who specifically request them; and
- Obtaining beneficial owners voting instructions.

In addition to soliciting proxies by mail, our board members, officers and employees may solicit proxies on our behalf, without additional compensation, personally or by telephone, or we may ask our proxy solicitor to solicit proxies on our behalf by telephone for a fee of $5.00 per phone call, plus reasonable expenses. We will also solicit proxies by email from stockholders who are our employees or who previously requested to receive proxy materials electronically.

What is the deadline to propose actions for consideration at the 2008 annual meeting of stockholders or to nominate individuals to serve as directors?

You may submit proposals, including director nominations, for consideration at future annual meetings of stockholders as follows:

Stockholder Proposals. For a stockholder proposal to be considered for inclusion in Sun s proxy statement for our 2008 annual meeting of stockholders, the written proposal must be received by the Secretary of Sun at our principal executive offices no later than May 28, 2008. The proposal will need to comply with Rule 14a-8 of the Securities Exchange Act of 1934 (the Exchange Act), which lists the requirements for the inclusion of stockholder proposals in company-sponsored proxy materials. If you intend to present a proposal at our 2008 annual meeting of stockholders, but you do not intend to have it included in our 2008 proxy statement, your proposal must be delivered to the Secretary of Sun no earlier than June 27, 2008 and no later than July 27, 2008. If the date of our 2008 annual meeting of stockholders is more than 30 calendar days before or after the one-year anniversary of the date of our Annual Meeting, your proposal must be delivered by the close of business on the tenth day following the day we publicly announce the date of the 2008 annual meeting of stockholders.

Nominations of Director Candidates. Stockholders may propose director candidates for consideration by the Board s Corporate Governance and Nominating Committee. Any such recommendations should include the candidate s name, home and business contact information, detailed biographical data, relevant qualifications for Board membership, information regarding any relationships between the candidate and Sun within the last three years and a written indication by the recommended candidate of her or his willingness to serve, and should be directed to the Secretary of Sun at the address of our principal executive offices. In addition, our Bylaws permit stockholders to nominate directors for election at an annual meeting of stockholders. If you want to nominate an individual for election to Sun s Board at the 2008 annual meeting of stockholders, you must deliver a written notice to the Secretary of Sun by no earlier than June 27, 2008 and no later than July 27, 2008. As set forth in our Bylaws, your notice must state: your name, your address and the number of Sun shares you own; the nominee s name, age, business address, principal occupation and the number of Sun shares the nominee owns; and all other information regarding nominees required by Regulation 14A of the Exchange Act.

Bylaw Provisions. The relevant Bylaw provisions regarding the requirements for making stockholder proposals and nominating director candidates are available on our website at *www.sun.com/company/cgov/*. You may also contact the Secretary of Sun at our principal executive offices to request a copy of the relevant Bylaw provisions.

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How can I communicate with the independent directors on Sun s Board?

Our Board encourages stockholders who are interested in communicating directly with our independent directors as a group to do so by writing to the independent directors in care of our Corporate Secretary. Stockholders can send communications electronically by clicking on Contact Board of Directors at our corporate governance website located at *www.sun.com/company/cgov/* or by mail to: Secretary, Sun Microsystems, Inc., 4150 Network Circle, Santa Clara, California 95054. Stockholder correspondence received addressed to our independent directors will be reviewed by our general counsel or his designee, who will regularly forward to our independent directors all correspondence that, in the opinion of our general counsel, deals with the functions of the Board or committees thereof or that our general counsel otherwise determines requires their attention. Our directors may at any time review a log of all correspondence received by Sun that is addressed to the independent members of the Board and request copies of any such correspondence.

ABOUT OUR BOARD AND ITS COMMITTEES

Our Board and its committees meet throughout the year on a set schedule and also hold special meetings and act by written consent from time to time as appropriate. In addition, at the conclusion of each regularly scheduled, in-person Board meeting, Sun s independent directors meet in executive session without employee-directors present.

During fiscal 2007, our Board held nine meetings. Each director attended 75% or more of the aggregate number of meetings of the Board of Directors and meetings of committees on which he or she served during fiscal 2007. We encourage directors to attend our annual meetings of stockholders. All of our directors serving on the Board as of our 2006 annual meeting of stockholders attended that meeting.

Our Board has an Audit Committee, a Leadership Development and Compensation Committee (the LDCC), and a Corporate Governance and Nominating Committee (the CGNC). The CGNC makes recommendations to the Board concerning committee memberships and the appointment of chairpersons for each committee, and the Board appoints the members and chairpersons of the committees. The following table lists the chairpersons and members of each committee as of the Record Date and the number of meetings held by each committee during fiscal 2007:

Director	Audit	LDCC	CGNC
Scott G. McNealy			
James L. Barksdale			Chair
Stephen M. Bennett(1)		Chair	
Peter L.S. Currie(2)	Member		
Robert J. Finocchio, Jr.	Chair		
Michael E. Marks(3)	Member		
Patricia E. Mitchell			Member
M. Kenneth Oshman(4)		Member	
P. Anthony Ridder(5)		Member	
Jonathan I. Schwartz			
Number of Meetings in Fiscal 2007	10	6	4

(1) Mr. Bennett became Chairman of the LDCC on November 2, 2006.

(2) Mr. Currie joined the Board and Audit Committee on November 2, 2006.

(3) Mr. Marks joined the Board on April 25, 2007 and the Audit Committee on August 1, 2007.

(4) Mr. Oshman served on the CGNC until August 1, 2007.

(5) Mr. Ridder joined the Board and the LDCC on November 2, 2006.

***Audit Committee*.** The Audit Committee oversees our accounting and financial reporting processes and audits of our financial statements. Among other matters, the Audit Committee:

Hires, evaluates performance of and replaces Sun s independent registered public accounting firm as appropriate;

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Discusses relationships or issues that could hinder the independence of, and pre-approves the services provided by, Sun s independent registered public accounting firm;

Discusses with management, internal auditors and Sun s independent registered public accounting firm the quality of Sun s accounting principles and financial reporting; and

Oversees the internal auditing functions and controls.

Each member of the Audit Committee meets the NASDAQ requirements as to independence and financial knowledge and is independent as defined in applicable SEC rules. Our Board has determined that Robert J. Finocchio, Jr. and Michael E. Marks qualify as audit committee financial experts, as that term is defined in Item 401(h) of Regulation S-K of the Exchange Act. The Audit Committee operates under a written charter that complies with applicable SEC and NASDAQ requirements, which was amended and restated effective August 27, 2007. The Audit Committee charter is posted on our website at *www.sun.com/company/cgov/bcc.jsp*.

LDCC. The LDCC has overall responsibility for approving and evaluating our compensation plans, policies and programs applicable to executive officers. Among other matters, the LDCC:

Reviews and approves the executive compensation policies, including compensation of the chief executive officer (the CEO);

Administers the employee stock option and stock purchase plans;

Reviews executive and leadership development policies, plans and practices; and

Advises the Board on executive successor planning.

The LDCC has delegated authority to our CEO to grant equity to employees below the level of Vice President. Please see Executive Compensation Compensation Disclosure and Analysis Other Compensation Policies for more information. The members of the LDCC are all independent directors under applicable NASDAQ rules. The LDCC operates under a written charter, a copy of which can be found on our website at *www.sun.com/company/cgov/bcc.jsp.*

CGNC. The purpose of the CGNC is to ensure that the Board is properly constituted to meet its fiduciary obligations to stockholders and Sun and that Sun has and follows appropriate governance standards. Among other matters, the CGNC:

Reviews and approves nominees for service on the Board;

Considers candidates recommended by stockholders; and

Adopts, reviews and implements corporate governance policies and procedures.

The members of the CGNC are all independent directors under applicable NASDAQ rules. The CGNC operates under a written charter, a copy of which can be found on our website at *www.sun.com/company/cgov/bcc.jsp.*

Consideration of Director Nominees

The CGNC regularly reviews the current composition and size of the Board. The CGNC considers and evaluates any candidates who have been properly recommended by a stockholder, as well as those candidates who have been identified by management, individual members of the Board or, if the CGNC determines, a search firm. This review may, in the CGNC s discretion, be based solely on information provided to the CGNC or may also include discussions with persons familiar with the candidate, an interview with the candidate, the retention of third-party interviewers or other actions. The CGNC Policies and Procedures for Director Candidates can be found on our website at *www.sun.com/company/cgov/bcc.jsp*.

During fiscal 2007, Sun retained a third-party search firm to assist in identifying and evaluating potential director candidates. Peter L.S. Currie and P. Anthony Ridder were each initially identified and recommended as director candidates by one of our non-employee directors. Michael E. Marks was appointed to the Board in connection with a private placement transaction between Sun and KKR Private Equity Investors, L.P. (KKR) pursuant to which Sun agreed to appoint one person to its Board nominated by KKR. Mr. Marks, who is a senior advisor to KKR, was KKR s nominee.

The CGNC evaluates candidates proposed by stockholders using the same criteria as those used for other candidates. In its evaluation of director candidates, including the members of the Board eligible for re-election, the CGNC considers the following:

- The current size and composition of the Board and the needs of the Board and the committees of the Board;

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- Such factors as issues of diversity, age, skills such as understanding of manufacturing, technology, finance, sales and marketing, and international background; and
- Such other factors as the CGNC may consider appropriate.

The CGNC requires the following minimum qualifications to be satisfied by any candidate for a position on the Board:

- Possession of the highest personal and professional ethics and integrity;
- Proven achievement and competence in the candidate s field and the ability to exercise sound business judgment;
- Attributes that are complementary to those of the existing directors;
- The acumen, drive and skills to assist and support management and make significant contributions to Sun s success;
- An understanding of the fiduciary responsibilities that are required of a member of the Board and the commitment of time and energy necessary to diligently carry out those responsibilities;
- Diversity of experiences and personal and cultural attributes; and
- Expansive professional background ensuring a comprehensive appreciation of Sun s business including manufacturing, technology development, finance, sales and marketing, and international business.

For a description of the process for a stockholder to recommend a director candidate for the CGNC s consideration or to nominate directors in accordance with our Bylaws, please see General Information What is the deadline to propose actions for consideration at the 2008 annual meeting of stockholders or to nominate individuals to serve as directors? .

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DIRECTOR COMPENSATION

Director Summary Compensation Table for Fiscal 2007

The following table summarizes the total compensation earned or paid by Sun to directors who were not executive officers during fiscal 2007.

Name	Fees Earned or Paid in Cash ($)(1)	Stock Awards ($)(2)	Option Awards ($)(2)	Non-Equity Incentive Plan Compensation ($)	Change in Pension Value ($)	All Other Compensation ($)	Total ($)
James L. Barksdale	$ 47,000	$	$ 25,326	$	$	$	$ 72,326
Stephen M. Bennett	45,324		22,205				67,529
Peter L.S. Currie	34,571		4,776				39,347
L. John Doerr	16,321		(3)				16,321
Robert J. Finocchio, Jr.	62,000		13,550				75,550
Robert J. Fisher	17,571		(3)				17,571
Michael E. Marks	7,816		1,019				8,835
Scott G. McNealy(4)	1,000,000	2,244,491	3,302,627	1,621,450(5)	831,094(6)	190,664(7)	9,190,326
Patricia E. Mitchell	42,000		14,684				56,684
M. Kenneth Oshman	42,000		25,326	(10,428)	(15,611)		
Proceeds from property sales, net of expenses	2,512						
Business acquired, net of cash acquired	(4,799)						
Net cash used in investing activities	(12,715)	(15,611)					
Cash flows from financing activities:							
Borrowings on revolving line of credit	473,000	10,000					
Repayments of revolving line of credit	(551,000)	(10,000)					
Proceeds from issuance of long-term debt		400,000					
Repayments of long-term debt	(24,144)	(407,856)					
Proceeds from issuance of common stock	30	1,062					
Repurchase of common stock	(17,849)	(48,314)					
Distribution to noncontrolling	(2,082)	(2,761)					

interest				
Excess tax benefits from stock-based awards		136		720
Payment of financing costs		(128)		(12,490)
Net cash used in financing activities		(122,037)		(69,639)
Effect of exchange rate changes on cash and cash equivalents		(202)		(168)
Net increase (decrease) in cash and cash equivalents		(1,539)		5,955
Cash and equivalents at beginning of period		26,929		85,668
Cash and equivalents at end of period	$	25,390	$	91,623
Supplemental information:				
Cash paid for interest	$	14,476	$	14,920
Cash paid for income taxes, net of refunds	$	10,634	$	8,339
Non-cash investing activities:				
Capital expenditures incurred but not paid	$	322	$	577
Non-cash financing activities				
Offset of subordinated notes with escrow	$	12,825	$	
Restricted share stock bonus	$	3,877	$	
Repurchased shares settled but not paid	$	174	$	

See notes to condensed consolidated financial statements.

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CENTRAL GARDEN & PET COMPANY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Nine Months Ended June 26, 2010

(unaudited)

1. Basis of Presentation

The condensed consolidated balance sheets of Central Garden & Pet Company and subsidiaries (the Company or Central) as of June 27, 2009 and June 26, 2010, the condensed consolidated statements of operations for the three and nine months ended June 27, 2009 and June 26, 2010, and the condensed consolidated statements of cash flows for the nine months ended June 27, 2009 and June 26, 2010 have been prepared by the Company, without audit. In the opinion of management, all adjustments (which include only normal recurring adjustments) considered necessary to present fairly the financial position, results of operations and cash flows of the Company for the periods mentioned above, have been made.

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 7, Supplemental Equity and Comprehensive Income Information, for further detail.

Due to the seasonal nature of the Company s garden business, the results of operations for the three and nine month periods ended June 27, 2009 and June 26, 2010 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 2009 Annual Report on Form 10-K, which has previously been filed with the Securities and Exchange Commission. The September 26, 2009 balance sheet presented herein was derived from the audited 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 fully 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. Effective September 27, 2009, the Company adopted new accounting guidance, as discussed further below, concerning the treatment of noncontrolling interests in consolidated financial statements. The new guidance changed the accounting and reporting for minority interests, which have been re-characterized as noncontrolling interests, as discussed above. Prior period financial statements and disclosures for existing minority interests have been restated in accordance with the new guidance. As of June 27, 2009, September 26, 2009, September 27, 2008 and September 29, 2007 the liability related to noncontrolling interest was $2.1 million, $2.3 million, $2.7 million and $1.8 million, respectively, and was included as mezzanine equity on the consolidated balance sheets. For the three and nine months ended June 27, 2009 and the fiscal years ended September 26, 2009, September 27, 2008 and September 29, 2007, the net income attributable to noncontrolling interest was $1.1 million, $1.5 million, $1.7 million, $0.8 million and $1.4 million, respectively, and was included as minority interest on the consolidated statements of operations. All other requirements of the new guidance will be applied prospectively. See Note 7, Supplemental Equity and Comprehensive Income Information, for additional information and revised disclosures required by the adoption of that guidance.

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 also enters into commodity futures and options 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 cost of sales in its condensed consolidated statements of operations. As of

June 26, 2010, the notional amount of these contracts was not significant.

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Recent Accounting Pronouncements

Accounting Standards Codification (ASC) Subtopic 820, Fair Value Measurements and Disclosures, provides a consistent definition of fair value that focuses on exit price, prioritizes the use of market-based inputs over entity-specific inputs for measuring fair value and establishes a three-level hierarchy for fair value measurements. On September 28, 2008, the Company adopted the applicable sections of ASC 820 for financial assets and financial liabilities and for nonfinancial assets and nonfinancial liabilities that are remeasured at least annually. At that time, the Company elected to defer adoption of ASC 820 for one year for nonfinancial assets and nonfinancial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis. On September 27, 2009, the Company adopted the sections of ASC 820 regarding nonfinancial assets and nonfinancial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis. Fair value measurements of non-financial assets and liabilities are used primarily in the impairment analyses of long-lived assets, goodwill and other intangible assets. The applicable sections of ASC 820 were applied prospectively. The adoption of the various sections of ASC 820 on September 28, 2008 and September 27, 2009 did not have a material impact on the Company s consolidated financial statements.

On September 27, 2009, the Company adopted the applicable sections of ASC 805, Business Combinations. ASC 805 provides revised guidance for recognizing and measuring identifiable assets and goodwill acquired, liabilities assumed and any noncontrolling interest in the acquiree in a business combination. Additionally, this ASC provides disclosure requirements to enable users of the financial statements to evaluate the nature and financial effects of the business combination. ASC 805 amends the applicable sections of ASC 740, Income Taxes, such that adjustments made to valuation allowances on deferred taxes and acquired tax contingencies related to acquisitions made prior to September 27, 2009 also fall within the scope of these sections. The adoption of the applicable sections of this ASC may have an impact on the accounting for any future acquisitions or divestitures.

On September 27, 2009, the Company adopted the applicable sections of ASC 805, Business Combinations, that address accounting for assets acquired and liabilities assumed in a business combination that arise from contingencies. These applicable sections address application issues raised on the initial recognition and measurement, subsequent measurement and accounting and disclosure of assets and liabilities arising from contingencies in a business combination. These sections generally apply to assets acquired and liabilities assumed in a business combination that arise from contingencies that would be within the scope of ASC 450, Contingencies, if not acquired or assumed in a business combination. The adoption of these applicable sections may have an impact on the accounting for any future acquisitions or divestitures.

On September 27, 2009, the Company adopted ASC 810-10-65-1, Consolidation. This section requires reporting entities to present noncontrolling interests in any of its consolidated entities as equity (as opposed to a liability or mezzanine equity) and provides guidance on the accounting for transactions between an entity and noncontrolling interests. The adoption did not have an impact on net earnings or equity available to the Company s shareholders, but impacted the presentation format of the Company s consolidated statements of operations and consolidated balance sheets as follows:

- Consolidated net income (loss) was recast to include net income (loss) attributable to both the Company and noncontrolling interests in the condensed consolidated statements of operations.

- Noncontrolling interests were reclassified from mezzanine equity to equity, separate from the Company s shareholders equity, in the condensed consolidated balance sheets.

- The condensed consolidated statements of cash flows now begin with net income (loss) (including noncontrolling interests) instead of net income (loss) attributable to Central Garden & Pet Company, with net income (loss) from noncontrolling interests no longer a reconciling item in arriving at net cash provided by operating activities.

- Interim disclosures of consolidated shareholders equity and comprehensive income have been added as part of the disclosure requirements.

On September 27, 2009, the Company adopted provisions of ASC 815, Derivatives and Hedging, which requires entities to disclose: (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for, and (c) how derivative instruments and related hedged items affect an entity s financial position, financial performance and cash flows. The adoption of the provisions of this ASC did not have a material impact on the Company s consolidated financial statements.

On September 27, 2009, the Company adopted the applicable sections of ASC 275, Risks and Uncertainties, and ASC 350, Intangibles Goodwill and Other, that address the determination of the useful life of intangible assets. These sections address the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset. The adoption of these applicable sections may have an impact on the accounting for intangible assets that are a part of any future acquisitions.

On September 27, 2009, the Company adopted the applicable sections of ASC 260-10, Earnings Per Share, that address whether instruments granted in share-based payment transactions are participating securities. These sections conclude that unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and shall be included in the computation of basic earnings per share pursuant to the two-class method. The adoption of these applicable sections did not have a material impact on the Company s consolidated financial statements.

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In August 2009, the FASB issued Accounting Standards Update (ASU) No. 2009-05, Measuring Liabilities at Fair Value. ASU 2009-05 amends ASC 820, Fair Value Measurements, by providing additional guidance on determining the fair value of liabilities when a quoted price in an active market for an identical liability is not available. This ASU became effective for the Company on September 27, 2009 and did not have a significant impact on the measurement of its liabilities as of that date; however, the ASU may affect the fair value measurement of liabilities for future acquisitions and divestitures.

In December 2009, the FASB issued ASU No. 2009-16, Accounting for Transfers of Financial Assets. ASU 2009-16 amends the guidance on accounting for transfers of financial assets, including securitization transactions, where entities have continued exposure to risks related to transferred financial assets, and also expands the disclosure requirements for such transactions. This ASU will become effective for the Company on September 26, 2010. The Company is currently evaluating the impact of this standard on its consolidated financial statements.

In December 2009, the FASB issued ASU No. 2009-17, Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities. This ASU amends the guidance for consolidation of VIEs primarily related to the determination of the primary beneficiary of the VIE. This ASU will become effective for the Company on September 26, 2010. The Company is currently evaluating the impact of this standard on its consolidated financial statements.

In January 2010, the FASB issued ASU No. 2010-6, Improving Disclosures about Fair Value Measurements. This ASU requires new disclosures regarding transfers in and out of Level 1 and Level 2 fair value measurements, as well as requiring presentation on a gross basis information about purchases, sales, issuances and settlements in Level 3 fair value measurements. The ASU also clarifies existing disclosures regarding level of disaggregation, inputs and valuation techniques. The ASU is effective for interim and annual reporting periods beginning after December 15, 2009 and became effective for the Company on December 27, 2009. Disclosures about purchases, sales, issuances and settlements in the roll forward of activity in Level 3 fair value measurements are effective for fiscal years beginning after December 15, 2010 and will be effective for the Company on September 25, 2011.

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).

Assets and Liabilities Measured at Fair Value on a Recurring Basis

The Company had no significant financial assets or liabilities on the balance sheet that were measured at fair value as of June 26, 2010.

In February 2009, the Company s $75 million pay-floating interest rate swap was terminated prior to its maturity by the counterparty in accordance with the terms of the interest rate swap agreement. Prior to its termination, the swap was measured under Level 2 inputs in the fair value hierarchy. As a result of this swap termination, the Company received cash proceeds and realized a settlement gain of $2.3 million that was recorded as an adjustment to the carrying amount of the related debt. In conjunction with the tender offer and purchase of our 9.125% senior subordinated notes in March 2010, the remaining unrecognized gain on the pay-floating interest rate swap was recognized and included as part of the loss on extinguishment of debt included in interest expense on the condensed consolidated statements of operations. See Note 6, Long Term Debt, for further information.

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 period ended June 26, 2010, the Company was not required to measure any significant non-financial assets and liabilities at fair value.

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3. Financial Instruments

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

The Company s remaining outstanding 9.125% senior subordinated notes due 2013 with a carrying value of $14.7 million were redeemed by the Company on April 21, 2010 for $14.9 million, which includes a redemption premium of $0.2 million.

The estimated fair value of the Company s $400 million 8.25 % senior subordinated notes due 2018 as of June 26, 2010 was $398.0 million, compared to a carrying value of $400.0 million. The estimated fair value is based on quoted market prices for these notes.

4. 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 all four reporting units to the Company s total market capitalization.

5. Other Intangible Assets

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

	Gross	Accumulated Amortization (in millions)	Impairment	Net Carrying Value
June 26, 2010				
Marketing-related intangible assets amortizable	$ 12.3	$ (4.7)	$	$ 7.6
Marketing-related intangible assets nonamortizable	59.6		(4.9)	54.7
Total	71.9	(4.7)	(4.9)	62.3
Customer-related intangible assets amortizable	41.6	(10.3)		31.3
Other acquired intangible assets amortizable	9.2	(3.0)		6.2
Other acquired intangible assets nonamortizable	1.2		(1.2)	
Total	10.4	(3.0)	(1.2)	6.2
Total other intangible assets	$ 123.9	$ (18.0)	$ (6.1)	$ 99.8
September 26, 2009				
Marketing-related intangible assets amortizable	$ 10.5	$ (3.6)	$	$ 6.9
Marketing-related intangible assets nonamortizable	61.4		(4.9)	56.5
Total	71.9	(3.6)	(4.9)	63.4
Customer-related intangible assets amortizable	41.6	(8.7)		32.9
Other acquired intangible assets amortizable	9.2	(2.1)		7.1
Other acquired intangible assets nonamortizable	1.2		(1.2)	

Total	10.4		(2.1)		(1.2)		7.1
Total other intangible assets	$ 123.9	$	(14.4)	$	(6.1)	$	103.4

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

The Company evaluates long-lived assets, including amortizable 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, and no impairment of its indefinite-lived intangible assets was indicated during its fiscal 2009 review. Other factors indicating the carrying value of the Company s amortizable intangible assets may not be recoverable were not present during fiscal 2009 or the first nine months of fiscal 2010, and accordingly, no impairment charges were recognized during fiscal 2009 or fiscal 2010. In fiscal 2008, indicators of impairment were identified within the Garden Products segment related to current operating losses in certain operations. Accordingly, the Company recognized a $6.1 million impairment charge related to certain trade names.

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The Company is currently amortizing its acquired intangible assets with definite lives over periods ranging from 1 to 25 years; over weighted average lives of 12 years for marketing-related intangibles, 22 years for customer-related intangibles and nine years for other acquired intangibles. Amortization expense for intangibles subject to amortization was approximately $1.2 million and $1.2 million, and $3.5 million and $3.1 million, for the three and nine month periods ended June 26, 2010 and June 27, 2009, 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 2010 through fiscal 2014.

6. Long-Term Debt

Long-term debt consists of the following:

	June 26, 2010	September 26, 2009
	(in thousands)	
Senior subordinated notes, interest at 8.25%, payable semi-annually, principal due March 2018	$ 400,000	
Senior subordinated notes, interest at 9.125% payable semi-annually		137,175
Term loan, interest at LIBOR + 1.50% or the prime rate plus 0.50%, quarterly principal payments of $750,000		268,602
Revolving credit facility, interest at prime plus 0% to 0.25% or LIBOR + 0.75% to 1.375%		
Revolving credit facility, interest at Alternate Base Rate (ABR) plus 1.5% to 2.5% or LIBOR + 2.5% to 3.5%, final maturity June 2015		
Unamortized deferred gain on pay-floating interest rate swap termination, maturing February 2013		1,901
Other notes payable	339	407
Total	400,339	408,085
Less current portion	(201)	(3,270)
Long-term portion	$ 400,138	$ 404,815

Senior Credit Facility

On June 25, 2010, the Company entered into an Amended and Restated Credit Agreement (the Credit Agreement) with respect to a five-year senior secured revolving credit facility (the Credit Facility) in an aggregate principal amount of $275 million. The Company has the option to increase the size of the Facility by an additional $200 million of incremental term loans and/or revolving loans should it exercise its option and one or more lenders are willing to make such increased amounts available to it. There was no outstanding balance at June 26, 2010 under the Credit Facility. There were $18.6 million of letters of credit outstanding. After giving effect to the financial covenants in the Credit Agreement, the remaining potential borrowing capacity was $256.4 million.

Interest on the Credit Facility is based, at the Company s option, on a rate equal to the ABR, which is the greatest of the prime rate, the Federal Funds rate plus $^1/2$ of 1% or one month LIBOR plus 1%, plus a margin, which fluctuates from 1.5% to 2.5%, or LIBOR plus a margin, which fluctuates from 2.5% to 3.5% and commitment fees that range from 0.35% to 0.75%, determined quarterly based on consolidated total debt to consolidated EBITDA for the most recent trailing 12-month period. As of June 26, 2010, the applicable interest rate on the Credit Facility related to alternate base rate borrowings was 5.25%, and the applicable interest rate related to LIBOR rate borrowings was 3.35%.

The Credit Facility is guaranteed by the Company s material subsidiaries and is secured by the Company s assets, excluding real property but including substantially all of the capital stock of the Company s subsidiaries. The Credit Agreement contains certain financial and other covenants which require the Company to maintain minimum levels of interest coverage and maximum levels of senior debt to EBITDA and that restrict the Company s ability to repurchase its stock, make investments in or acquisitions of other businesses and pay dividends above certain levels over the life of the Credit Facility. Under the terms of the Company s Credit Facility, it may make restricted payments, including cash dividends and stock repurchases, in an aggregate amount initially not to exceed $200 million over the life of the Credit Facility, subject to qualifications and baskets as defined in the Credit Agreement. Apart from the covenants limiting restricted payments and capital expenditures, the Credit Facility does not restrict the use of retained earnings or net income. The Company was in compliance with all financial covenants as of June 26, 2010.

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The Company incurred approximately $2.9 million of costs in conjunction with this transaction, which included banking fees and legal expenses. These costs will be amortized over the term of the Credit Facility.

Senior Subordinated Notes and Debt Refinancing

On March 8, 2010, the Company issued $400 million aggregate principal amount of 8.25% senior subordinated notes due March 1, 2018 (the 2018 Notes). The Company used the proceeds together with available cash to purchase its outstanding $135.3 million aggregate principal amount of 9.125% senior subordinated notes due February 1, 2013 (the 2013 Notes), including accrued interest, to repay the $267.1 million outstanding under its senior term loan maturing February 2012 and pay fees and expenses related to the offering. The Company received tenders and consents from the holders of $135.3 million of its 2013 Notes, including $12.8 million held in escrow for the benefit of the Company, which was previously recorded as a reduction of debt for accounting purposes against the Company s 2013 Notes. The remaining $14.7 million of 2013 Notes were redeemed on April 21, 2010.

The Company incurred approximately $9.5 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 2018 Notes.

As a result of this debt refinancing, the Company incurred a pre-tax loss of $3.2 million, comprised of the unamortized deferred financing costs related to the 2013 Notes and the retired term loan, the tender call premium, consent fees and the unamortized gain on the swap termination related to the 2013 Notes. The amount is included in interest expense in the condensed consolidated statements of operations.

The 2018 Notes require semiannual interest payments, which commence on September 1, 2010. The 2018 Notes are unsecured senior subordinated obligations and are subordinated to all of the Company s existing and future senior debt, including the Company s Credit Facility. The obligations under the 2018 Notes are fully and unconditionally guaranteed on a senior subordinated basis by each of the Company s existing and future domestic restricted subsidiaries with certain exceptions. The guarantees are general unsecured senior subordinated obligations of the guarantors and are subordinated to all existing and future senior debt of the guarantors.

The Company may redeem some or all of the 2018 Notes at any time prior to March 1, 2014 at the principal amount plus a make whole premium. The Company may redeem some or all of the 2018 Notes at any time on or after March 1, 2014 for 104.125%, after March 1, 2015 for 102.063% and after March 1, 2016 for 100%, plus accrued and unpaid interest. Additionally, at any time prior to March 1, 2013, the Company may redeem up to 35% of the 2018 Notes with any proceeds the Company receives from certain equity offerings at a redemption price of 108.25% of the principal amount, plus accrued and unpaid interest. The holders of the 2018 Notes have the right to require the Company to repurchase all or a portion of the 2018 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 2018 Notes contain customary high yield covenants, including covenants limiting debt incurrence and restricted payments, subject to certain baskets and exceptions.

7. Supplemental Equity and Comprehensive Income Information

The following table summarizes the allocation of total comprehensive income between controlling and noncontrolling interests for the nine months ended June 26, 2010 and June 27, 2009:

	Nine Months Ended June 26, 2010		
(in thousands)	**Controlling Interest**	**Noncontrolling Interest**	**Total**
Net income	$ 54,599	$ 1,943	$ 56,542
Other comprehensive loss:			
Foreign currency translation	(598)		(598)
Total comprehensive income	$ 54,001	$ 1,943	$ 55,944

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	Nine Months Ended June 27, 2009		
(in thousands)	Controlling Interest	Noncontrolling Interest	Total
Net income	$ 57,912	$ 1,498	$ 59,410
Other comprehensive loss:			
Foreign currency translation	(1,853)		(1,853)
Total comprehensive income	$ 56,059	$ 1,498	$ 57,557

The following table provides a summary of the changes in the carrying amounts of shareholders equity attributable to controlling interest and noncontrolling interest for the nine months ended June 26, 2010 and June 27, 2009:

	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 26, 2009	$ 188	$ 475	$ 16	$ 531,300	$ 12,044	$ 1,062	$ 545,085	$ 2,250	$ 547,335
Comprehensive income (loss)					54,599	(598)	54,001	1,943	55,944
Stock based compensation				2,624			2,624		2,624
Restricted share activity				(198)			(198)		(198)
Issuance of common stock		3		1,608			1,611		1,611
Repurchase of common stock	(20)	(28)		(38,233)	(9,025)		(47,306)		(47,306)
Distributions to noncontrolling interest								(2,761)	(2,761)
Other								(5)	(5)
Tax benefit on stock option exercise				720			720		720
Balance June 26, 2010	$ 168	$ 450	$ 16	$ 497,821	$ 57,618	$ 464	$ 556,537	$ 1,427	$ 557,964

	Controlling Interest								
(in thousands)	Common Stock	Class A Common Stock	Class B Stock	Additional Paid In Capital	Retained Earnings (Deficit)	Accumulated Other Comprehensive Income	Total	Noncontrolling Interest	Total
Balance September 27, 2008	$ 210	$ 485	$ 16	$ 555,310	$ (50,463)	$ 3,200	$ 508,758	$ 2,667	$ 511,425
Comprehensive income (loss)					57,912	(1,853)	56,059	1,498	57,557
Stock based compensation				6,627			6,627		6,627
Restricted share activity				(222)			(222)		(222)
Issuance of common stock		8		1,471			1,479		1,479
Repurchase of common stock	(15)	(12)		(17,773)			(17,800)		(17,800)
Distributions to noncontrolling interest								(2,082)	(2,082)
Tax benefit on stock option exercise				136			136		136
Other								4	4
Balance June 27, 2009	$ 195	$ 481	$ 16	$ 545,549	$ 7,449	$ 1,347	$ 555,037	$ 2,087	$ 557,124

8. Stock-Based Compensation

The Company recognized share-based compensation expense of $4.0 million and $8.2 million for the nine month periods ended June 26, 2010 and June 27, 2009, respectively, as a component of selling, general and administrative expenses. The tax benefit associated with share-based compensation expense for the nine month periods ended June 26, 2010 and June 27, 2009 was $1.5 million and $3.1 million, respectively.

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9. Earnings per Share

The following is a reconciliation of the numerators and denominators of the basic and diluted per share computations for income from continuing operations.

	Three Months Ended June 26, 2010			Nine Months Ended June 26, 2010		
	Income	Shares	Per Share	Income	Shares	Per Share
	(in thousands, except per share amounts)					
Basic EPS:						
Net income available to common shareholders	$ 25,873	63,810	$ 0.41	$ 54,599	64,879	$ 0.84
Effect of dilutive securities:						
Options to purchase common stock		665	(0.01)		704	(0.01)
Restricted shares		131			133	
Diluted EPS:						
Net income available to common shareholders	$ 25,873	64,606	$ 0.40	$ 54,599	65,716	$ 0.83

	Three Months Ended June 27, 2009			Nine Months Ended June 27, 2009		
	Income	Shares	Per Share	Income (Loss)	Shares	Per Share
	(in thousands, except per share amounts)					
Basic EPS:						
Net income available to common shareholders	$ 31,076	69,345	$ 0.45	$ 57,912	69,885	$ 0.83
Effect of dilutive securities:						
Options to purchase common stock		724	(0.01)		503	(0.01)
Restricted shares		380			410	
Diluted EPS:						
Net income available to common shareholders	$ 31,076	70,449	$ 0.44	$ 57.912	70,798	$ 0.82

Options to purchase 11.3 million shares of common stock at prices ranging from $4.26 to $17.99 per share were outstanding at June 26, 2010 and options to purchase 8.8 million shares of common stock at prices ranging from $4.26 to $17.99 per share were outstanding at June 27, 2009.

For the three month periods ended June 26, 2010 and June 27, 2009, options to purchase 7.9 million and 6.1 million shares of common stock, respectively, were outstanding but were not included in the computation of diluted earnings per share because the option exercise prices were greater than the average market price of the common shares and, therefore, the effect would be anti-dilutive.

For the nine month period ended June 26, 2010 and June 27, 2009, options to purchase 7.7 million and 6.4 million shares of common stock, respectively, were outstanding but were not included in the computation of diluted earnings per share because the option exercise prices were greater than the average market price of the common shares and, therefore, the effect would be anti-dilutive.

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10. 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 Executive Officer reviews the results of operations to make decisions regarding performance assessment and resource allocation. These operating segments are Pet Products and Garden Products and are presented in the table below (in thousands).

	Three Months Ended		Nine Months Ended	
	June 27, 2009	June 26, 2010	June 27, 2009	June 26, 2010
Net sales:				
Pet Products	$ 215,010	$ 222,700	$ 629,525	$ 626,595
Garden Products	267,152	242,786	621,604	550,063
Total net sales	$ 482,162	$ 465,486	$ 1,251,129	$ 1,176,658
Income (loss) from operations:				
Pet Products	$ 29,822	$ 32,611	$ 74,594	$ 85,002
Garden Products	35,270	30,137	64,235	60,616
Corporate	(13,522)	(10,108)	(32,769)	(31,935)
Total income from operations	51,570	52,640	106,060	113,683
Interest expense net	(5,199)	(9,796)	(17,232)	(24,543)
Other income	1,161	42	80	428
Income taxes	15,371	15,860	29,498	33,026
Income including noncontrolling interest	32,161	27,026	59,410	56,542
Net income attributable to noncontrolling interest	1,085	1,153	1,498	1,943
Net income attributable to Central Garden & Pet Company	$ 31,076	$ 25,873	$ 57,912	$ 54,599
Depreciation and amortization:				
Pet Products	$ 3,907	$ 3,833	$ 11,937	$ 11,677
Garden Products	1,612	1,575	4,949	4,546
Corporate	1,670	1,838	4,999	5,486
Total depreciation and amortization	$ 7,189	$ 7,246	$ 21,885	$ 21,709

	June 27, 2009	June 26, 2010	September 26, 2009
Assets:			
Pet Products	$ 430,840	$ 405,703	$ 394,150
Garden Products	410,283	373,394	348,825
Corporate	361,188	404,610	407,950
Total assets	$ 1,202,311	$ 1,183,707	$ 1,150,925
Goodwill (included in corporate assets above):			
Pet Products	$ 202,074	$ 202,950	$ 202,950
Garden Products	4,799	5,680	4,799

Total goodwill	$ 206,873	$ 208,630	$ 207,749

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11. 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 $400 million 8.25% Senior Subordinated Notes issued on March 8, 2010 (the Notes). Certain subsidiaries and operating divisions are not guarantors of the Notes and have been included in the financial results of the Parent in the information below. These Non-Guarantor entities are not material to the Parent. Those subsidiaries that are guarantors and co-obligors of the Notes are as follows:

Farnam Companies, Inc.

Four Paws Products Ltd.

Grant Laboratories, Inc.

Gulfstream Home & Garden, Inc.

Interpet USA, LLC

Kaytee Products, Inc.

Matthews Redwood & Nursery Supply, Inc.

Matson, LLC

New England Pottery, LLC

Pennington Seed, Inc. (including Pennington Seed, Inc. of Nebraska, Gro Tec, Inc., Seeds West, Inc., All-Glass Aquarium Co., Inc. and Cedar Works, LLC.)

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 June 26, 2010
(in thousands)
(unaudited)

	Parent	Guarantor Subsidiaries	Eliminations	Consolidated
Net sales	$ 151,716	$ 346,876	$ (33,106)	$ 465,486
Cost of products sold and occupancy	107,151	228,667	(33,106)	302,712
Gross profit	44,565	118,209		162,774
Selling, general and administrative expenses	36,025	74,109		110,134

Income from operations	8,540	44,100		52,640
Interest net	(9,879)	83		(9,796)
Other income (loss)	(4,612)	4,654		42
Income (loss) before income taxes	(5,951)	48,837		42,886
Income taxes (tax benefit)	(2,202)	18,062		15,860
Income (loss) including noncontrolling interest	(3,749)	30,775		27,026
Income attributable to noncontrolling interest	1,153			1,153
Income (loss) attributable to Central Garden & Pet Co. before equity in undistributed income of guarantor subsidiaries	(4,902)	30,775		25,873
Equity in undistributed income of guarantor subsidiaries	30,775		(30,775)	
Net income attributable to Central Garden & Pet Co.	$ 25,873	$ 30,775	$ (30,775)	$ 25,873

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CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS

Three Months Ended June 27, 2009

(in thousands)
(unaudited)

	Parent	Guarantor Subsidiaries	Eliminations	Consolidated
Net sales	$ 151,915	$ 363,921	$ (33,674)	$ 482,162
Cost of products sold and occupancy	109,350	241,432	(33,674)	317,108
Gross profit	42,565	122,489		165,054
Selling, general and administrative expenses	35,447	78,037		113,484
Income from operations	7,118	44,452		51,570
Interest net	(5,347)	148		(5,199)
Other income (expense)	(4,339)	5,500		1,161
Income (loss) before income taxes	(2,568)	50,100		47,532
Income taxes (tax benefit)	(1,186)	16,557		15,371
Income (loss) including noncontrolling interest	(1,382)	33,543		32,161
Income attributable to noncontrolling interest	1,085			1,085
Income (loss) attributable to Central Garden & Pet Co. before equity in undistributed income of guarantor subsidiaries	(2,467)	33,543		31,076
Equity in undistributed income of guarantor subsidiaries	33,543		(33,543)	
Net income attributable to Central Garden & Pet Co.	$ 31,076	$ 33,543	$ (33,543)	$ 31,076

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CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS
Nine Months Ended June 26, 2010
(in thousands)
(unaudited)

	Parent	Guarantor Subsidiaries	Eliminations	Consolidated
Net sales	$ 379,937	$ 898,866	$ (102,145)	$ 1,176,658
Cost of products sold and occupancy	269,911	597,160	(102,145)	764,926
Gross profit	110,026	301,706		411,732
Selling, general and administrative expenses	94,092	203,957		298,049
Income from operations	15,934	97,749		113,683
Interest net	(24,779)	236		(24,543)
Other income (loss)	(7,771)	8,199		428
Income (loss) before income taxes	(16,616)	106,184		89,568
Income taxes (tax benefit)	(6,113)	39,139		33,026
Income (loss) including noncontrolling interest	(10,503)	67,045		56,542
Income attributable to noncontrolling interest	1,943			1,943
Income (loss) attributable to Central Garden & Pet Co. before equity in undistributed income of guarantor subsidiaries	(12,446)	67,045		54,599
Equity in undistributed income of guarantor subsidiaries	67,045		(67,045)	
Net income attributable to Central Garden & Pet Co.	$ 54,599	$ 67,045	$ (67,045)	$ 54,599

CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS
Nine Months Ended June 27, 2009
(in thousands)
(unaudited)

	Parent	Guarantor Subsidiaries	Eliminations	Consolidated
Net sales	$ 386,655	$ 979,159	$ (114,685)	$ 1,251,129
Cost of products sold and occupancy	282,007	672,719	(114,685)	840,041
Gross profit	104,648	306,440		411,088
Selling, general and administrative expenses	91,982	213,046		305,028
Income from operations	12,666	93,394		106,060
Interest net	(17,702)	470		(17,232)
Other income (expense)	(5,992)	6,072		80
Income (loss) before income taxes	(11,028)	99,936		88,908
Income tax (tax benefit)	(4,219)	33,717		29,498
Income (loss) including noncontrolling interest	(6,809)	66,219		59,410
Income attributable to noncontrolling interest	1,498			1,498
Income (loss) attributable to Central Garden & Pet Co. before equity in undistributed income of guarantor subsidiaries	(8,307)	66,219		57,912

Equity in undistributed income of guarantor subsidiaries