

SCOTTS LIQUID GOLD INC

Form 10-K

March 29, 2013

Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-K**

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

For the fiscal year ended December 31, 2012

OR

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

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

Commission File Number 001-13458

**SCOTT S LIQUID GOLD-INC.**

(Name of small business as specified in its charter)

**Colorado**  
(State or other jurisdiction of  
incorporation or organization)  
**84-0920811**  
(I.R.S. Employer  
Identification No.)  
**4880 Havana Street, Suite 400, Denver, CO 80239**  
(Address of principal executive offices and Zip Code)  
**(303) 373-4860**  
(Registrant's telephone number, including area code)

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

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

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

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

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

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

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

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act.)  Yes  No

The aggregate market value of the common stock held by non-affiliates of the issuer was \$1,604,772 on June 29, 2012.

As of March 29, 2013, there were 11,201,622 shares of common stock, \$0.10 par value per share, outstanding.

#### **DOCUMENTS INCORPORATED BY REFERENCE**

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

Certain information required by Part III is incorporated by reference to the Registrant's definitive Proxy Statement for the Annual Meeting of Shareholders to be filed within 120 days after December 31, 2012.

**Table of Contents**

**CAUTIONARY NOTE ON FORWARD-LOOKING INFORMATION**

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

**Table of Contents**

## TABLE OF CONTENTS

	<b>Page</b>
<b>PART I</b>	
Item 1. <u>Business</u>	1
Item 1A. <u>Risk Factors</u>	8
Item 1B. <u>Unresolved Staff Comments</u>	11
Item 2. <u>Properties</u>	11
Item 3. <u>Legal Proceedings</u>	11
Item 4. <u>Mine Safety Disclosures</u>	11
<b>PART II</b>	
Item 5. <u>Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	12
Item 6. <u>Selected Financial Data</u>	13
Item 7. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	13
Item 7A. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	18
Item 8. <u>Financial Statements and Supplementary Data</u>	19
Item 9. <u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	37
Item 9A. <u>Controls and Procedures</u>	37
Item 9B. <u>Other Information</u>	38
<b>PART III</b>	
Item 10. <u>Directors, Executive Officers and Corporate Governance</u>	38
Item 11. <u>Executive Compensation</u>	38
Item 12. <u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	38
Item 13. <u>Certain Relationships and Related Transactions, and Director Independence</u>	38
Item 14. <u>Principal Accounting Fees and Services</u>	38
<b>PART IV</b>	
Item 15. <u>Exhibits and Financial Statement Schedules</u>	38

**Table of Contents****PART I****ITEM 1. BUSINESS****General**

Scott's Liquid Gold-Inc., a Colorado corporation, was incorporated on February 15, 1954. Through our wholly-owned subsidiaries, we develop, manufacture, market and sell quality household and skin and hair care products. Our most well-recognized product, Scott's Liquid Gold® wood cleaner and preservative, has been sold in the United States for over 60 years. Our Alpha Hydrox® skin care brand was one of the first to use alpha hydroxy acids ( AHAs ). Our Neoteric Diabetic® products were developed to address the skin conditions of persons living with diabetes. We are the exclusive distributor in the United States of Montagne Jeunesse skin sachets and Batiste Dry Shampoo manufactured by two other companies.

In this Report the terms we, us or our refers to Scott's Liquid Gold-Inc. and our subsidiaries, collectively. Our business is divided into two operating segments, household products and skin and hair care products.

The following table sets forth the principal products in our household products segment.

<i>Operating Segment</i>	<i>Key Products</i>
Household	Scott's Liquid Gold® Wood Cleaner and Preservative Scott's Liquid Gold® Wood Wash Scott's Liquid Gold® Dust 'N Go Wipes Scott's Liquid Gold® Clean Screen Touch of Scent® Air Freshener

The following table sets forth the principal products in our skin and hair care products segment.

<i>Operating Segment</i>	<i>Key Products</i>
Skin and Hair Care	Alpha Hydrox® Skin Care Products Neoteric Diabetic® Healing Cream Neoteric Diabetic® Shampoo and Scalp Care Neoteric Massage Oils Montagne Jeunesse Face Masque Sachets Batiste Dry Shampoos

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

**Subsequent Event**

On February 1, 2013, we consummated the sale of our real estate assets located at 4880 Havana Street, Denver, Colorado, consisting of approximately 10.8 acres of land improved with four buildings containing approximately 241,684 square feet of office, warehouse and manufacturing space, with associated improvements and personal property, and adjacent vacant land of approximately 5.5 acres (together, the Property). We sold the Property for a purchase price of \$9,500,000 and incurred selling expenses of \$579,800, including \$570,000 for real estate broker commissions.

In connection with the sale, we leased back from the purchaser approximately 16,078 square feet of office space (the Office Lease) and approximately 113,620 square feet of manufacturing and warehouse space (the Warehouse Lease) currently used by us. Each of the Office Lease and the

## **Table of Contents**

Warehouse Lease has an initial term of three years, with options to extend the term for two additional terms of three years each. Rent for the Office Lease is \$13.00 per square foot per annum, with annual 3% increases. Rent for the Warehouse Lease is \$3.25 per square foot per annum, with annual 3% increases, and we will pay an additional \$1.25 per square foot per annum as our share of the purchaser's operating expenses under the Warehouse Lease (including taxes, insurance and common area maintenance charges). If certain uncontrollable operating expenses increase by more than 5% per year, our share of operating expenses under the Warehouse Lease may be increased.

As of the date of the closing, the principal and interest balance on our long-term debt secured by the Property with Citywide Banks (the Bank) was \$3,373,961. This debt was repaid in full at closing. We also paid approximately \$202,000 at closing for real estate property taxes for 2012. In addition, on February 4, 2013, we paid \$909,778 to Summit Financial Resources, L.P. (Summit) to repay the outstanding balance on our credit line with Summit and we have maintained a zero loan balance since that time. We made this payment to reduce our interest costs. Please see Note 1(e) to our Consolidated Financial Statements in Item 8 for a discussion of our financing agreement with Summit. Also, in February 2013, we paid certain other financial obligations to suppliers and vendors in the amount of approximately \$960,000 and incurred approximately \$150,000 in capital expenditures as a result of the sale of our Property. We estimate that our remaining cash from the sale of the Property after the payment of all of the foregoing expenses was approximately \$3.3 million.

Because the sale of our Property was consummated after the end of our fiscal year, its effects are not reflected in our financial statements. We believe the sale of our Property will allow us to carry less debt, reduce our interest and other borrowing expenses, satisfy certain outstanding financial obligations, allow us to negotiate better terms with suppliers and vendors, increase the amount we invest in advertising and allow us to pursue potential strategic transactions. We also believe having the Office Lease and Warehouse Lease in place will allow us to continue to reduce and better control our operating costs and expenses.

## **Strategy**

We are focused on strategies that we believe will enhance our long-term financial health and deliver long-term shareholder value. In order to achieve these objectives, we plan to generate continued growth of our existing brands and products, as well as pursue new opportunities to develop, acquire or distribute new brands and products. For 2013, we continue to pursue the following primary goals that we established in 2012: (1) increase sales by strengthening and broadening consumer awareness of our products; (2) add additional products to the mix of products that one or more of our existing major customers already buy from us; (3) add at least one major retailer as a customer; and (4) reduce operating costs and expenses. As discussed below, we believe that we made substantial progress on these goals. One of our primary goals from 2012 was to deal with our Property. As discussed above, we sold the Property on February 1, 2013 and leased back certain portions of the Property.

## **Household Products**

Scott's Liquid Gold® wood cleaner and preservative has been our core product since our inception. It has been sold in the United States for over 60 years. Unlike a furniture polish, our product contains natural oils that penetrate the wood's surface to clean, replace lost moisture, minimize the appearance of scratches and bring out the natural beauty of wood. We have also introduced an additional wood care product in a wipe form and a wood wash product. Our Dust 'N Go pre-moistened cloth wipes are quick, easy and convenient dusting wipes for wood and numerous other surfaces. Our wood wash product simply and safely cleans all types of wood surfaces.

During the second quarter of 2006, we introduced our mold remediation product Mold Control 500. Due to declining sales and distribution, this product was discontinued at the end of 2012. We

## **Table of Contents**

attribute this decline to the following three primary factors: (1) generally lower actual consumer demand than anticipated; (2) the product is effective, but expensive; and (3) the product involves a delivery system considered by many not to be consumer friendly.

During the first quarter of 2009, we introduced Clean Screen, an affordable, simple and easy way for cleaning electronic screens, especially today's new sensitive electronics. Clean Screen is a liquid formulated with a state-of-the-art water treatment technology that not only cleans away dirt, but also mineral deposits and other impurities. In 2010, we introduced Clean Screen in a wipe form and marketed the product as Little Clean Screen.

Since 1982, we have sold Touch of Scent® air fresheners. Our air fresheners offer a unique dispenser with aerosol refills. Touch of Scent® air fresheners are available in a wide assortment of beautiful fragrances, which are quick, easy to use and effective.

Household products accounted for 30.5% of our consolidated net sales in 2012 and 38.0% in 2011. We continually evaluate possible new household products to be developed, acquired, manufactured and/or distributed by us.

## **Skin and Hair Care Products**

In early 1992, we began to develop, manufacture, market and sell skin care products under the trade name of Alpha Hydrox®. These products include facial care products, a body lotion, a body wash and a foot cream. Our Alpha Hydrox® skin care brand was one of the first to use AHAs. Products containing AHAs gently slough off dead skin cells to promote a healthier, more youthful appearance and help to diminish fine lines and wrinkles.

Our first Neoteric Diabetic® product was a healing cream introduced in 2001 and a subsequent product was a shampoo and scalp care product introduced in 2011. Both of these products were developed to address the skin conditions of persons living with diabetes, caused by poor blood circulation, and which contain a patented oxygenated oil technology. Our healing cream is a therapeutic moisturizer that provides a clinically proven treatment for dry skin by increasing blood circulation and helping to speed the healing of minor scrapes and cuts. Our shampoo and scalp care product helps to soothe the discomfort of dryness, flaking and itching of the scalp while gently cleaning the hair.

Since 2001, we have been the exclusive distributor in the United States for face masque sachets manufactured by Montagne Jeunesse International Ltd. ( Montagne Jeunesse ). Montagne Jeunesse is based in the United Kingdom. Their sachet products are currently sold in over 70 countries. These masques are sold for single use in unique and attractive packages in a wide assortment of types and fragrances. A significant portion of our business consists of the sale of these sachet products. See Manufacturing and Suppliers in this Item 1 below for information on the terms of our agreement with Montagne Jeunesse.

In the fourth quarter of 2009, we became the exclusive distributor in the United States for Batiste Dry Shampoo with the exception of certain warehouse stores and governmental entities. Dry shampoo is a quick and convenient way to refresh hair between washes. Batiste was one of the innovators of dry shampoo. We believe that there is a large and fast-growing market for dry shampoo. In that regard, Church & Dwight Co. Inc. ( Church & Dwight ) acquired Batiste Dry Shampoo in 2011. We continue to be the exclusive distributor for the shampoo under the terms of our distribution agreement with Church & Dwight. The initial term of our agreement with Church & Dwight runs through December 31, 2014 and the agreement will be automatically renewed for additional one year terms, unless terminated. See Manufacturing and Suppliers in this Item 1 below for information on the terms of our agreement with Church & Dwight. Church & Dwight is a leading global consumer products company with such well-recognized brand names as Arm & Hammer, Oxiclean and Orajel.



## **Table of Contents**

Skin and hair care products accounted for 69.5% of our consolidated net sales in 2012 and 62.0% in 2011. We continually evaluate possible new skin and hair care products as well as other beauty care products to be developed, acquired, manufactured and/or distributed by us.

### **Marketing and Distribution**

We primarily market our products through: (1) trade promotions to support price features, displays and other merchandising of our products by our retail customers; (2) consumer incentives such as coupons and rebates; and (3) consumer marketing in print, social media and television advertising.

Our products are sold nationally, directly through our sales force and indirectly through independent brokers, to mass marketers, drugstores, supermarkets, hardware stores and other retail outlets and to wholesale distributors. In 2012 and 2011, Wal-Mart Stores, Inc. ( Wal-Mart ) accounted for approximately 32% and 33% of our sales of household products, respectively. With regard to our skin and hair care products, Wal-Mart accounted for approximately 18% of sales in both 2012 and 2011. Wal-Mart accounted for approximately 22% and 24% of our aggregate net sales on a consolidated basis in 2012 and 2011, respectively.

In 2012 and 2011, Ulta Salon, Cosmetics & Fragrance, Inc. ( Ulta ) accounted for approximately 16% and 12%, respectively, of our skin and hair care products. During 2012 and 2011, we did not sell household products to Ulta. Ulta accounted for approximately 11% and 8% in 2012 and 2011, respectively, of our aggregate net sales on a consolidated basis.

In 2012 and 2011, Walgreens Co. ( Walgreens ) accounted for approximately 14% and 17%, respectively, of our sales of skin and hair care products. During 2012 and 2011, we did not sell household products to Walgreens. Walgreens accounted for approximately 7% and 11% in 2012 and 2011, respectively, of our aggregate net sales on a consolidated basis. As is typical in our industry, we do not have a long-term contract with Wal-Mart, Ulta, Walgreens or any other retail customer.

We also use our Scott's Liquid Gold and Neoteric Cosmetics websites for sales of our products directly to consumers. Such sales were approximately 9% and 8% of total sales in 2012 and 2011, respectively.

Our household and skin and hair care products are available in limited distribution in Canada and other foreign countries. Please see Note 8, Segment Information , to our Consolidated Financial Statements in Item 8 for information regarding our sales in foreign countries. Currently, foreign sales are made to distributors who are responsible for the marketing of the products, and we are paid for these products in United States currency.

From time to time, our customers return products to us. For our household products, we permit returns only for a limited time. With regard to our skin and hair care products, returns are more frequent under an unwritten industry standard that permits returns for a variety of reasons. In the event a skin and hair care customer requests a return of a product, we will consider the request, and may grant such request in order to maintain or enhance our relationship with the customer, even in the absence of an enforceable right of the customer to do so. Typically, customers that return products to us take a credit on our invoice equal to the original sale price plus a handling charge ranging from 8-10% of the original sales price.

## **Table of Contents**

### **Manufacturing and Suppliers**

We owned all of our manufacturing facilities until February 1, 2013. Please see Note 12 to our Consolidated Financial Statements in Item 8 for information on the sale of our real estate assets and our leasing back certain of the manufacturing facilities that we sold. We own and operate all of our manufacturing equipment. We manufacture all of our products with the exception of the following products: (1) those products for which we act as a distributor; (2) our Scott's Liquid Gold® Dust 'N Go wipes; and (3) our Little Clean Screen product. For all of our products, we must maintain sufficient inventories to ship most orders as they are received.

Quality control is enforced at all stages of production, as well as upon the receipt of raw materials from suppliers. Raw materials are purchased from a number of suppliers and, at the present time, are readily available. However, we do not have long term contracts with our suppliers and any contracts we do have with suppliers may be terminated at any time. Our sole supply for the oxygenated oil used in our Neoteric Diabetic® skin care products is a French company with which we have a non-exclusive supply agreement. We believe that we have good relationships with all of our suppliers.

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

In 2001, we commenced purchases of skin care sachets from Montagne Jeunesse under a distributorship agreement covering the United States. On May 4, 2005, our wholly-owned subsidiary, Neoteric Cosmetics, Inc. ( Neoteric ), entered into a new distribution agreement with Montagne Jeunesse. Pursuant to this new agreement, Neoteric is the exclusive distributor to market and sell Montagne Jeunesse's skin care sachets in the United States. The initial term was for 18 months, but the agreement continues until it is terminated by either party giving to the other party no less than three or six months' written notice of termination, depending on the reason for termination. To date, neither party has provided such notice. As a practical matter, we believe that the continuation of the distribution agreement is dependent on maintaining our good relationship with Montagne Jeunesse.

Under the terms of the agreement, Neoteric agreed, among other things: (1) not to distribute during the duration of the agreement and for 36 months thereafter any goods of the same description as and which compete with the Montagne Jeunesse products; (2) to use our best endeavors to develop, promote and sell the products in the United States and to expand the sale of the products to all potential purchasers by all reasonable and proper means; (3) to purchase certain core products; and (4) to maintain an inventory of the products for our own account for sale of these products throughout the United States. Montagne Jeunesse agreed to use all reasonable endeavors to meet all of our orders for the products to the extent that such orders do not exceed the forecast that we provide them periodically for each type of product. We purchase the products for the published list prices as established by Montagne Jeunesse from time to time with the provision that they are required to give us three months prior written notice of any changes in the published list prices. Neither party may assign or transfer any rights or obligations under the agreement or subcontract the performance of any obligation.

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

## **Table of Contents**

In January of 2012, we entered into a distribution agreement with Church & Dwight allowing us to act as the exclusive distributor of Batiste Dry Shampoo products in the United States. Church & Dwight still has the right to sell Batiste products to government agencies and departments, as well as warehouse clubs and multinational superstores or hypermarkets. The agreement requires us to satisfy certain annual sales objectives. If we fail to purchase a sufficient amount of Batiste Dry Shampoo products, Church & Dwight may terminate the agreement, or we may lose our exclusive distribution rights. This minimum amount will increase each year. We have also agreed to spend a minimum amount each year for advertising and sales promotion in support of Batiste Dry Shampoo products.

The agreement provides that we will not be permitted to manufacture, distribute or sell any products that are competitive with Batiste Dry Shampoo products. The initial pricing terms for the Batiste products were negotiated with Church & Dwight, but may be increased by Church & Dwight at any time upon 90 days prior written notice of any price increase. While the agreement may be terminated in the case of an uncured breach, upon a change in control, or upon our violation of export control laws, the initial term of the agreement will be three years and will automatically renew for successive one year terms upon written notice by either party.

### **Competition**

Our business is highly competitive in both household and skin and hair care products. We compete in both categories primarily on the basis of quality and the distinguishing characteristics of our products.

The wood care, air freshener, and clean screen product categories are dominated by three to five companies significantly larger than us and each of these competitors produces several competing products. Irrespective of the foregoing, we maintain a visible position in the wood care category, but do not have sufficient information to make an accurate representation as to the market share of our products.

The skin and hair care category is also highly competitive. Several competitors are significantly larger than us and each of these competitors produces several competing products. Some of these companies also manufacture products with AHAs with which our Alpha Hydrox<sup>®</sup> products must compete. Because of the number of varied products produced by our competitors, we cannot make an accurate representation as to the market share of our skin and hair care products.

### **Regulation**

We are subject to various federal, state and local laws and regulations that pertain to the type of consumer products that we manufacture and sell. Many chemicals used in consumer products, some of which are used in several of our product formulations, have come under scrutiny by various state governments and the Federal government. These chemicals are called volatile organic compounds ( VOC s ), which arguably contribute to the formation of ground level ozone. Many states as well as the Federal government have passed regulations that limit the amount of VOC s allowed in various categories of consumer products. All of our products currently meet the most stringent VOC regulations and may be sold throughout the United States. Any new or revised VOC regulations developed by various states or the Federal government may apply to our products and could potentially require reformulation of those products in the future. Limitation of VOC content in consumer products by both state and Federal governments will continue to be part of regulatory efforts to achieve compliance with clean air regulations. We continue to monitor all environmental regulatory activities and believe that we have done all that is necessary to satisfy the current requirements of the Federal Clean Air Act and the laws of various state governments.

Many of our skin care products, most of which contain AHAs, are considered cosmetics within the definition of the Federal Food Drug and Cosmetic Act (the FFDC A ). The FFDC A defines

## **Table of Contents**

cosmetics as products intended for cleansing, beautifying, promoting attractiveness or altering the appearance without affecting the body's structure or functions. Our cosmetic products are subject to the regulations under the FFDCFA and the Fair Packaging and Labeling Act (the FPLA). The relevant laws and regulations are enforced by the U.S. Food and Drug Administration (the FDA). Such laws and regulations govern the ingredients and labeling of cosmetic products and set forth good manufacturing practices for companies to follow. Although FDA regulations require that the safety of a cosmetic ingredient be substantiated prior to marketing, there is no requirement that a company submit the results of any testing performed or any other data or information with respect to any ingredient to the FDA.

The FDA's National Center for Toxicological Research has periodically been investigating the effect of long term exposure to AHAs since 2003. On December 31, 2003, the FDA published a call for data on certain ingredients in various products, including AHAs that are part of wrinkle remover products. Manufacturers were asked to submit any data supporting the reclassification of these cosmetic products as over-the-counter drugs. In January 2005, the FDA issued final guidance to the effect that products containing AHAs should alert users that those products may increase skin sensitivity to sun and possible sunburn and the steps to avoid such consequences. On October 27, 2008, FDA published a set of Q&A's that dealt with both long term exposure and drug/cosmetic issues.

With respect to the drug/cosmetic issue, the FDA restated its traditional position that certain AHA products intended for therapeutic use, such as acne treatments or skin lighteners, are considered drugs. Other AHA products, including those marketed by us, are considered cosmetics. The Q&A also reported on the results of two studies on the issue of skin damage caused by UV rays, and the potential photocarcinogenicity of AHA products. The studies concluded that applying AHA products to the skin resulted in increasing UV sensitivity, but that the effect was completely reversible. In addition another study on potential photocarcinogenesis found that AHA products had no effect on the process. Accordingly, we lawfully market our products as cosmetics, and our labeling fully complies with the FDA's guidance.

Our advertising is subject to regulation under the Federal Trade Commission Act and related regulations, which prohibit the false and misleading claims in advertising. We believe that all of our labeling and promotional materials comply with these regulations.

## **Employees**

We employ 67 persons of which 29 work in plant and production related functions and 38 work in administrative, sales and advertising functions. No contracts exist between us and any union. We monitor wage and salary rates in the Rocky Mountain area and pursue a policy of providing competitive compensation to our employees. The compensation of our executive officers is under the review of the Compensation Committee of our Board of Directors. Fringe benefits for our employees include medical, vision and dental plans, short-term disability, life insurance, a 401(k) plan with matching contributions for employees earning \$35,000 or less per annum and an employee stock ownership (ESOP) plan. We consider our employee relations to be satisfactory with the average tenure of our employees to be approximately 15 years.

## **Patents and Trademarks**

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

## **Table of Contents**

### **Available Information and Code of Ethics**

We will make available free of charge through the website <http://www.businesswire.com/cnn/slqd.htm>, this annual report on Form 10-K, our quarterly reports on Form 10-Q, our current reports on Form 8-K, and amendments to such reports, as soon as reasonably practicable after we electronically file or furnish such material with the Securities and Exchange Commission (the "SEC"). These reports are also available through a link on our website ([www.scottsliquidgold.com](http://www.scottsliquidgold.com)). Information on our website is not incorporated by reference into this Report and should not be considered part of this document. We will provide upon request (see below for instructions) and at no charge electronic or paper copies of these filings with the SEC (excluding exhibits).

We will also provide to any person without charge, upon request (see below for instructions), a copy of our code of business conduct and ethics.

A request for our reports filed with the SEC or our code of business conduct and ethics may be made to: Corporate Secretary, Scott's Liquid Gold-Inc., 4880 Havana Street, Suite 400, Denver, Colorado 80239.

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

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

#### **We need to increase our revenues and/or further reduce our costs in order to become profitable.**

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

#### **Our cash flow is dependent upon operating cash flow, available cash and available funds under our financing agreements with Summit and Wells Fargo Bank, National Associations ( "Wells Fargo" ).**

Because we are dependent on our operating cash flow, any loss of a significant customer, any further decreases in the distribution of our skin and hair care or household products, new competitive products affecting sales levels of our products or any significant expense not included in our internal budget could result in the need to raise cash. Our financing agreement with Summit was amended on March 16, 2011 (effective March 1, 2011) and then again on June 29, 2012 (effective July 1, 2012). The agreement has a term that expires on January 1, 2014, but it may be renewed for additional 12 month periods unless either party elects to cancel in writing at least 60 days prior to January 1, 2014 and thereafter on the anniversary date of each 12 month period. On March 16, 2011, under a consent agreement from Summit, we entered into an agreement that enables us to sell the receivables of our largest customer to Wells Fargo. Except for these agreements, we have no arrangements for any external financing of debt or equity, and we are not certain any such financing would be available on acceptable terms. In order to improve our operating cash flow, we need to achieve profitability, and/or further reduce our costs.

## **Table of Contents**

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

The turmoil in the investment market of the United States, the tightening of credit and relatively high level of unemployment in the United States have led to an increased level of commercial and consumer delinquencies, lack of consumer confidence, increased market volatility and possibly a reduction in business activity generally. A continuation of these conditions could have, among other things, the following potential negative effects: (1) a reduction in spending of consumers in general including in the area of household products and skin and hair care products, which could reduce our sales; (2) the potential increase in bad debts or reserve for bad debts affecting our financial condition or cash flow; and (3) exposure to any increased interest expense to the extent that any financing or refinancing could be at costs higher than our existing debt.

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

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

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

Our large competitors regularly introduce new products and spend considerably more than we can on advertising. The distribution of our products and sales can be adversely impacted by the actions of our competitors.

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

We believe the growth of our net sales is substantially dependent upon our ability to introduce our products to current and new consumers through advertising and marketing. At present, we have limited resources compared to many of our competitors to spend on advertising and marketing. Advertising, particularly television advertising, can be important in reaching consumers, although the effectiveness of any particular advertisement cannot be predicted. Additionally, we may not be able to obtain optimal advertising placements at our current advertising budget. Our limited resources to promote our products through advertising may adversely affect our net sales and operating performance.

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

If we are not successful in making ongoing sales of our newer products to retail stores or these products are not well received by consumers, our revenues could be materially and adversely affected.

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

For more than a majority of our sales, we are dependent upon sales to major customers, including Wal-Mart, which is our largest customer, Ulta, which is our second largest customer and Walgreens, which is our third largest customer. The easy access of consumers to our products is dependent upon major retail stores and other retail stores carrying our products. The willingness of these customers (i.e.,

## **Table of Contents**

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

**A significant part of our sales of skin and hair care products are represented by the Montagne Jeunesse sachet products and Batiste Dry Shampoo products, each of which depends upon the continuation of our distributorship agreement with the manufacturers of these products.**

Our distributorship agreement with Montagne Jeunesse does not have a fixed term, but continues until it is terminated by either party giving the other party no less than three or six months' written notice of termination, depending on the reason for termination. To date, neither party has provided such notice. As a practical matter, we believe that the continuation of our agreement with Montagne Jeunesse is dependent upon maintaining our good relationship with them. Our distribution agreement with Church & Dwight, the manufacturer of Batiste Dry Shampoo products, has an initial term of three years and, following this term, may be automatically renewed. If our agreements with Montagne Jeunesse or Church & Dwight are terminated, we may no longer be able to distribute Montagne Jeunesse or Batiste Dry Shampoo products on an exclusive basis, or at all, and sales in our skin and hair care segment would be adversely affected.

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

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

**Our sales are affected adversely by returns.**

In our industry, our customers may be given authorization by us to return products. These returns result in refunds, a reduction of our revenues and usually the need to dispose of the resulting inventory at discounted prices. Accordingly, the level of returns can significantly impact our revenues and cash flow. See information about returns in Results of Operations in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations.

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

Regulations affecting our products include requirements of the FDA for cosmetic products and environmental regulations affecting emissions from our products. In the past, the FDA has mentioned the treatment of products with AHAs as drugs, which could make our production and sale of certain Alpha Hydrox<sup>®</sup> products more expensive or prohibitive. Also, in the past, we were required to change the formulation of our household products to comply with environmental regulations and will continue to do so as required.

## **Table of Contents**

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

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

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

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

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

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

### **ITEM 1B. UNRESOLVED STAFF COMMENTS.**

**Not applicable.**

### **ITEM 2. PROPERTIES.**

Our facilities, located in Denver, Colorado, which we owned until February 1, 2013, consisted of four connected buildings and a parking garage (approximately 241,684 square feet in total) and about 16.3 acres of land. These buildings range in age from approximately 16 to 39 years (126,600 square feet having been added in 1995 and 1996). As described above under Item 1, Business, we sold the Property on February 1, 2013 and leased a portion of our facilities back from the purchaser. Our facilities house our corporate headquarters and all of our manufacturing and warehouse operations, which are used by both of our operating segments. Until the sale of the Property on February 1, 2013, our facilities served as collateral for a \$5.2 million bank loan with a principal balance at December 31, 2012 of \$3.4 million. Please see Note 12 to our Consolidated Financial Statements in Item 8 for information on the sale of our facilities, the leasing back of certain of the facilities that we sold and the repayment of our bank loan. We believe that our current leased space will provide capacity for growth for the foreseeable future.

### **ITEM 3. LEGAL PROCEEDINGS.**

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

### **ITEM 4. MINE SAFETY DISCLOSURES.**

**Not applicable.**



**Table of Contents****PART II****ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.****Market Information**

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

	2012			2011	
	Three Months Ended			Three Months Ended	
	High	Low		High	Low
March 31	\$ 0.28	\$ 0.17	March 31	\$ 0.51	\$ 0.20
June 30	\$ 0.21	\$ 0.20	June 30	\$ 0.52	\$ 0.30
September 30	\$ 0.32	\$ 0.13	September 30	\$ 0.35	\$ 0.31
December 31	\$ 0.39	\$ 0.14	December 31	\$ 0.35	\$ 0.16

**Shareholders**

As of March 29, 2013, based on inquiry, we had approximately 772 shareholders of record.

**Dividends**

We did not pay any cash dividends during the two most recent fiscal years. No decision has been made as to future dividends. See **Results of Operations Liquidity and Capital Resources** for information concerning restrictions on our ability to pay dividends.

**Equity Plans**

The following table provides, as of December 31, 2012, information regarding our 1998 and 2005 Stock Option Plans. The 1998 plan has expired, but options under that plan remain outstanding. We also have an employee stock ownership plan which invests only in our common stock, but which is not included in the table below.

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by security holders	1,387,350	\$ 0.25	1,570,650
Equity compensation plans not approved by security holders	0	0	0
<b>Total</b>	<b>1,387,350</b>	<b>\$ 0.25</b>	<b>1,570,650</b>



**Table of Contents**

**ITEM 6. SELECTED FINANCIAL DATA.**

Not applicable.

**ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.**

**Critical Accounting Policies**

We have identified the policies below as critical to our business operations and the understanding of our results of operations. These policies involve significant judgments, estimates and assumptions by us. For a detailed discussion on the application of these and other accounting policies, see Note 1 to our Consolidated Financial Statements in Item 8.

*Revenue Recognition*

Our revenue recognition policy is significant because the amount and timing of revenue is a key component of our results of operations. We follow guidance issued by the Financial Accounting Standards Board ( FASB ), which requires that certain criteria be met in order to recognize revenue. If these criteria are not met, then the associated revenue is deferred until it is met. In our case, the criteria generally are met when we have an arrangement to sell a product, we have delivered the product in accordance with that arrangement, the sales price of the product is determinable and we believe that we will be paid for the sale.

We establish reserves for customer returns of our products and customer allowances. We estimate these reserves based upon, among other things, an assessment of historical trends, information from customers and anticipated returns and allowances related to current sales activity. These reserves are established in the period of sale and reduce our revenue in that period.

Our reserve for customer allowances includes primarily reserves for trade promotions to support price features, displays and other merchandising of our products to our customers. The actual level of returns and customer allowances are influenced by several factors, including the promotional efforts of our customers, changes in mix of our customers, changes in the mix of the products we sell and the maturity of the product. We may change our estimates based on actual results and consideration of other factors that cause returns and allowances. In the event that actual results differ from our estimates, the results of future periods may be impacted.

We also establish reserves for coupons, rebates and certain other promotional programs for consumers. We estimate these reserves based upon, among other things, an assessment of historical trends and current sales activity. These reserves are recorded as a reduction of revenue at the later of the date at which the revenue is recognized or the date at which the sale incentive is offered. In the event that actual results differ from our estimates, the results of future periods may be impacted.

We have also established an allowance for doubtful accounts. We estimate this allowance based upon, among other things, an assessment of the credit risk of specific customers and historical trends. We believe our allowance for doubtful accounts is adequate to absorb any losses which may arise. In the event that actual losses differ from our estimates, the results of future periods may be impacted.

*Income Taxes*

As of December 31, 2012, we have net deferred income tax assets of approximately \$4,212,000 which primarily relate to net operating loss carryforwards, expenses that are not yet deductible for tax purposes and tax credit carryforwards. These assets are offset by deferred income tax liabilities for

## **Table of Contents**

differences in the book and tax bases of property and equipment. The net deferred tax asset is fully reserved by a valuation allowance. The valuation allowance represents our determination that, more likely than not, we will be unable to realize the value of such assets at this time due to the uncertainty of future profitability.

### *Inventory Valuation and Reserves*

Our inventory is valued at the lower of cost or market, cost being determined under the first-in, first-out method. We estimate an inventory reserve for slow moving and obsolete products and raw materials based upon, among other things, an assessment of historical and anticipated sales of our products. In the event that actual results differ from our estimates, the results of future periods may be impacted.

### *Long-Lived Assets and Assets Held for Sale*

Please refer to Note 1(i) of our Consolidated Financial Statements in Item 8 as to our determination that there has been no impairment in the carrying values of our long-lived assets at December 31, 2012. However, please refer to the same note as to our determination to reclassify our long-lived assets as held for sale .

### *Recently Issued Accounting Pronouncements*

We have considered recently issued accounting pronouncements and do not believe that such pronouncements are of significance or potential significance to us.

## **Results of Operations**

Our consolidated net sales for 2012 were \$16,041,400 versus \$15,616,300 for 2011, an increase of \$425,100 or 2.7%. We saw a 14.9% increase in net sales of our own line of skin care products and a 15.4% increase in net sales of the skin and hair care products that we distribute for other companies. These increases were offset in part by a 17.6% decrease in net sales of our household products. The reasons for the decrease in the sales of our household products are described below.

Our net loss for 2012 was \$1,371,800 versus a net loss \$633,800 for 2011. The increased loss for 2012 compared to 2011 resulted primarily from: (1) an impairment to the carrying value of our facilities as detailed below; (2) a reclassification of our facilities to assets held for sale and related impairment as detailed below; (3) increases in trade promotions to our customers; (4) increases in costs of sales as detailed below; and (5) increases in operating expenses as detailed below.

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

	<b>Year Ended December 31,</b>	
	<b>2012</b>	<b>2011</b>
Net sales		
Household products	30.5%	38.0%
Skin and hair care products	69.5%	62.0%
Total net sales	100.0%	100.0%
Cost of sales	56.6%	54.8%
Gross profit	43.4%	45.2%
Other revenue	1.5%	1.0%
	44.9%	46.2%
Operating expenses	46.2%	48.8%
Loss on impairment of long-lived assets	1.8%	0%
Loss on impairment of assets held for sale	3.6%	0%
Interest expense	1.8%	1.5%
	53.4%	50.3%
(Loss) income before taxes	(8.6%)	(4.1%)

Our gross margins may not be comparable to those of other companies because some companies include all of the costs related to their distribution network in cost of sales. In contrast, other companies, like us, exclude a portion of these costs (i.e., freight out to customers) from gross margin. Instead, we include them as part of selling expenses. See Note 1(n), Operating Costs and Expenses Classification, to our Consolidated Financial Statements in Item 8.

**Comparative Net Sales**

	<b>Year Ended December 31,</b>		<b>Percentage</b>
	<b>2012</b>	<b>2011</b>	<b>Increase (Decrease)</b>
Scott's Liquid Gold® and other household products	\$ 4,895,600	\$ 5,941,100	(17.6%)
Total household products	4,895,600	5,941,100	(17.6%)
Alpha Hydrox®, Diabetic cream and shampoo and other skin care products	4,499,800	3,915,900	14.9%
Montagne Jeunesse and Batiste Dry Shampoo	6,646,000	5,759,300	15.4%
Total skin and hair care products	11,145,800	9,675,200	15.2%
Total net sales	\$ 16,041,400	\$ 15,616,300	2.7%

During 2012, net sales of skin and hair care products accounted for 69.5% of consolidated net sales compared to 62.0% in 2011. The net sales of these products were \$11,145,800 in 2012 compared to \$9,675,200 in 2011, an increase of \$1,470,600 or 15.2%.

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

The net sales of our Alpha Hydrox® and other manufactured skin care products were \$4,499,800 in 2012 versus \$3,915,900 in 2011, an increase of \$583,900 or 14.9%. This increase is primarily attributable to increased distribution to new and existing customers and the improved placement of our products at existing customers.

The net sales of Montagne Jeunesse and Batiste Dry Shampoo were \$6,646,000 in 2012 versus \$5,759,300 in 2011, an increase of \$886,700 or 15.4%. This increase is primarily attributable to increased distribution at new and existing customers and the improved placement of our products at existing customers.

Sales of household products for 2012 accounted for 30.5% of consolidated net sales compared to 38.0% for the same period in 2011. During 2012, the sales of our household products were \$4,895,600 as compared to \$5,941,100 for the same period in 2011, a decrease of \$1,045,500 or 17.6%. This decrease

**Table of Contents**

reflects primarily decreased distribution in our Clean Screen and Little Clean Screen products. We believe the decline in sales of Clean Screen is the result of new competitors in the segment including competitors with significant name brand recognition. We believe that this trend is likely to continue impacting our net sales going forward, as our competitors continue to gain market share in this area.

Due to the decline in sales and distribution of Mold Control 500, this product was discontinued at the end of 2012. We attribute this decline to the following three primary factors: (1) generally lower actual consumer demand than anticipated; (2) the product is effective, but expensive; and (3) the product involves a delivery system considered by many not to be consumer friendly.

We paid our customers a total of \$1,735,700 in 2012 versus \$1,315,200 in 2011, an increase of \$420,500 or 32% for trade promotions to support price features, displays and other merchandising of our products. We made a strategic decision this year to invest more in the promotion and marketing of our products. Our primary goal was to obtain additional distribution with our existing customers, better product placement in the stores with these customers and to obtain distribution with new customers. We believe our increased net sales in our skin and hair products segment during the latter part of 2012 has demonstrated the early benefits of our decision to increase spending in support of promotions and marketing.

From time to time, our customers return products to us. For our household products, we permit returns only for a limited time. With regard to our skin and hair care products, returns are more frequent under an unwritten industry standard that permits returns for a variety of reasons. In the event a skin and hair care customer requests a return of a product, we will consider the request, and may grant such request in order to maintain or enhance our relationship with the customer, even in the absence of an enforceable right of the customer to do so. Typically, customers that return products to us take a credit on our invoice equal to the original sale price plus a handling charge ranging from 8-10% of the original sales price. Our product returns (as a percentage of net sales) were 0.60% in 2012 compared to 0.15% in 2011. The increase reflects primarily returns due to reducing the fill amount and reducing the number of colors in the graphics on our cans of Scott's Liquid Gold® Wood Cleaner and Preservative to reduce costs.

On a consolidated basis, cost of sales was \$9,074,700 for 2012 compared to \$8,553,500 for 2011, an increase of \$521,200 or 6.1%, on a net sales increase of 2.7%. As a percentage of consolidated net sales, cost of sales was 56.6% in 2012 versus 54.8% in 2011.

The cost of sales for our skin and hair care products was 53.7% of net sales in both 2012 and 2011. The costs of sales for our household products increased to 63.1% of net sales in 2012 as compared to 57.9% in 2011. This increase primarily reflect more spending on trade promotions in 2012 as compared to 2011, more obsolete inventory charged to expense in 2012 as compared to 2011, and increases in our costs for certain raw materials.

**Table of Contents****Operating Expenses, Interest Expense and Other Income**

	Year Ended December 31,		Percentage
	2012	2011	Increase (Decrease)
Operating Expenses			
Advertising	\$ 320,200	\$ 773,300	(58.6%)
Selling	4,305,200	4,527,100	(4.9%)
General and administrative	2,792,200	2,318,100	20.5%
Impairment of long-lived assets	286,900	0	100.0%
Impairment on assets held for sale	579,800	0	100.0%
<b>Total operating expenses</b>	<b>\$ 8,284,300</b>	<b>\$ 7,618,500</b>	<b>8.7%</b>
Rental and Other Income	\$ 240,400	\$ 159,200	51.0%
Interest Expense	\$ 294,600	\$ 237,300	24.1%

Our operating expenses increased by \$665,800 in 2012 when compared to 2011 or 8.7%. These expenses consist primarily of advertising, selling, general and administrative expenses, an impairment of long-lived assets and an impairment on assets held for sale, which are discussed below.

Advertising expenses for 2012 were \$320,200 compared to \$773,300 for 2011, a decrease of \$453,100 or 58.6%. The decrease relates primarily to the cost of a national television campaign for Scott's Liquid Gold wood cleaner and preservative in the fourth quarter of 2011 as well as a national coupon drop that was part of the same marketing program. We did not do a similar national television campaign and coupon drop in 2012.

Selling expenses for 2012 were \$4,305,200 compared to \$4,527,100 for 2011, a decrease of \$221,900 or 4.9%. The decrease was comprised primarily of the following three factors: (1) a decrease in the costs of displays for certain of our products; (2) a decrease in shipping and handling costs; and (3) a decrease in postage expense for sampling programs.

General and administrative expenses for 2012 were \$2,792,200 compared to \$2,318,100 for 2011, an increase of \$474,100 or 20.5%. This increase is attributable to the following three primary factors: (1) recent changes in personnel within our finance and accounting group; (2) an increase in expenses for audit fees and legal fees, including legal fees incurred in connection with the sale of our real estate assets; and (3) an increase in repairs and maintenance costs for our real estate assets.

The impairment of our long-lived assets for 2012 was \$286,900 compared to \$0 for 2011. The increase is due to an impairment to the carrying value of our facilities as discussed in Note 1(i) of our Consolidated Financial Statements in Item 8.

The impairment of our assets held for sale for 2012 was \$579,800 compared to \$0 for 2011. The increase is due to a reclassification of our long-lived assets to assets held for sale as discussed in Note 1(i) of our Consolidated Financial Statements in Item 8.

Rental and other income in 2012 of \$240,400 included \$152,100 of net rental receipts, \$2,500 in interest earned on our cash reserves and other income of \$85,800. This compares to total rental and other income for 2011 of \$159,200 which included \$153,100 of net rental receipts, \$4,900 in interest earned on our cash reserves and other income of \$1,200. The increase in other income is due primarily to the sale of certain manufacturing equipment that was no longer required.

Interest expense for 2012 was \$294,600 and included \$98,000 in administrative fees incurred relative to the sale of accounts receivable invoices to Summit. Interest expense for 2011 was \$237,300 and included \$64,500 in administrative fees paid to Summit. The increase is due to higher borrowings under our line of credit with Summit to fund increased gross sales activity and trade promotions.





## **Table of Contents**

During 2012 and 2011, our expenditures for research and development were insignificant.

### **Liquidity and Capital Resources**

#### *Citywide Loan*

Please see Note 4 to our Consolidated Financial Statements in Item 8 for information on our loan with Citywide Banks (the Bank ) for \$5,156,600 secured by the land, building and fixtures at our Denver, Colorado facilities with an outstanding principal balance at December 31, 2012 of \$3,363,300. In addition, please see Note 12 to our Consolidated Financial Statements in Item 8 for information regarding our repayment of this loan in connection with our sale of our Property.

#### *Financing Agreements*

Please see Note 1(e) to our Consolidated Financial Statements in Item 8 for a discussion of our financing agreements with Summit and Wells Fargo. Note 1(e) also includes a discussion of the accounting treatment of the funds borrowed pursuant to these agreements. In addition, please see Note 12 to our Consolidated Financial Statements in Item 8 for information regarding the repayment of our credit line with Summit in connection with our sale of our Property.

#### *Liquidity*

At December 31, 2012, we had \$253,900 in cash and approximately \$298,600 of our credit line with Summit was available for future borrowing. Our net cash provided by operating activities in 2012 decreased by \$455,000 to \$17,900 as compared to 2011. For 2012, the primary components of working capital (exclusive of cash that was \$322,000 less at December 31, 2012 compared to December 31, 2011) that significantly affected operating cash flows are the following: (1) trade receivables, net were \$521,300 more at December 31, 2012 than at December 31, 2011 due primarily to increased gross sales activity and the timing of receiving payment; (2) obligations collateralized by those receivables and inventory were \$924,300 more at December 31, 2012 than at December 31, 2011 due primarily to higher borrowings under our line of credit with Summit to fund increased gross sales activity and trade promotions and a reduction in accounts payable and other accrued expenses; (3) inventory at December 31, 2012 was \$43,400 less than at December 31, 2011 due primarily to timing differences in the receipt of our inventory; and (4) accounts payable and other accrued expenses at December 31, 2012 were \$351,400 less than at December 31, 2011 due primarily to the timing of making payments and lower accruals for payroll and benefits, trade promotions and an insurance claim.

We anticipate that our existing cash, especially given the cash proceeds from the sale of our real estate assets, and our cash flow from operations, together with our current borrowing arrangements with Summit and Wells Fargo, will be sufficient to meet our cash requirements for the next 12 months. We expect to make capital expenditures of approximately \$150,000 for 2013 as a result of the sale of our real estate assets on February 1, 2013. Please see Note 12 to our Consolidated Financial Statements in Item 8 for information on the sale of our real estate assets.

### **ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.**

**Not applicable.**

**Table of Contents**

**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.**

**Report of Independent Registered Public Accounting Firm**

Board of Directors and Shareholders

Scott's Liquid Gold-Inc.

Denver, Colorado

We have audited the accompanying consolidated balance sheets of Scott's Liquid Gold-Inc. and subsidiaries (the Company) as of December 31, 2012 and 2011, and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the two years in the period ended December 31, 2012. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Scott's Liquid Gold-Inc. and subsidiaries as of December 31, 2012 and 2011, and the results of their operations and their cash flows for each of the two years in the period ended December 31, 2012, in conformity with accounting principles generally accepted in the United States of America.

/s/ EKS&H LLLP

March 29, 2013

Denver, Colorado

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

	<b>Year Ended December 31,</b>	
	<b>2012</b>	<b>2011</b>
Net sales	\$ 16,041,400	\$ 15,616,300
Operating costs and expenses:		
Cost of sales	9,074,700	8,553,500
Advertising	320,200	773,300
Selling	4,305,200	4,527,100
General and administrative	2,792,200	2,318,100
Loss on impairment of long-lived assets	286,900	0
Loss on impairment of assets held for sale	579,800	0
	17,359,000	16,172,000
Loss from operations	(1,317,600)	(555,700)
Rental and other income	240,400	159,200
Interest expense	(294,600)	(237,300)
Loss before income taxes	(1,371,800)	(633,800)
Income tax expense	0	0
Net loss	\$ (1,371,800)	\$ (633,800)
Net loss per common share :		
Basic	\$ (0.13)	\$ (0.06)
Diluted	\$ (0.13)	\$ (0.06)
Weighted average shares outstanding:		
Basic	10,934,945	10,898,800
Diluted	10,934,945	10,898,800

See accompanying notes to these Consolidated Financial Statements.

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

	December 31,	
	2012	2011
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 253,900	\$ 575,900
Trade receivables, net	969,200	447,900
Inventories, net	1,975,800	2,019,200
Prepaid expenses	139,100	133,400
<b>Total current assets</b>	<b>3,338,000</b>	<b>3,176,400</b>
Property, plant and equipment, net	467,400	10,632,100
Assets held for sale	8,907,600	0
Other assets	82,800	68,400
<b>Total assets</b>	<b>\$ 12,795,800</b>	<b>\$ 13,876,900</b>
<b>Liabilities and Shareholders' Equity</b>		
Current liabilities:		
Obligations collateralized by receivables and inventory	\$ 1,201,400	\$ 277,100
Accounts payable	1,371,600	1,442,700
Accrued payroll and benefits	509,200	579,200
Accrued property taxes	227,900	230,600
Other accrued expenses	19,700	227,300
Current maturities of long-term debt	352,600	340,800
<b>Total current liabilities</b>	<b>3,682,400</b>	<b>3,097,700</b>
Long-term debt, net of current maturities	3,010,700	3,363,400
<b>Total liabilities</b>	<b>6,693,100</b>	<b>6,461,100</b>
Commitments and contingencies		
Shareholders' equity:		
Common stock; \$0.10 par value, authorized 50,000,000 shares; issued and outstanding 10,937,000 shares (2012) and 10,907,000 shares (2011)	1,093,700	1,090,700
Capital in excess of par	5,502,600	5,446,900
Retained earnings (deficit)	(493,600)	878,200
<b>Total shareholders' equity</b>	<b>6,102,700</b>	<b>7,415,800</b>
<b>Total liabilities and shareholders' equity</b>	<b>\$ 12,795,800</b>	<b>\$ 13,876,900</b>

See accompanying notes to these Consolidated Financial Statements.

**Table of Contents****Consolidated Statements of Shareholders' Equity**

	Common Stock		Capital in Excess of Par	Retained Earnings (deficit)	Total
	Shares	Amount			
Balance, December 31, 2010	10,898,500	\$ 1,089,900	\$ 5,373,100	\$ 1,512,000	\$ 7,975,000
Stock-based compensation	0	0	72,800		72,800
Stock options exercised	8,500	800	1,000		1,800
Net loss				(633,800)	(633,800)
Balance, December 31, 2011	10,907,000	\$ 1,090,700	\$ 5,446,900	\$ 878,200	\$ 7,415,800
Stock-based compensation	0	0	53,600		53,600
Stock options exercised	30,000	3,000	2,100		5,100
Net loss				(1,371,800)	(1,371,800)
Balance, December 31, 2012	10,937,000	\$ 1,093,700	\$ 5,502,600	\$ (493,600)	\$ 6,102,700

See accompanying notes to these Consolidated Financial Statements.

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

	<b>Year Ended December 31,</b>	
	<b>2012</b>	<b>2011</b>
<b>Cash flows from operating activities:</b>		
Net loss	\$ (1,371,800)	\$ (633,800)
<b>Adjustment to reconcile net loss to net cash provided by operating activities:</b>		
Depreciation and amortization	420,300	502,300
Impairment of long-lived assets	286,900	0
Impairment on assets held for sale	579,800	0
Stock-based compensation	53,600	72,800
(Gain) loss on disposal of assets	(25,800)	3,000
<b>Change in operating assets and liabilities:</b>		
Trade receivables	(521,300)	388,500
Inventories	43,400	(337,700)
Prepaid expenses and other assets	(20,100)	68,600
Net proceeds on obligations collateralized by receivables and inventory	924,300	(63,800)
Accounts payable and accrued expenses	(351,400)	473,000
<b>Total adjustments to net loss</b>	<b>1,389,700</b>	<b>1,106,700</b>
<b>Net Cash Provided by Operating Activities</b>	<b>17,900</b>	<b>472,900</b>
<b>Cash flow from investing activities:</b>		
Proceeds from sale of property, plant and equipment	26,600	0
Purchase of property, plant and equipment	(30,700)	(49,400)
<b>Net Cash Used by Investing Activities</b>	<b>(4,100)</b>	<b>(49,400)</b>
<b>Cash flow from financing activities:</b>		
Principal payments on long-term debt	(340,900)	(330,100)
Proceeds from exercise of stock options	5,100	1,800
<b>Net Cash Used by Financing Activities</b>	<b>(335,800)</b>	<b>(328,300)</b>
<b>Net (Decrease) Increase in Cash and Cash Equivalents</b>	<b>(322,000)</b>	<b>95,200</b>
Cash and Cash Equivalents, beginning of year	575,900	480,700
Cash and Cash Equivalents, end of year	\$ 253,900	\$ 575,900
<b>Supplemental disclosures:</b>		
Cash paid during the period for interest	\$ 294,800	\$ 237,400

See accompanying notes to these Consolidated Financial Statements.

**Table of Contents**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

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

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

Scott's Liquid Gold-Inc. (a Colorado corporation) was incorporated on February 15, 1954. Scott's Liquid Gold-Inc. and its wholly-owned subsidiaries (collectively, the Company, we, our, or us) develop, manufacture, market and sell quality household and skin and hair care products. We are also an exclusive distributor in the United States of Montagne Jeunesse skin sachets and Batiste Dry Shampoo manufactured by two other companies. Our business is comprised of two segments, household products and skin and hair care products.

We have experienced significant losses over an extended number of years primarily attributable to sales declines and have used a significant amount of our cash reserves to fund operations and for debt service. To address these trends, we have implemented cost reduction initiatives, entered into financing agreements (please see Note 1(e) for information on our financing agreements) and continue to focus on existing and new product sales and distribution at improved margins to increase our cash provided by operations.

We anticipate that our existing cash, especially given the cash proceeds from the sale of our real estate assets, and our cash flow from operations, together with our current borrowing arrangements with Summit Financial Resources, L.P. (Summit) and Wells Fargo Bank, National Association (Wells Fargo) will be sufficient to meet our cash requirements for the next 12 months. We expect to make capital expenditures of approximately \$150,000 for 2013 as a result of the sale of our real estate assets on February 1, 2013. Please see Note 12 for information on the sale of our real estate assets.

(b) *Principles of Consolidation*

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

(c) *Use of Estimates*

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires us to make estimates and assumptions that affect the reported amounts in our financial statements of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates include, but are not limited to, the realization of deferred tax assets, reserves for slow moving and obsolete inventory, customer returns and allowances, coupon redemptions and stock-based compensation. Actual results could differ from our estimates.

(d) *Cash Equivalents*

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

(e) *Sale of Accounts Receivable*

On November 3, 2008, effective as of October 31, 2008, we entered into a financing agreement with Summit for the purpose of improving working capital. The financing agreement with Summit was amended on March 12, 2010, March 16, 2011 (effective March 1, 2011) and then again on June 29, 2012 (effective July 1, 2012). The agreement has a term that expires on January 1, 2014, but it may be renewed for additional 12 month periods unless either party elects to cancel in writing at least 60 days prior to January 1, 2014 and thereafter on the anniversary date of each 12 month period.





**Table of Contents**

The agreement provides for a factoring line up to \$1.5 million and is secured primarily by accounts receivable, inventory, any lease in which we are a lessor and all investment property and guarantees by our active subsidiaries. Under the agreement, Summit will make loans at our request and in its discretion based on: (i) its purchases of our receivables, with recourse against us, at an advance rate of 85% (or such other percentage determined by Summit in its discretion) and (ii) our inventory not to exceed certain amounts, including an aggregate maximum of \$500,000. Prior to the recent amendment on June 29, 2012, advances under the agreement had an interest rate of 1.5% over the prime rate (as published in The Wall Street Journal) for the accounts receivable portion of the advances and 4.0% over the prime rate for the inventory portion of the borrowings. The recent amendment reduced these interest rates to 1.0% over the prime rate for the accounts receivable portion and 2.5% over the prime rate for the inventory portion. Consequently, our interest cost adjusts with changes in the prime rate. At December 31, 2012, the prime rate was 3.25%.

In addition, prior to the recent amendment on June 29, 2012, there was an administrative fee of 1.0% per month on the average monthly outstanding loan on the receivable portion of any advance and 1.35% per month on the average monthly outstanding loan on the inventory portion of any advance. The recent amendment reduced these administrative fees to 0.85% per month on the average monthly outstanding loan on the receivable portion of any advance if the average quarterly loan in the prior quarter was less than or equal to \$1,000,000, and to 0.75% if the average quarterly loan in the prior quarter was greater than \$1,000,000 and to 1.0% per month on the average monthly outstanding loan on the inventory portion of any advance.

The agreement provides that neither we nor our active subsidiaries may engage in a change in control transaction without the prior written consent of Summit. Events of default include, but are not limited to, our failure to make a payment when due or a default occurring on any of our other indebtedness.

In 2012, we sold approximately \$11,415,500 of our accounts receivables to Summit for approximately \$9,703,200. As the advance rate on these accounts receivables was 85%, we retained an interest equal to 15% of those accounts receivables. At December 31, 2012, approximately \$298,600 of this credit line was available for future factoring of accounts receivable invoices. On February 4, 2013, we paid \$909,778 to Summit to repay the outstanding balance on our credit line and we have maintained a zero loan balance since that time.

We report these transactions using the authoritative guidance of the Financial Accounting Standards Board ( FASB ) as a secured borrowing rather than as a sale. As a result, affected accounts receivable are reported under Current Assets within our Consolidated Balance Sheets as Trade receivables, net. Similarly, the net liability owing to Summit appears as Obligations collateralized by receivables and inventory within the Current Liabilities section of our Consolidated Balance Sheets. Net proceeds received on obligations collateralized by receivables and inventory appear as cash provided by operating activities within our Consolidated Statements of Cash Flow.

On March 16, 2011, under a consent agreement from Summit, we entered into a financing agreement with Wells Fargo for the purpose of further lowering the cost of borrowing associated with the financing of our accounts receivable. Pursuant to this agreement, we may sell accounts receivables from our largest customer, Wal-Mart Stores, Inc. ( Wal-Mart ), at a discount to Wells Fargo; provided, however, that Wells Fargo may reject offers to purchase such receivables in its discretion. These receivables may be purchased by Wells Fargo at a cost to us equal to LIBOR plus 1.15% per annum. The LIBOR rate used depends on the days to maturity of the receivable sold, typically ranging from 102 to 105 days. At December 31, 2012, Wells Fargo used the 104-day LIBOR rate of 0.51%.

The agreement has no fixed termination date, but continues unless terminated by either party giving 30 days prior written notice to the other party. In 2012, we sold approximately \$3,641,900 of our relevant accounts receivable to Wells Fargo for approximately \$3,578,200. The difference between the invoiced amount of the receivable and the cash that we received from Wells Fargo is a cost to us. This cost is in lieu of any cash discount our customer would have been allowed and, thus, is treated in a manner consistent with standard trade discounts granted to our customers.

## **Table of Contents**

The reporting of the sale of accounts receivables to Wells Fargo is treated as a sale rather than as a secured borrowing. As a result, affected accounts receivables are relieved from the Company's financial statements upon receipt of the cash proceeds.

### *(f) Inventories*

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

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

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

### *(h) Financial Instruments*

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

The recorded amounts for cash and cash equivalents, receivables, other current assets, accounts payable and accrued expenses approximate fair value due to the short-term nature of these financial instruments. Our long-term debt bears interest at a fixed rate that adjusts annually on the anniversary date to the then prime rate. The carrying value of our long-term debt approximates fair value as of December 31, 2012.

### *(i) Long-Lived Assets and Assets Held for Sale*

We follow FASB authoritative guidance as it relates to the proper accounting treatment for the impairment or disposal of long-lived assets. This guidance requires that long-lived assets and certain identifiable intangibles be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

As of December 31, 2011, due to changes in the real estate market in Denver, Colorado, we conducted an evaluation into the fair value impairment of our property, plant and equipment with particular attention to our land and office, warehouse and manufacturing buildings (the Facilities ). The Facilities

**Table of Contents**

have an original cost of \$17,485,800 and a depreciated book value at December 31, 2011 of approximately \$10,068,900. We evaluated the value of the Facilities using both an income capitalization approach and a market value approach. This evaluation returned a range of fair value estimates between approximately \$10.1 million to \$10.6 million. Based upon this evaluation, we found there to be no impairment in the carrying values of our long-lived assets at December 31, 2011.

However, at September 30, 2012, due to recent developments in the commercial real estate market in which our Facilities are located, we found there to be an impairment of \$286,900 in the carrying values of our long-lived assets. We determined the impairment amount after concluding that the low end of the range of fair value estimates at September 30, 2012 should be \$9.5 million and the depreciated book value of the Facilities at September 30, 2012 was \$9,786,900.

The impact of the impairment appears on our Consolidated Statements of Operations as an expense of \$286,900 under Loss on impairment of long-lived assets and a reduction of \$286,900 to our Property, plant and equipment, net on our Consolidated Balance Sheets.

On November 5, 2012, pursuant to FASB authoritative guidance, we classified the Facilities as an asset held for sale. Upon classification as held for sale, the long-lived asset is measured at the lower of its carrying value or fair value less cost to sell, depreciation is ceased and the asset is separately presented on our Consolidated Balance Sheets. The impact of the classification as held for sale appears on our Consolidated Statements of Operations as an expense of \$579,800 under Loss on impairment of Assets Held for Sale, a reduction of \$8,907,600 to our Property, plant and equipment, net on our Consolidated Balance Sheets and a new asset of \$8,907,600 under Assets Held for Sale on our Consolidated Balance Sheets.

On February 1, 2013, we sold our Facilities for \$9.5 million. Please see Note 12 for information on the sale of our Facilities.

*(j) Income Taxes*

We follow FASB authoritative guidance for the accounting for income taxes which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences attributable to differences between the financial statement carrying amounts of assets and liabilities and their respective income tax bases. A valuation allowance is provided when it is more likely than not that some portion or all of a deferred tax asset will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the period in which related temporary differences become deductible. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled.

Taxes are reported based on tax positions that meet a more-likely-than-not standard and that are measured at the amount that is more-likely-than-not to be realized. Differences between financial and tax reporting which do not meet this threshold are required to be recorded as unrecognized tax benefits. We classify penalty and interest expense related to income tax liabilities as an income tax expense. There are no significant interest and penalties recognized in the statement of operations or accrued on the balance sheet.

*(k) Revenue Recognition*

Our revenue recognition policy is significant because the amount and timing of revenue is a key component of our results of operations. We follow guidance issued by the FASB, which requires that certain criteria be met in order to recognize revenue. If these criteria are not met, then the associated revenue is deferred until it is met. In our case, the criteria generally are met when we have an arrangement to sell a product, we have delivered the product in accordance with that arrangement, the sales price of the product is determinable and we believe that we will be paid for the sale.

**Table of Contents**

We establish reserves for customer returns of our products and customer allowances. We estimate these reserves based upon, among other things, an assessment of historical trends, information from customers and anticipated returns related to current sales activity. These reserves are established in the period of sale and reduce our revenue in that period.

Our reserve for customer allowances includes primarily reserves for trade promotions to support price features, displays and other merchandising of our products to our customers. The actual level of returns and customer allowances are influenced by several factors, including the promotional efforts of our customers, changes in mix of our customers, changes in the mix of the products we sell and the maturity of the product. We may change our estimates based on actual results and consideration of other factors that cause returns and allowances. In the event that actual results differ from our estimates, the results of future periods may be impacted.

We also establish reserves for coupons, rebates and certain other promotional programs for consumers. We estimate these reserves based upon, among other things, an assessment of historical trends and current sales activity. These reserves are recorded as a reduction of revenue at the later of the date at which the revenue is recognized or the date at which the sale incentive is offered.

We have also established an allowance for doubtful accounts. We estimate this allowance based upon, among other things, an assessment of the credit risk of specific customers and historical trends. We believe our allowance for doubtful accounts is adequate to absorb any losses which may arise. In the event that actual losses differ from our estimates, the results of future periods may be impacted.

At December 31, 2012 and December 31, 2011 approximately \$468,400 and \$636,500, respectively, had been reserved for as a reduction of accounts receivable, and approximately \$0 and \$85,000, respectively, had been reserved as current liabilities. Trade promotions to our customers and incentives such as coupons and rebates to the consumer are deducted from gross sales and totaled \$1,735,700 and \$1,315,200 for the years ended December 31, 2012 and 2011, respectively.

**(l) Advertising Costs**

Advertising costs are expensed as incurred.

**(m) Stock-based Compensation**

During 2012, we granted 100,000 options for shares of our common stock to an executive officer at a price of \$0.24 per share and 25,000 options for shares of our common stock to our controller at a price of \$0.17 per share. The options which vest ratably over forty-eight months, or upon a change in control, and which expire after five years, were granted at 120% of the market value as of the date of grant.

The weighted average fair market value of the options granted in the years ended December 31, 2012 and 2011 were estimated on the date of grant, using a Black-Scholes option pricing model with the following assumptions:

	2012	2011
Expected life of options (using the simplified method)	4.5 years	4.5 years
Average risk-free interest rate	0.8%	0.9%
Average expected volatility of stock	143%	98%
Expected dividend rate	None	None

**Table of Contents**

Compensation cost related to stock options recognized in operating results (included in general and administrative expenses) under authoritative guidance issued by the FASB was \$53,600 and \$72,800 in the twelve months ended December 31, 2012 and 2011, respectively. Approximately \$78,800 of total unrecognized compensation costs related to non-vested stock options is expected to be recognized over the next forty-eight months. In accordance with this same authoritative guidance, there was no tax benefit from recording the non-cash expense as it relates to the options granted to employees, as these were qualified stock options which are not normally tax deductible. With respect to the non-cash expense associated with the options granted to the non-employee directors, no tax benefit was recognized due to the existence of as yet unutilized net operating losses. At such time as these operating losses have been utilized and a tax benefit is realized from the issuance of non-qualified stock options, a corresponding tax benefit may be recognized.

**(n) Operating Costs and Expenses Classification**

Cost of sales includes costs associated with manufacturing and distribution including labor, materials, freight-in, purchasing and receiving, quality control, internal transfer costs, repairs, maintenance and other indirect costs, as well as warehousing and distribution costs. We classify shipping and handling costs comprised primarily of freight-out as selling expenses. Other selling expenses consist primarily of wages and benefits for sales and sales support personnel, travel, brokerage commissions and promotional costs, as well as certain other indirect costs. Shipping and handling costs totaled \$1,487,300 and \$1,514,400, for the years ended December 31, 2012 and 2011, respectively.

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

**(o) Recently Issued Accounting Pronouncements**

We have considered recently issued accounting pronouncements and do not believe that such pronouncements are of significance or potential significance to us.

**Note 2: Inventories**

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

	<b>2012</b>	<b>2011</b>
Finished goods	\$ 959,100	\$ 1,191,000
Raw materials	1,079,600	1,067,200
Inventory reserve for obsolescence	(62,900)	(239,000)
	\$ 1,975,800	\$ 2,019,200

**Table of Contents****Note 3: Property, Plant and Equipment**

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

	2012	2011
Land	\$ 0	\$ 1,091,500
Buildings	0	16,394,300
Production equipment	5,004,900	6,053,700
Office furniture and equipment	1,211,800	1,519,400
Other	34,200	34,200
	6,250,900	25,093,100
Less accumulated depreciation	(5,783,500)	(14,461,000)
	\$ 467,400	\$ 10,632,100

Depreciation expense for the years ended December 31, 2012 and 2011 was \$420,300 and \$476,700, respectively. Please see Note 12 for information on the sale of our land and buildings.

**Note 4: Debt**

On June 28, 2006, we entered into a loan with a fifteen year amortization with Citywide Banks (the Bank) for \$5,156,600 secured by the land, building and fixtures at our Denver, Colorado facilities. Interest on the bank loan is at the prime rate as published in The Wall Street Journal, adjusted annually each June. At December 31, 2012, this rate was 3.25%. The loan requires 180 monthly payments of approximately \$38,200 each. We believe, based upon both an income capitalization approach and a market value approach, that the real property assets securing the loan significantly exceed the principal amount outstanding under the loan agreement. Nevertheless, the loan agreement contains a number of covenants, including the requirement for us to maintain a current ratio through November 30, 2012 of at least 0.9:1.0 and thereafter of at least 1.0:1.0, and a ratio of consolidated long-term debt to consolidated net worth of not more than 1.0:1.0. These ratios are to be calculated in accordance with generally accepted accounting principles in the United States. We may not declare any dividends that would result in a violation of either of these covenants.

With regard to our current ratio, our loan agreement with the Bank was temporarily modified on August 10, 2012, to change our current ratio during the period from April 1, 2012 through November 30, 2012 to 0.9:1.0 from 1.0:1.0. We agreed to pay to the Bank a one-time modification fee of \$17,500. The modification was necessary because our current ratio decreased to below 1.0:1.0 during the second quarter of 2012. The modification enabled us to remain in compliance with the terms of the loan agreement with respect to the ratio through November 30, 2012 and avoid being deemed in default under the loan agreement through such date for failing to comply with the original current ratio requirement. At December 31, 2012, our current ratio was 0.9:1.0 and we were not in compliance with our current ratio covenant. However, our loan with the Bank was repaid in full at the closing of our real estate assets. Please see Note 12 for information on sale of our real estate assets on February 1, 2013.

Affirmative covenants in the loan agreement with the Bank included, among other things, compliance in all material respects with applicable laws and regulations and compliance with our agreements with other parties that materially affect our financial condition. Negative covenants in the loan agreement include, among other things, that without the consent of the Bank, we do not: (1) sell, lease or grant a security interest in our assets; (2) engage in any business activity substantially different than those in which we are presently engaged; (3) sell assets out of the ordinary course of business; or (4) purchase another entity or an interest in another entity.

Long-term debt at December 31 is presented below:

	2012	2011
Bank loan	\$ 3,363,300	\$ 3,704,200
Less current maturities	352,600	340,800

Long-term debt	\$ 3,010,700	\$ 3,363,400
----------------	--------------	--------------



**Table of Contents**

Maturities of long-term debt for the years 2013 through 2017 are \$352,600, \$364,400, \$376,600, \$388,900, \$402,200 and \$1,478,600 thereafter. Please see Note 12 for information on the repayment of our long-term debt on February 1, 2013.

Please see Note 1(e) for a discussion of our financing agreements with Summit and Wells Fargo. Note 1(e) also includes a discussion of the accounting treatment of the funds borrowed pursuant to these agreements.

**Note 5: Income Taxes**

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

	2012	2011
<b>Current provision (benefit):</b>		
Federal	\$ 0	\$ 0
State	0	0
<b>Total current provision (benefit)</b>	<b>0</b>	<b>0</b>
<b>Deferred provision (benefit):</b>		
Federal	(407,800)	(144,000)
State	(36,600)	(11,600)
Valuation allowance	444,400	155,600
<b>Total deferred provision (benefit)</b>	<b>0</b>	<b>0</b>
<b>Provision (benefit):</b>		
Federal	0	0
State	0	0
<b>Total provision (benefit)</b>	<b>\$ 0</b>	<b>\$ 0</b>

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

	2012	2011
Federal income tax at statutory rates	\$ (466,400)	\$ (213,800)
State income taxes, net of federal tax effect	(41,900)	(19,200)
Change in unrecognized benefit	24,900	67,900
Other	39,000	9,500
<b>Total</b>	<b>(444,400)</b>	<b>(155,600)</b>
Change in valuation allowance	444,400	155,600
<b>Provision for income taxes</b>	<b>\$ 0</b>	<b>\$ 0</b>

**Table of Contents**

Deferred income taxes are based on estimated future tax effects of differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amount used for income tax purposes given the provision of enacted tax laws. The net deferred tax assets and liabilities as of December 31, 2012 and 2011 are comprised of the following:

	2012	2011
<b>Deferred tax assets:</b>		
Net operating loss carryforwards	\$ 4,531,300	\$ 3,988,700
Tax credit and other carryforwards	255,200	255,200
Trade receivables	20,900	22,600
Inventories	16,600	93,900
Accrued vacation	157,100	184,500
Other	44,300	38,100
Total deferred taxes	5,025,400	4,583,000
 <b>Deferred tax liability:</b>		
Accumulated depreciation for tax purposes	(813,400)	(815,400)
Total deferred tax liabilities	(813,400)	(815,400)
Net deferred tax asset, before allowance	4,212,000	3,767,600
Valuation allowance	(4,212,000)	(3,767,600)
Net deferred tax asset	\$ 0	\$ 0

At December 31, 2012, we had federal net operating loss carryforwards of approximately \$11,721,300 and federal tax credit carryforwards related to research and development efforts of approximately \$255,200, both of which expire over a period ending in 2032. State tax loss carryforwards at December 31, 2012 are approximately \$17,870,100 expiring over a period ending in 2032.

A valuation allowance was established due mainly to the uncertainty relating to the future utilization of net operating loss carryforwards. The valuation allowance was further increased by \$251,100 and \$155,600 for 2012 and 2011, respectively, primarily related to uncertainty as to realization of our operating losses and tax credits for these years. The amount of the deferred tax assets considered realizable could be adjusted in the future based upon changes in circumstances that result in a change in our assessment of our ability to realize those deferred tax assets through the generation of taxable income or other tax events.

We adhere to the authoritative guidance with respect to accounting for uncertainty in income taxes. This guidance prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. It requires that we recognize in our consolidated financial statements, only those tax positions that are more-likely-than-not of being sustained as of the adoption date, based on the technical merits of the position. As a result of the implementation of this guidance, each year we perform a comprehensive review of our material tax positions.

As a result of this review, we identified certain deferred tax assets that need to be adjusted. As of December 31, 2012 and December 31, 2011, we identified approximately \$412,100 and \$345,000 of related tax positions, respectively.

	2012	2011
Balance at January 1,	\$ 345,000	\$ 161,800
Additions based on tax positions related to current year	67,100	198,000
Reductions for tax positions of prior years	0	(14,800)
Balance at December 31,	\$ 412,100	\$ 345,000

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

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

**Table of Contents**

Our policy is to recognize interest and penalties related to uncertain tax benefits in income tax expense. As a result of our net operating loss carryforward position, we have no accrued interest or penalties related to uncertain tax positions as of December 31, 2012 or December 31, 2011.

We and our subsidiaries are subject to the following material taxing jurisdictions: United States and Colorado. The tax years that remain open to examination by the Internal Revenue Service are 2009 through 2012. However, due to our net operating loss carryforwards from prior periods, the Internal Revenue Service could potentially review the losses back to 2000. The tax years that remain open to examination by the state of Colorado are 2008 through 2012.

**Note 6: Shareholders Equity**

In 1997, an incentive stock option plan was adopted for our employees. This plan expired on November 7, 2007. Accordingly, no shares are available for the grant of options under that plan. In 1998 and 2005, stock option plans for our employees, officers and directors were adopted. The 1998 plan expired on November 27, 2008. Accordingly no shares are available for the grant of options under that plan.

At the Annual Shareholders Meeting in May 2011, shareholders approved an amendment to the 2005 Plan to increase the number of shares issuable under the plan from 1,500,000 shares to a total of 3,000,000 shares. Options granted before May 2011 are granted at not less than current market price of the stock on the date of grant and are exercisable from five to ten years from the grant date. Options granted after May 2011, pursuant to the plan amendment in May, are required to be granted at not less than the higher of (1) 120% of current market price on the date of grant or (2) the average of market price over the prior 30 trading days. Further, pursuant to the amendment the number of options granted to an executive officer or director cannot exceed 200,000, except to the extent such limit had already been exceeded at the time of the amendment. The options granted in 2012 and 2011 are vested each month over a four-year period or upon a change in control.

	1997 Plan		1998 Plan		2005 Plan	
	Number of Shares	Average Option Price Per Share	Number of Shares	Average Option Price Per Share	Number of Shares	Average Option Price Per Share
Maximum number of shares under the plans	300,000		1,100,000		3,000,000	
Outstanding, December 31, 2010	240,500	\$ 0.82	296,900	\$ 0.71	1,396,150	\$ 0.25
Granted in 2011	0	0	0	0	30,000	0.37
Exercised	0	0	0	0	(8,500)	0.21
Cancelled/Expired	0	0	0	0	0	0
Outstanding, December 31, 2011	240,500	\$ 0.82	296,900	\$ 0.71	1,417,650	\$ 0.25
Granted in 2012	0		0		125,000	0.23
Exercised	0		0		(30,000)	0.17
Cancelled/Expired	(240,500)	\$ 0.82	(172,900)	\$ 0.71	(249,300)	0.42
Outstanding, December 31, 2012	0		124,000		1,263,350	\$ 0.22
Available for issuance, December 31, 2012	None		None		(a)1,570,650	

- (a) Options available under the 2005 plan are limited by the amount of options outstanding under the 1997 and 1998 Plans. As the options outstanding under these earlier plans expire, the number of shares available for issuance under the 2005 Plan will increase accordingly.

**Table of Contents**

A summary of additional information related to the options outstanding as of December 31, 2012 is as follows:

Range of Exercise Prices	Number Outstanding	Options Outstanding and Exercisable Weighted Average Remaining Contractual Life	Exercise Price
\$0.17 \$0.82	1,387,350	2.1 years	\$ 0.25
Total	1,387,350	2.1 years	\$ 0.25

We have an Employee Stock Ownership Plan ( Plan ) to provide retirement benefits for our employees. The Plan is designed to invest primarily in our common stock and is non-contributory on the part of our employees. Contributions to the Plan are discretionary as determined by our Board of Directors. We expense the cost of contributions to the Plan. No contributions were made to the Plan in 2012 or 2011.

**Note 7: Earnings per Share**

We present basic and diluted earnings or loss per share in accordance with authoritative guidance which establishes standards for computing and presenting basic and diluted earnings per share. Per share data is determined by using the weighted average number of common shares outstanding. Common equivalent shares are considered only for diluted earnings per share, unless considered anti-dilutive. Common equivalent shares, determined using the treasury stock method, result from stock options with exercise prices that are below the average market price of the common stock.

The potentially dilutive securities are comprised of outstanding stock options of 1,387,350 and 1,955,050 at December 31, 2012 and 2011, respectively, a decrease of 567,700 or 29%. This decrease is due primarily to stock options expiring as well as a more limited number of stock options being exercised.

A reconciliation of the weighted average number of common shares outstanding for the years ended December 31 is as follows:

	2012	2011
Common shares outstanding, beginning of the year	10,907,000	10,898,500
Weighted average common shares issued	27,945	300
Weighted average number of common shares outstanding	10,934,945	10,898,800
Dilutive effect of common share equivalents	0	0
Diluted weighted average number of common shares outstanding	10,934,945	10,898,800

We have authorized 20,000,000 shares of preferred stock issuable in one or more series, none of which are issued or outstanding as of December 31, 2012.

Stock options outstanding which have been excluded from diluted shares outstanding due to their antidilutive effect totaled 1,387,350 at December 31, 2012 and 1,955,050 at December 31, 2011.

**Note 8: Segment Information**

We operate in two different segments: household products and skin and hair care products. Our products are sold nationally and internationally (primarily Canada), directly through our sales force and indirectly through independent brokers, to mass merchandisers, drugstores, supermarkets, hardware stores and other retail outlets and to wholesale distributors. Management has chosen to organize our business around these segments based on differences in the products sold.

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

Accounting policies for our segments are the same as those described in Note 1. We evaluate segment performance based on segment income or loss before income taxes.

**Table of Contents**

The following provides information on our segments as of and for the years ended December 31:

	2012		2011	
	Household Products	Skin and Hair Care Products	Household Products	Skin and Hair Care Products
Net sales to external customers	\$ 4,895,600	\$ 11,145,800	\$ 5,941,100	\$ 9,675,200
(Loss) income before income taxes	\$ (1,985,600)	\$ 613,800	\$ (934,500)	\$ 300,700
Identifiable assets	\$ 2,388,200	\$ 3,905,600	\$ 2,376,700	\$ 3,549,400

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

	2012	2011
Net sales to external customers	\$ 16,041,400	\$ 15,616,300
(Loss) income before income taxes	\$ (1,371,800)	\$ (633,800)
Consolidated (loss) income before income taxes	\$ (1,371,800)	\$ (633,800)
Identifiable assets	\$ 6,508,800	\$ 5,926,100
Corporate assets	6,287,000	7,950,800
Consolidated total assets	\$ 12,795,800	\$ 13,876,900

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

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

	2012	2011
United States	\$ 15,975,800	\$ 15,485,300
Foreign countries	65,600	131,000
Total net sales	\$ 16,041,400	\$ 15,616,300

In 2012 and 2011, Wal-Mart accounted for approximately \$3,577,800 and \$4,165,000, respectively, of our consolidated net sales, Ulta Salon, Cosmetics & Fragrance, Inc. ( Ulta ) accounted for approximately \$1,742,000 and \$1,188,600, of our consolidated net sales, respectively and Walgreens Co. ( Walgreens ) accounted for approximately \$1,110,500 and \$1,818,600 of our consolidated net sales, respectively. We sell both household products and skin and hair care products to Wal-Mart, but we sell only skin and hair care products to Ulta and Walgreens. These customers are not related to us.

The outstanding trade receivables from Wal-Mart accounted for 8.7% and 15.0% of our total trade receivables at December 31, 2012 and 2011, respectively. The outstanding trade receivables from Ulta accounted for 19.4% and 9.9% of our total trade receivables at December 31, 2012 and 2011, respectively. The outstanding trade receivables from Walgreens accounted for 15.0% and 10.5% of our total trade receivables at December 31, 2012 and 2011, respectively. A loss of one or more of these customers could have a material adverse effect on us because it is

uncertain whether our consumer base served by these customers would purchase our products at other retail outlets. No long-term contracts exist between us and these customers or any other customer.

**Note 9: Retirement Plans**

We have a 401(k) Profit Sharing Plan ( 401(k) Plan ) covering our full-time employees who have completed four months of service as defined in the 401(k) Plan, and are age 18 or older. Participants may



**Table of Contents**

defer up to 75% of their compensation up to the maximum limit determined by law. We may make discretionary matching contributions up to a maximum of 6% of each participant's compensation, but only for those employees earning no more than \$35,000 annually. Additionally, we can make discretionary profit sharing contributions to eligible employees. Participants are always fully vested in their contributions, matching contributions and allocated earnings thereon. Vesting in our profit sharing contribution is based on years of service, with a participant fully vested after five years. Our Company matching contributions totaled \$2,500 and \$2,900, in 2012 and 2011, respectively. We have made no discretionary profit sharing contributions in 2012 and 2011.

**Note 10. Commitments and Contingencies***Leases*

We have entered into various operating lease agreements, primarily for office equipment. Annual rental expense under these leases totaled \$77,400 and \$72,800, in 2012 and 2011, respectively. Minimum annual rental payments under noncancellable operating leases are approximately \$69,100, \$45,600 and \$5,500 for the years ending December 31, 2013, 2014 and 2015, respectively. Presently we have no lease commitments beyond 2015.

In October 2009, we entered into a five-year operating lease agreement for one floor of our five-story office building to an established subsidiary of an international company. We began to receive rent payments in November 2009 that will continue through October 2014. These rent payments include annual rental escalations of between 3.7% and 4.2%. In August 2010, we entered into a two-year lease for one-half of a floor of our office building to an unrelated third party. We began to receive rent payments in February 2011. However, these payments stopped at the end of December 2011 when the tenant vacated the space due to financial difficulties. In September of 2012, we entered into a lease expiring December 31, 2015 for one-half of a floor of our office building. We began to receive rent payments in November 2012. In December of 2012, we entered into a lease expiring March 31, 2016 for one of our warehouse buildings. Rent payments are not due until May 2013. In connection with the sale of our real estate assets, we assigned the foregoing leases to the purchaser. Please see Note 12 for information on the sale of our real estate assets.

**Note 11. Valuation and Qualifying Accounts**

	Balance at beginning of year	Additions charged to expense	Deductions	Balance at end of year
Year ended December 31, 2011				
Returns and allowances and doubtful accounts reserve	\$ 364,300	\$ 1,618,900	\$ 1,346,700	\$ 636,500
Year ended December 31, 2012				
Returns and allowances and doubtful accounts reserve	\$ 636,500	\$ 1,978,800	\$ 2,146,900	\$ 468,400

**Note 12. Subsequent Event**

On February 1, 2013, we consummated the sale of our real estate assets located at 4880 Havana Street, Denver, Colorado, consisting of approximately 10.8 acres of land improved with four buildings containing approximately 241,684 square feet of office, warehouse, and manufacturing space, with associated improvements and personal property, and adjacent vacant land of approximately 5.5 acres (together, the Property). We sold the Property for a purchase price of \$9,500,000 and incurred selling expenses of \$579,800, including \$570,000 for real estate brokerage commissions.

---

**Table of Contents**

In connection with the sale, we leased back from the purchaser approximately 16,078 square feet of office space (the Office Lease ) and approximately 113,620 square feet of manufacturing and warehouse space (the Warehouse Lease ) currently used by us. Each of the Office Lease and the Warehouse Lease has an initial term of three years, with options to extend the term for two additional terms of three years each. Rent for the Office Lease is \$13.00 per square foot per annum, with annual 3% increases. Rent for the Warehouse Lease is \$3.25 per square foot per annum, with annual 3% increases, and we will pay an additional \$1.25 per square foot per annum as our share of the purchaser's operating expenses under the Warehouse Lease (including taxes, insurance and common area maintenance charges). If certain uncontrollable operating expenses increase by more than 5% per year, our share of operating expenses under the Warehouse Lease may be increased.

As of the date of the closing, the principal and interest balance on our long-term debt secured by the Property with the Bank was \$3,373,961. This debt was repaid in full at closing. We also paid approximately \$202,000 at closing for real estate property taxes for 2012. In addition, on February 4, 2013, we paid \$909,778 to Summit to repay the outstanding balance on our credit line with Summit and we have maintained a zero loan balance since that time. We made this payment to reduce our interest costs. Please see Note 1(e) for a discussion of our financing agreement with Summit. Also, in February 2013, we paid certain other financial obligations to suppliers and vendors in the amount of approximately \$960,000 and we incurred approximately \$150,000 in capital expenditures as a result of the sale of our Property. We estimate that our remaining cash from the sale of the Property after the payment of all of the foregoing expenses was approximately \$3.3 million.

**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.**

None.

**ITEM 9A. CONTROLS AND PROCEDURES.**

**Disclosure Controls and Procedures**

As of December 31, 2012, we conducted an evaluation, under the supervision and with the participation of the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective as of December 31, 2012.

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

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

Management, including the Chief Executive Officer and Chief Financial Officer, has conducted an evaluation of the effectiveness of the Company's internal control over financial reporting as of December 31, 2012, based on the criteria for effective internal control described in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on its assessment, management concluded that the Company's internal control over financial reporting was effective as of December 31, 2012.

**Table of Contents**

This report does not include an attestation report of our independent registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by our independent registered public accounting firm pursuant to rules of the Securities and Exchange Commission that permits us to provide only management's report in this Report.

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

**Changes in Internal Control over Financial Reporting**

There was no change in our internal control over financial reporting during the quarter ended December 31, 2012 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**ITEM 9B. OTHER INFORMATION.**

None.

**PART III**

For Part III, the information set forth in our definitive Proxy Statement for our Annual Meeting of Shareholders to be filed within 120 days after December 31, 2012, hereby is incorporated by reference into this Report.

**ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE.**

**ITEM 11. EXECUTIVE COMPENSATION.**

**ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS.**

**ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE.**

**ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES.**

**PART IV**

**ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES.**

**Exhibits**

See Exhibit Index at page 40 of this Report

**Consolidated Financial Statements:**

Report of Independent Registered Public Accounting Firm

Consolidated Statements of Operations for the years ended December 31, 2012 and 2011

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

Consolidated Balance Sheets as of December 31, 2012 and 2011

Consolidated Statements of Shareholders' Equity for the years ended December 31, 2012 and 2011

Consolidated Statements of Cash Flows for the years ended December 31, 2012 and 2011

Notes to Consolidated Financial Statements

**Table of Contents**

**SIGNATURES**

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

SCOTT S LIQUID GOLD-INC.,

a Colorado corporation

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

By: /s/ Barry J. Levine  
 Barry J. Levine, Treasurer, Chief Financial Officer  
  
 and Chief Operating Officer  
 (Principal Financial and Accounting Officer)

Date: March 29, 2013

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

Date	Name and Title	Signature
March 29, 2013	Mark E. Goldstein, Director, President and Chief Executive Officer	
March 29, 2013	Jeffrey R. Hinkle, Director	/s/ Mark E. Goldstein
March 29, 2013	Dennis H. Field, Director	Mark E. Goldstein, for himself and as
March 29, 2013	Jeffry B. Johnson, Director	Attorney-in-Fact for the named directors
March 29, 2013	Gerald J. Laber, Director	who constitute all of the members of the
March 29, 2013	Phil Neri, Director	the Board of Directors and for the named officers
March 29, 2013	Barry J. Levine, Treasurer, Chief Financial Officer and Chief Operating Officer	

**Table of Contents**

EXHIBIT INDEX

**Exhibit**

**Number**

**Document**

3.1	Restated Articles of Incorporation, as amended and restated through May 1, 1996, incorporated by reference to Exhibit 3.1 of our Annual Report on Form 10-KSB for the year ended December 31, 2007.
3.2	Bylaws, as amended through July 13, 2011, incorporated by reference to Exhibit 99.1 of our Current Report on Form 8-K filed on July 19, 2011.
4.1	Change in Terms Agreement with Citywide Banks, dated June 28, 2006, between us and Citywide Banks, incorporated by reference to Exhibit 10.1 of our Current Report on Form 8-K filed on June 30, 2006.
4.2	Business Loan Agreement, dated June 28, 2006, between us and Citywide Banks, incorporated by reference to Exhibit 10.2 of our Current Report on Form 8-K filed on June 30, 2006.
4.3	Addendum to Loan Documents, dated June 28, 2006, incorporated by reference to Exhibit 10.3 of our Current Report on Form 8-K filed on June 30, 2006.
4.4	Promissory Note dated June 7, 2006 by us to Citywide Banks; Deed of Trust dated June 7, 2006 among us, Citywide Banks and the Public Trustee of the City and County of Denver, Colorado; Assignment of Rents dated June 7, 2006 between us and Citywide Banks; letter agreement dated June 7, 2006 regarding the change in the amount under the existing bank line of credit with Citywide Banks, incorporated by reference to Exhibit 10.0 of our Current Report on Form 8-K filed on June 12, 2006.
4.5	Second Amendment to Shareholder Rights Agreement, dated as of January 6, 2012, between the Company and Broadridge Corporate Issuer Solutions, Inc., as Rights Agent, incorporated by reference to Exhibit 4.1 of our Current Report on Form 8-K filed with the Commission on January 10, 2012.
10.1*	Scott's Liquid Gold-Inc. Health and Accident Plan, Plan Document and Summary Plan Description Amended and Restated Effective October 1, 2003 incorporated by reference to Exhibit 10.1 of our Annual Report on Form 10-K for the year ended December 31, 2004.
10.2	Scott's Liquid Gold & Affiliated Companies Employee Benefit Health And Welfare Plan Amendment #1-2004 incorporated by reference to Exhibit 10.2 of our Annual Report on Form 10-K for the year ended December 31, 2004.
10.3*	Form of Indemnification Agreement for executive officers and directors.
10.4	Agreement dated as of May 3, 2005 between Montagne Jeunesse International Ltd. and Neoteric Cosmetics, Inc., incorporated by reference to Exhibit 10.2 of our Quarterly Report on Form 10-Q for the quarter ended March 31, 2005.
10.5*	Scott's Liquid Gold-Inc. Employee Stock Ownership Plan and Trust Agreement, Amended and Restated Effective January 1, 2001; and Second Amendment to Scott's Liquid Gold-Inc. Employee Stock Ownership Plan, effective as of January 1, 2003, incorporated by reference to Exhibit 10.6 of our annual Report on Form 10-K for the year ended December 31, 2003.
10.6*	Third Amendment to Scott's Liquid Gold-Inc. Employee Stock Ownership Plan, effective March 28, 2005, incorporated by reference to Exhibit 10.1 of our Quarterly Report on Form 10-Q for the quarter ended March 31, 2005.
10.7*	Scott's Liquid Gold-Inc. 1998 Stock Option Plan, incorporated by reference to Exhibit 4.3 of our Registration Statement No. 333-51710, filed with the Commission on December 12, 2000.
10.8*	2005 Stock Incentive Plan, as amended, incorporated by reference to Exhibit 4 of our Registration Statement No. 333-156191, filed with the Commission on December 16, 2008.
10.9	Product Development, Production and Marketing Agreement with Modec, Inc. dated April 4, 2006, incorporated by reference to Exhibit 10.1 of our Quarterly Report on Form 10-Q for the quarter ended June 30, 2006.

**Table of Contents**

**Exhibit**

<b>Number</b>	<b>Document</b>
10.10	Amendment to Modec Agreement dated November 9, 2007, incorporated by reference to Exhibit 10.12 of our Annual Report on Form 10-KSB for the year ended December 31, 2007.
10.11	Form of 1997 Stock Option Plan Incentive Stock Option Agreement, incorporated by reference to Exhibit 10.2 of our Quarterly Report on Form 10-QSB for the quarter ended March 31, 2007.
10.12	Form of 1998 Stock Option Plan Incentive Stock Option Agreement, incorporated by reference to Exhibit 10.3 of our Quarterly Report on Form 10-QSB for the quarter ended March 31, 2007.
10.13	Form of 2005 Stock Option Plan Incentive Stock Option Agreement, incorporated by reference to Exhibit 10.4 of our Quarterly Report on Form 10-QSB for the quarter ended March 31, 2007.
10.14	Form of 1998 Stock Option Plan Nonqualified Stock Option Agreement, incorporated by reference to Exhibit 10.5 of our Quarterly Report on Form 10-QSB for the quarter ended March 31, 2007.
10.15	Form of 2005 Stock Incentive Plan Nonqualified Stock Option Agreement, incorporated by reference to Exhibit 10.6 of our Quarterly Report on Form 10-QSB for the quarter ended March 31, 2007.
10.16	Financing Agreement and Addendum to Financing Agreement, both dated October 31, 2008, between Summit Financial Resources, L.P. and the Company, incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed with the Commission on November 4, 2008.
10.17	Guarantees, dated October 31, 2008, by SLG Plastics, Inc. Advertising Promotions Incorporated, Colorado Product Concepts, Inc., Neoteric Cosmetics, Inc., and SLG Chemicals, Inc., incorporated by reference to Exhibit 10.2 of the Company's Current Report on Form 8-K filed with the Commission on November 4, 2008.
10.18	First Amendment to Financing Agreement dated March 12, 2009 between Summit Financial Resources, L.P. and the Company, incorporated by reference to Exhibit 10.18 of our Annual Report on Form 10-K for the year ended December 31, 2008.
10.19	Second Amended and Restated Financing Agreement and Addendum to dated March 16, 2011 between Summit Financial Resources, L.P. and the Company, incorporated by reference to Exhibit 10.19 of the Company's Annual Report on Form 10-K filed with the Commission on March 29, 2011.
10.20	Receivables Purchase Agreement dated March 16, 2011 between Wells Fargo Bank, National Association and Scott's Liquid Gold, Inc., incorporated by reference to Exhibit 10.20 of the Company's Annual Report on Form 10-K filed with the Commission on March 29, 2011.
10.21	Receivables Purchase Agreement dated March 16, 2011 between Wells Fargo Bank, National Association and Neoteric Cosmetics, Inc., incorporated by reference to Exhibit 10.21 of the Company's Annual Report on Form 10-K filed with the Commission on March 29, 2011.
10.22**	Distribution Agreement, dated January 1, 2012, between Church & Dwight UK Limited and Neoteric Cosmetics, Inc.
10.23	First Amendment to the Second Amended and Restated Financing Agreement, dated June 29, 2012, between Summit Financial Resources, L.P. and the Company, incorporated by reference to Exhibit 99.1 of the Current Report on Form 8-K filed with the Commission on July 2, 2012.

**Table of Contents**

**Exhibit**

<b>Number</b>	<b>Document</b>
10.24	Purchase and Sale Agreement, dated November 21, 2012, between the Company and Havana Gold, LLC.
10.25	Real Property Lease (Warehouse Lease), dated February 1, 2013, between the Company and Havana Gold, LLC.
10.26	Real Property Lease (Office Lease), dated February 1, 2013, between the Company and Havana Gold, LLC.
21	List of Subsidiaries, incorporated by reference to Exhibit 21 of the Company's Annual Report on Form 10-K filed with the Commission on March 29, 2011.
23	Consent of EKS&H LLLP.
24	Powers of Attorney.
31.1	Rule 13a-14(a) Certification of the Chief Executive Officer.
31.2	Rule 13a-14(a) Certification of the Chief Financial Officer.
32.1***	Section 1350 Certification.
101.INS****	XBRL Instance Document.
101.SCH****	XBRL Taxonomy Extension Schema Document.
101.CAL****	XBRL Taxonomy Extension Calculation Linkbase Document.
101.LAB****	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE****	XBRL Taxonomy Extension Presentation Linkbase Document.

\* Management contract or compensatory plan or arrangement.

\*\* Confidential portions of this agreement have been redacted pursuant to a confidential treatment request filed separately with the Commission.

\*\*\* Furnished, not filed.

\*\*\*\* XBRL (Extensible Business Reporting Language) information is furnished and not filed or a part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, is deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, and is otherwise not subject to liability under these sections.