

SHERWIN WILLIAMS CO

Form 10-K

February 28, 2008

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

FORM 10-K

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

For the fiscal year ended December 31, 2007

Commission file number 1-04851

THE SHERWIN-WILLIAMS COMPANY
(Exact name of registrant as specified in its charter)

OHIO
(State or other jurisdiction of incorporation or organization)
34-0526850
(I.R.S. Employer Identification No.)

101 Prospect Avenue, N.W., Cleveland, Ohio
(Address of principal executive offices)

44115-1075
(Zip Code)

(216) 566-2000
Registrant's telephone number, including area code

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, Par Value \$1.00	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

None

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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 Section 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 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 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 the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

		Non-accelerated filer <input type="checkbox"/>	
	(Do not check if a smaller reporting		Smaller reporting
Large accelerated filer <input checked="" type="checkbox"/>	Accelerated filer <input type="checkbox"/>	company)	company <input type="checkbox"/>

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

At January 31, 2008, 122,804,070 shares of common stock were outstanding, net of treasury shares. The aggregate market value of common stock held by non-affiliates of the Registrant at June 29, 2007 was \$8,657,799,790 (computed by reference to the price at which the common stock was last sold on such date).

DOCUMENTS INCORPORATED BY REFERENCE

Portions of our Annual Report to Shareholders for the fiscal year ended December 31, 2007 (2007 Annual Report) are incorporated by reference into Parts I, II and IV of this report.

Portions of our Proxy Statement for the 2008 Annual Meeting of Shareholders (Proxy Statement) to be filed with the Securities and Exchange Commission within 120 days of our fiscal year ended December 31, 2007 are incorporated by reference into Part III of this report.

THE SHERWIN-WILLIAMS COMPANY

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PART I

ITEM 1. BUSINESS

Introduction

The Sherwin-Williams Company, founded in 1866 and incorporated in Ohio in 1884, is engaged in the development, manufacture, distribution and sale of paint, coatings and related products to professional, industrial, commercial and retail customers primarily in North and South America with additional operations in the United Kingdom, Europe, India and China. Our principal executive offices are located at 101 Prospect Avenue, N.W., Cleveland, Ohio 44115-1075, telephone (216) 566-2000. As used in this report, the terms Sherwin-Williams, Company, we and our mean The Sherwin-Williams Company and its consolidated subsidiaries unless the context indicates otherwise.

Available Information

We make available free of charge on or through our website our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K, and amendments to these reports, as soon as reasonably practicable after we electronically file such material with, or furnish such material to, the Securities and Exchange Commission. You may access these documents on the Investor Relations page of our website at www.sherwin.com.

We also make available free of charge on our website our Corporate Governance Guidelines, our Director Independence Standards, our Business Ethics Policy and the charters of our Audit Committee, our Compensation and Management Development Committee, and our Nominating and Corporate Governance Committee. You may access these documents in the Corporate Governance section on the Investor Relations page of our website at www.sherwin.com. Any person may receive a copy of any of these documents free of charge by writing to us at The Sherwin-Williams Company, 101 Prospect Avenue, N.W., Cleveland, Ohio 44115, Attention: Investor Relations.

Basis of Reportable Segments

We report our segment information in the same way that management internally organizes our business for assessing performance and making decisions regarding allocation of resources in accordance with Statement of Financial Accounting Standards (FAS) No. 131, Disclosures about Segments of an Enterprise and Related Information. Effective January 1, 2006, we changed our reportable operating segments based on organizational changes in our management structure. Our reportable operating segments now are: Paint Stores Group, Consumer Group and Global Group (collectively, the Reportable Operating Segments). The Global Group consists of certain business units with foreign or worldwide operations that were reported in the previous Paint Stores, Consumer, Automotive Finishes and International Coatings segments. Amounts reported prior to January 1, 2006 have been reclassified to conform to the current presentation. Factors considered in determining our Reportable Operating Segments include the nature of the business activities, existence of managers responsible for the operating activities and information presented to our Board of Directors. We report all other business activities and immaterial operating segments that are not reportable in the Administrative segment.

The Company's chief operating decision maker (CODM) has been identified as the Chief Executive Officer because he has final authority over performance assessment and resource allocation decisions. Because of the diverse operations of the Company, the CODM regularly receives discrete financial information about each Reportable Operating Segment as well as a significant amount of additional financial information about certain divisions, business units or subsidiaries of the Company. The CODM uses all such financial information for performance assessment and resource

allocation decisions. The CODM evaluates the performance of and allocates resources to the Reportable Operating Segments based on profit or loss and cash generated from operations before income taxes. The accounting policies of the Reportable Operating Segments are the same as those described in Note 1 of the Notes to Consolidated Financial Statements on pages 47 through 51 of our 2007 Annual Report, which is incorporated herein by reference.

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Paint Stores Group

The Paint Stores Group consisted of 3,325 company-operated specialty paint stores and seven manufacturing/distribution facilities in the United States, Canada, Jamaica, Virgin Islands and Puerto Rico at December 31, 2007. Each store in this segment is engaged in the related business activity of selling paint, coatings and related products to end-use customers. The acquisitions of M.A. Bruder & Sons, Incorporated and Columbia Paint & Coatings Co. are included in this segment. The Paint Stores Group markets and sells Sherwin-Williams® branded architectural paint and coatings, industrial and marine products, original equipment manufacturer (OEM) product finishes and related items. These products are produced by manufacturing facilities in the Paint Stores, Consumer and Global Groups. In addition, each store sells selected purchased associated products. During 2007, this segment acquired 172 stores and opened 107 net new stores, consisting of 81 stores in the United States, 18 in the Caribbean region and 8 in Canada. In 2006, there were 117 net new stores opened (113 in the United States). In 2005, there were 95 net new stores opened (88 in the United States). The loss of any single customer would not have a material adverse effect on the business of this segment.

Consumer Group

The Consumer Group develops, manufactures and distributes a variety of paint, coatings and related products to third party customers and the Paint Stores Group primarily in the United States and Canada. The acquisitions of the brand names, formulas and patents of the VHT® brand paint line and Life Shield Engineered Systems, LLC in 2007 are included in this segment. Approximately 56 percent of the total sales of the Consumer Group in 2007, including inter-segment transfers, represented products sold through the Paint Stores Group. Sales and marketing of certain controlled brand and private labeled products is performed by a direct sales staff. The products distributed through third party customers are intended for resale to the ultimate end-user of the product. The Consumer Group had sales to certain customers that, individually, may be a significant portion of the sales of the segment. However, the loss of any single customer would not have a material adverse effect on the overall profitability of the segment. This segment incurred most of the Company's capital expenditures related to ongoing environmental compliance measures.

Global Group

The Global Group develops, licenses, manufactures, distributes and sells a variety of architectural paint and coatings, industrial and marine products, automotive finishes and refinish products, OEM coatings and related products in North and South America, the United Kingdom, Europe, China and India. The acquisitions of Nitco Paints Private Limited (India), Pinturas Industriales S.A. (Uruguay), Napko, S.A. de C.V. (Mexico) and Flex Recubrimientos, S.A. de C.V. (Mexico) are included in this segment. This segment meets the demands of its customers for a consistent worldwide product development, manufacturing and distribution presence and approach to doing business. This segment licenses certain technology and trade names worldwide. Sherwin-Williams® and other controlled brand products are distributed through the Paint Stores Group and this segment's network of 519 company-operated branches and by a direct sales staff and outside sales representatives to retailers, dealers, jobbers, licensees and other third party distributors. During 2007, this segment added 50 net new branches consisting of 29 net new branches in South America, 19 branches in the United States and 2 in Canada. At December 31, 2007, the Global Group consisted of operations in the United States, subsidiaries in 15 foreign countries, 3 foreign joint ventures and income from licensing agreements in 14 foreign countries.

Administrative Segment

The Administrative segment includes the administrative expenses of the Company's corporate headquarters site. Also included in the Administrative segment was interest expense which was unrelated to retail real estate leasing activities, interest and investment income, certain foreign currency transaction losses related to dollar-denominated debt and

foreign currency option and forward contracts, certain expenses related to closed facilities and environmental-related matters, and other expenses which were not directly associated with any Reportable Operating Segment. The Administrative segment did not include any significant foreign operations. Also included in the Administrative segment was a real estate management unit that is responsible for the ownership, management, and leasing of non-retail properties held primarily for use by the Company, including the Company's

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headquarters site, and disposal of idle facilities. Sales of this segment represented external leasing revenue of excess headquarters space or leasing of facilities no longer used by the Company in its operations. Gains and losses from the sale of property were not a significant operating factor in determining the performance of the Administrative segment.

Segment Financial Information

For financial information regarding our Reportable Operating Segments, including net external sales, segment profit, identifiable assets and other information by segment, see Note 18 of the Notes to Consolidated Financial Statements on pages 76 through 78 of our 2007 Annual Report, which is incorporated herein by reference.

Domestic and Foreign Operations

Financial and other information regarding domestic and foreign operations is set forth in Note 18 of the Notes to Consolidated Financial Statements on page 77 of our 2007 Annual Report, which is incorporated herein by reference.

Additional information regarding risks attendant to foreign operations is set forth on page 34 of our 2007 Annual Report under the caption entitled Management's Discussion and Analysis of Financial Condition and Results of Operation, which is incorporated herein by reference.

Business Developments

For additional information regarding our business and business developments, see pages 6 through 14 of our 2007 Annual Report and the Letter to Shareholders on pages 2 through 5 of our 2007 Annual Report, which is incorporated herein by reference.

Raw Materials and Products Purchased for Resale

Raw materials and fuel supplies are generally available from various sources in sufficient quantities that none of the Reportable Operating Segments anticipate any significant sourcing problems during 2008. There are sufficient suppliers of each product purchased for resale that none of the Reportable Operating Segments anticipate any significant sourcing problems during 2008.

Seasonality

The majority of the sales for the Paint Stores Group, Consumer Group and Global Group traditionally occur during the second and third quarters. There is no significant seasonality in sales for the Administrative segment.

Working Capital

In order to meet increased demand during the second and third quarters, the Company usually builds its inventories during the first quarter. Working capital items (inventory and receivables) are generally financed through short-term borrowings, which include the use of lines of credit and the issuance of commercial paper. For a description of the Company's liquidity and capital resources, see pages 23 through 34 of our 2007 Annual Report under the caption entitled Management's Discussion and Analysis of Financial Condition and Results of Operations, which is incorporated herein by reference.

Trademarks and Trade Names

Customer recognition of our trademarks and trade names collectively contribute significantly to our sales. The major trademarks and trade names used by each Reportable Operating Segment are set forth below.

Paint Stores Group: Sherwin-Williams®, ProMar®, SuperPaint®, A-100®, PrepRite®, Classic 99®, Pro Classic®, Duration®, Master Hide®, ExpressTech®, Duron®, Columbia™ and MAB™.

Consumer Group: Thompson ® WaterSeal®, Dutch Boy®, Cuprinol®, Pratt & Lambert®, Martin Senour®, H&C®, Rubberset®, Dupli-Color®, Minwax®, White Lightning®, Krylon®, Purdy®, Bestt Liebco®, Accurate Dispersions™, Dobco™, Kool Seal®, Snow Roof®, Uniflex® and VHT®.

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Global Group: Sherwin-Williams®, Martin Senour®, Lazzuril®, Excelo®, Baco®, Planet Color™, Ultra-Cure®, Dutch Boy®, Krylon®, Kem-Tone®, Pratt & Lambert®, Minwax®, Sher-Wood®, Powdura®, Polane®, Ronseal™, Colorgin™, Sumare™, Andina™, Marson™, Tri-Flow®, Thompson ® WaterSeal®, Metalatex®, Novacor®, Loxon®, Napko™, AWX™ and Ultra™.

Patents

Although patents and licenses are not of material importance to our business as a whole or any segment, the international operations of the Global Group derive a portion of its income from the licensing of technology, trademarks and trade names to foreign companies.

Backlog and Productive Capacity

Backlog orders are not significant in the business of any Reportable Operating Segment since there is normally a short period of time between the placing of an order and shipment. We believe that sufficient productive capacity currently exists to fulfill our needs for paint, coatings and related products through 2008.

Research and Development

For information regarding our costs of research and development included in technical expenditures, see Note 1 of the Notes to Consolidated Financial Statements on page 50 of our 2007 Annual Report, which is incorporated herein by reference.

Competition

We experience competition from many local, regional, national and international competitors of various sizes in the manufacture, distribution and sale of our paint, coatings and related products. We are a leading manufacturer and retailer of paint, coatings and related products to professional, industrial, commercial and retail customers, however, our competitive position varies for our different products and markets.

In the Paint Stores Group, competitors include other paint and wallpaper stores, mass merchandisers, home centers, independent hardware stores, hardware chains and manufacturer-operated direct outlets. Product quality, product innovation, breadth of product line, technical expertise, service and price determine the competitive advantage for this segment.

In the Consumer Group, domestic and foreign competitors include manufacturers and distributors of branded and private labeled paint and coatings products. Technology, product quality, product innovation, breadth of product line, technical expertise, distribution, service and price are the key competitive factors for this segment.

The Global Group has numerous competitors in its domestic and foreign markets with broad product offerings and several others with niche products. Key competitive factors for this segment include technology, product quality, product innovation, breadth of product line, technical expertise, distribution, service and price.

The Administrative segment has many competitors consisting of other real estate owners, developers and managers in areas in which this segment owns property. The main competitive factors are the availability of property and price.

Employees

We employed 31,572 persons at December 31, 2007.

Environmental Compliance

For additional information regarding environmental-related matters, see pages 25 through 27 of our 2007 Annual Report under the caption entitled Management's Discussion and Analysis of Financial Condition and Results of Operations and Notes 1, 8 and 13 of the Notes to Consolidated Financial Statements on pages 49, 63 and 64, and 73, respectively, of our 2007 Annual Report, which is incorporated herein by reference.

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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

Certain statements contained in Management's Discussion and Analysis of Financial Condition and Results of Operations, Business and elsewhere in this report constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements are based upon management's current expectations, estimates, assumptions and beliefs concerning future events and conditions and may discuss, among other things, anticipated future performance (including sales and earnings), expected growth, future business plans and the costs and potential liability for environmental-related matters and the lead pigment and lead-based paint litigation. Any statement that is not historical in nature is a forward-looking statement and may be identified by the use of words and phrases such as expects, anticipates, believes, will, will likely result, will continue, plans to and similar expressions.

Readers are cautioned not to place undue reliance on any forward-looking statements. Forward-looking statements are necessarily subject to risks, uncertainties and other factors, many of which are outside our control, that could cause actual results to differ materially from such statements and from our historical results and experience. These risks, uncertainties and other factors include such things as:

general business conditions, strengths of retail and manufacturing economies and the growth in the coatings industry;

competitive factors, including pricing pressures and product innovation and quality;

changes in raw material and energy supplies and pricing;

changes in our relationships with customers and suppliers;

our ability to attain cost savings from productivity initiatives;

our ability to successfully integrate past and future acquisitions into our existing operations, as well as the performance of the businesses acquired;

risks and uncertainties associated with our ownership of Life Shield Engineered Systems, LLC;

changes in general domestic economic conditions such as inflation rates, interest rates, tax rates, unemployment rates, higher labor and healthcare costs, recessions, and changing government policies, laws and regulations;

risks and uncertainties associated with our expansion into and our operations in China, India, South America and other foreign markets, including general economic conditions, inflation rates, recessions, foreign currency exchange rates, foreign investment and repatriation restrictions, legal and regulatory constraints, civil unrest and other external economic and political factors;

the achievement of growth in developing markets, such as China, India, Mexico and South America;

increasingly stringent domestic and foreign governmental regulations including those affecting the environment;

inherent uncertainties involved in assessing our potential liability for environmental-related activities;

other changes in governmental policies, laws and regulations, including changes in accounting policies and standards and taxation requirements (such as new tax laws and new or revised tax law interpretations);

the nature, cost, quantity and outcome of pending and future litigation and other claims, including the lead pigment and lead-based paint litigation, and the effect of any legislation and administrative regulations relating thereto; and

unusual weather conditions.

Readers are cautioned that it is not possible to predict or identify all of the risks, uncertainties and other factors that may affect future results and that the above list should not be considered to be a complete list. Any forward-looking statement speaks only as of the date on which such statement is made, and we undertake no obligation to update or revise any forward-looking statement, whether as a result of new information, future events or otherwise.

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ITEM 1A. RISK FACTORS

Described below and elsewhere in this report and other documents that we file from time to time with the Securities and Exchange Commission are risks, uncertainties and other factors that can adversely affect our business, results of operation and financial condition. The following are some of the more important of these risks, uncertainties and other factors. Additional risks, uncertainties and other factors that are currently not known to us or we believe are not currently material may also adversely affect our business, results of operation and financial condition.

Adverse changes in general business conditions in the United States and worldwide may adversely affect our results of operations and financial condition.

Adverse changes in general business conditions in the United States and worldwide may reduce the demand for some of our products and adversely affect our results of operations and financial condition. Higher inflation rates, interest rates, tax rates and unemployment rates, higher labor and healthcare costs, recessions, changing governmental policies, laws and regulations, and other economic factors that adversely affect the demand for our paint, coatings and related products could adversely affect our results of operations and financial condition.

Economic downturns in cyclical segments of the economy may reduce the demand for some of our products and adversely affect our sales and earnings.

Portions of our business involve the sale of paint, coatings and related products to segments of the economy that are cyclical in nature, particularly segments relating to construction, housing and manufacturing. Our sales to these segments are affected by the levels of discretionary consumer and business spending in these segments. During economic downturns in these segments, the levels of consumer and business discretionary spending may decrease. This decrease in spending will likely reduce the demand for some of our products and adversely affect our sales and earnings.

Increases in the cost of raw materials and energy may adversely affect our earnings.

We purchase raw materials and energy for use in the manufacturing, distribution and sale of our products. Factors such as adverse weather conditions, including hurricanes, and other disasters can disrupt raw material and fuel supplies and increase our costs. Although raw materials and energy supplies are generally available from various sources in sufficient quantities, unexpected shortages and increases in the cost of raw materials and energy may have an adverse effect on our earnings in the event we are unable to offset these costs by sufficiently decreasing our operating costs or raising the prices of our products. Many of our paint and coatings products utilize titanium dioxide, which is widely used as a white pigment for paint.

Although we have an extensive customer base, the loss of any of our largest customers could adversely affect our sales and earnings.

We have a large and varied customer base due to our extensive distribution network. During 2007, no individual customer accounted for sales totaling more than ten percent of our sales. However, we have some customers that, individually, purchase a large amount of products from us. Although our broad distribution channels would help to minimize the impact of the loss of any one customer, the loss of any of these large customers could have an adverse effect on our sales and earnings.

Adverse weather conditions may reduce the demand for some of our products and could have a negative effect on our sales.

From time to time, adverse weather conditions in certain parts of the United States have had an adverse effect on our sales of paint, coatings and related products. For example, unusually cold and rainy weather, especially during the exterior painting season, could have an adverse effect on sales of our exterior paint products.

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Increased competition may reduce our sales and earnings performance.

We face substantial competition from many international, national, regional and local competitors of various sizes in the manufacture, distribution and sale of our paint, coatings and related products. Some of our competitors are larger than us and have greater financial resources to compete. Other competitors are smaller and may be able to offer more specialized products. Technology, product quality, product innovation, breadth of product line, technical expertise, distribution, service and price are the key competitive factors for our business. Competition in any of these areas may reduce our sales and adversely affect our earnings by resulting in decreased sales volumes, reduced prices and increased costs of manufacturing, distributing and selling our products.

Our operating results and financial condition may be negatively impacted if we do not successfully integrate past and future acquisitions into our existing operations and if the performance of the businesses we acquire do not meet our expectations.

We have historically made strategic acquisitions of businesses in the paint and coatings industry and will likely acquire additional businesses in the future as part of our long term growth strategy. These acquisitions involve challenges and risks. In the event that we do not successfully integrate these acquisitions into our existing operations so as to realize the expected return on our investment, our operating results and financial condition could be adversely affected.

Risks and uncertainties associated with our expansion into and our operations in China, India, South America and other foreign markets could adversely affect our sales and earnings.

Net external sales of our consolidated foreign subsidiaries totaled approximately \$965 million in 2007, or 12.1% of our total consolidated net sales. Sales outside of the United States make up an important part of our current business and future strategic plans. Our sales and earnings could be adversely affected by a variety of international factors, including general economic conditions, inflation rates, recessions, foreign currency exchange rates, foreign investment and repatriation restrictions, legal and regulatory constraints, civil unrest, difficulties in staffing and managing foreign operations and other external economic and political factors. Our inability to successfully manage the risks and uncertainties relating to these factors could adversely affect our sales and earnings.

In many foreign countries, it is acceptable to engage in certain business practices that we are prohibited from engaging in because of regulations that are applicable to us, such as the Foreign Corrupt Practices Act. Although we have internal control policies and procedures designed to ensure compliance with these regulations, there can be no assurance that our policies and procedures will prevent a violation of these regulations. Any violation could cause an adverse effect on our results of operations.

Fluctuations in foreign currency exchange rates could adversely affect our sales and earnings.

Because of our international operations, we are exposed to risk associated with interest rates and value changes in foreign currencies, which may adversely affect our business. Historically, our reported net sales and net earnings have been subjected to fluctuations in foreign exchange rates. Our primary exchange rate exposure is with the euro, the British pound, the Argentine peso, the Brazilian real, the Chilean peso, the Canadian dollar and the Mexican peso against the U.S. dollar. While we actively manage the exposure of our foreign currency risk as part of our overall financial risk management policy, we believe we may experience losses from foreign currency translation, and such losses could adversely affect our sales and earnings.

We are required to comply with increasingly stringent federal, state and local environmental laws and regulations, the cost of which is likely to increase and may adversely affect our earnings.

Our operations are subject to various federal, state and local environmental laws and regulations. These laws and regulations not only govern our current operations and products, but also impose potential liability on us for our past operations. We expect environmental laws and regulations to impose increasingly stringent requirements upon our industry and us in the future. Our costs to comply with these laws and regulations may increase as these requirements become more stringent in the future, and these increased costs may adversely affect our earnings.

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We are involved with environmental investigation and remediation activities at some of our currently and formerly owned sites, as well as a number of third-party sites, for which our ultimate liability may exceed the current amount we have accrued.

We are involved with environmental investigation and remediation activities at some of our currently and formerly owned sites and a number of third-party sites. We accrue for estimated costs of investigation and remediation activities at these sites for which commitments or clean-up plans have been developed and when such costs can be reasonably estimated based on industry standards and professional judgment. These estimated costs are based on currently available facts regarding each site. We continuously assess our potential liability for investigation and remediation activities and adjust our environmental-related accruals as information becomes available upon which more accurate costs can be reasonably estimated. Due to the uncertainties surrounding environmental investigation and remediation activities, our liability may result in costs that are significantly higher than currently accrued and may have an adverse affect on our earnings.

The nature, cost, quantity and outcome of pending and future litigation, such as litigation arising from the historical manufacture and sale of lead pigments and lead-based paint, could have a material adverse effect on our results of operations, liquidity and financial condition.

In the course of our business, we are subject to a variety of claims and lawsuits, including litigation relating to product liability and warranty, personal injury, environmental, intellectual property, commercial, contractual and antitrust claims that are inherently subject to many uncertainties regarding the possibility of a loss to us. These uncertainties will ultimately be resolved when one or more future events occur or fail to occur confirming the incurrence of a liability or the reduction of a liability. In accordance with Statement of Financial Accounting Standards (FAS) No. 5,

Accounting for Contingencies, we accrue for these contingencies by a charge to income when it is both probable that one or more future events will occur confirming the fact of a loss and the amount of the loss can be reasonably estimated. In the event that a loss contingency is ultimately determined to be significantly higher than currently accrued, the recording of the additional liability may result in a material impact on our results of operations, liquidity or financial condition for the annual or interim period during which such additional liability is accrued. In those cases where no accrual is recorded because it is not probable that a liability has been incurred and cannot be reasonably estimated, any potential liability ultimately determined to be attributable to us may result in a material impact on our results of operations, liquidity or financial condition for the annual or interim period during which such liability is accrued. In those cases where no accrual is recorded or exposure to loss exists in excess of the amount accrued, FAS No. 5 requires disclosure of the contingency when there is a reasonable possibility that a loss or additional loss may have been incurred if even the possibility may be remote.

Our past operations included the manufacture and sale of lead pigments and lead-based paints. Along with other companies, we are a defendant in a number of legal proceedings, including individual personal injury actions, purported class actions, actions brought by the State of Rhode Island and the State of Ohio, and actions brought by various counties, cities, school districts and other government-related entities, arising from the manufacture and sale of lead pigments and lead-based paints. The plaintiffs are seeking recovery based upon various legal theories, including negligence, strict liability, breach of warranty, negligent misrepresentations and omissions, fraudulent misrepresentations and omissions, concert of action, civil conspiracy, violations of unfair trade practice and consumer protection laws, enterprise liability, market share liability, public nuisance, unjust enrichment and other theories. The plaintiffs seek various damages and relief, including personal injury and property damage, costs relating to the detection and abatement of lead-based paint from buildings, costs associated with a public education campaign, medical monitoring costs and others. We are also a defendant in legal proceedings arising from the manufacture and sale of non-lead-based paints which seek recovery based upon various legal theories, including the failure to adequately warn of potential exposure to lead during surface preparation when using non-lead-based paint on surfaces previously painted with lead-based paint. We believe that the litigation brought to date is without merit or subject to

meritorious defenses and are vigorously defending such litigation. We expect that additional lead pigment and lead-based paint litigation may be filed against us in the future asserting similar or different legal theories and seeking similar or different types of damages and relief.

During September 2002, a jury trial commenced in the first phase of an action brought by the State of Rhode Island against us and the other defendants. The sole issue before the court in this first phase was whether lead

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pigment in paint constitutes a public nuisance under Rhode Island law. In October 2002, the court declared a mistrial as the jury, which was split four to two in favor of the defendants, was unable to reach a unanimous decision.

The State of Rhode Island retried the case and on February 22, 2006, the jury returned a verdict, finding that (i) the cumulative presence of lead pigment in paints and coatings on buildings in the State of Rhode Island constitutes a public nuisance, (ii) we, along with two other defendants, caused or substantially contributed to the creation of the public nuisance, and (iii) we and two other defendants should be ordered to abate the public nuisance. On February 28, 2006, the Court granted the defendants' motion to dismiss the punitive damages claim, finding insufficient evidence to support the State's request for punitive damages. On February 26, 2007, the Court issued a decision on the post-trial motions and other matters pending before the Court. Specifically, the Court (i) denied the defendant's post-trial motions for judgment as a matter of law and for a new trial, (ii) decided to enter a judgment of abatement in favor of the State against us and two other defendants, and (iii) decided to appoint a special master for the purpose of assisting the Court in its consideration of a remedial order to implement the judgment of abatement, and if necessary, any monitoring of the implementation of that order. On March 16, 2007, final judgment was entered against us and two other defendants. Also on March 16, 2007, we filed our notice of appeal to the Rhode Island Supreme Court. Oral argument on our and the other two defendants' appeal to the Rhode Island Supreme Court is scheduled for May 2008. Proceedings relating to a remedial order to implement the judgment of abatement are continuing in the Court during the pending appeal to the Rhode Island Supreme Court.

We cannot reasonably determine the impact that the State of Rhode Island decision and determination of liability will have on the number or nature of present or future claims and proceedings against us or estimate the amount or range of ultimate loss that we may incur.

Notwithstanding our views on the merits, litigation is inherently subject to many uncertainties and we ultimately may not prevail. Adverse court rulings, such as the judgment against us and other defendants in the State of Rhode Island action and the Wisconsin State Supreme Court's July 2005 determination that Wisconsin's risk contribution theory may apply in the lead pigment litigation, or determinations of liability, among other factors, could affect the lead pigment and lead-based paint litigation against us and encourage an increase in the number and nature of future claims and proceedings. In addition, from time to time, various legislation and administrative regulations have been enacted, promulgated or proposed to impose obligations on present and former manufacturers of lead pigments and lead-based paints respecting asserted health concerns associated with such products or to overturn the effect of court decisions in which we and other manufacturers have been successful.

Due to the uncertainties involved, management is unable to predict the outcome of the lead pigment and lead-based paint litigation, the number or nature of possible future claims and proceedings, or the effect that any legislation and/or administrative regulations may have on the litigation or against us. In addition, management cannot reasonably determine the scope or amount of the potential costs and liabilities related to such litigation, or any such legislation and regulations. In accordance with FAS No. 5, we have not accrued any amounts for such litigation. Any potential liability that may result from such litigation or such legislation and regulations cannot reasonably be estimated. In the event any significant liability is determined to be attributable to us relating to such litigation, the recording of the liability may result in a material impact on net income for the annual or interim period during which such liability is accrued. Additionally, due to the uncertainties associated with the amount of any such liability and/or the nature of any other remedy which may be imposed in such litigation, any potential liability determined to be attributable to us arising out of such litigation may have a material adverse effect on our results of operations, liquidity or financial condition. An estimate of the potential impact on our results of operations, liquidity or financial condition cannot be made due to the aforementioned uncertainties.

We discuss the risks and uncertainties related to litigation, including the lead pigment and lead-based paint litigation, in more detail on pages 21 and 22 of our 2007 Annual Report under the caption "Litigation and Other Contingent

Liabilities, and pages 29 through 33 of our 2007 Annual Report under the caption *Litigation of Management's Discussion and Analysis of Financial Condition and Results of Operations* and in Note 9 of the Notes to Consolidated Financial Statements on pages 64 through 68 of our 2007 Annual Report.

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The costs or potential liability ultimately determined to be attributable to us through our ownership of Life Shield could have an adverse effect on our results of operations, liquidity or financial condition.

We own Life Shield Engineered Systems, LLC. Life Shield develops and manufactures blast and fragment mitigating systems and ballistic resistant systems. The blast and fragment mitigating systems and ballistic resistant systems create a potentially higher level of product liability for us than is normally associated with coatings and related products we manufacture, distribute and sell. Depending upon the extent of any potential liability ultimately determined to be attributable to us relating to Life Shield, such liability could have an adverse effect on our results of operations, liquidity and financial condition. We discuss these risks and uncertainties in more detail on page 29 of our 2007 Annual Report under the caption entitled *Contingent Liabilities* of *Management's Discussion and Analysis of Financial Condition and Results of Operations*.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

We own our world headquarters located in Cleveland, Ohio, which includes the world headquarters for the Paint Stores Group, Consumer Group and Global Group. Our principal manufacturing and distribution facilities are located as set forth below. We believe our manufacturing and distribution facilities are well-maintained and are suitable and adequate, and have sufficient productive capacity, to meet our current needs.

PAINT STORES GROUP*Manufacturing Facilities*

Atlanta, Georgia	Owned	Orlando, Florida	Owned
Beltsville, Maryland	Owned	Spokane, Washington	Leased
Helena, Montana	Leased	Terre Haute, Indiana	Owned
Kingston, Jamaica	Leased		

Distribution Facilities

Atlanta, Georgia	Owned	Spokane, Washington	Leased
Kingston, Jamaica	Owned	Spokane Valley, Washington	Leased
Newark, New Jersey	Leased	Terre Haute, Indiana	Owned
Orlando, Florida	Owned		

CONSUMER GROUP*Manufacturing Facilities*

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Andover, Kansas	Owned	Holland, Michigan	Owned
Baltimore, Maryland	Owned	Largo, Florida	Owned
Bedford Heights, Ohio	Owned	Lawrenceville, Georgia	Owned
Chicago, Illinois	Owned	Manchester, Georgia	Owned
Cincinnati, Ohio	Owned	Memphis, Tennessee	Owned
Coffeyville, Kansas	Owned	Morrow, Georgia	Owned
Crisfield, Maryland	Leased	Norfolk, Virginia	Leased
Deshler, Ohio	Owned	Olive Branch, Mississippi	Owned
Ennis, Texas	Owned	Orlando, Florida	Owned
Fernley, Nevada	Owned	Portland, Oregon	Leased
Flora, Illinois	Owned	Reno, Nevada	Leased
Fort Erie, Ontario, Canada	Owned	San Diego, California	Leased
Garland, Texas	Owned	South Holland, Illinois	Owned
Greensboro, North Carolina	Owned		

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Distribution Facilities

Atlanta, Georgia	Leased	San Juan, Puerto Rico	Leased
Effingham, Illinois	Leased	Swaffham, England	Leased
Fredericksburg, Pennsylvania	Owned	Vaughan, Ontario, Canada	Leased
Memphis, Tennessee	Leased	Waco, Texas	Leased
Reno, Nevada	Leased	Winter Haven, Florida	Owned

GLOBAL GROUP

Manufacturing Facilities

Aprilia, Italy
 Arica, Chile
 Arlington, Texas
 Buenos Aires, Argentina
 Columbus, Ohio
 Dongguan, China
 Greensboro, North Carolina
 Grimsby, Ontario, Canada
 Monterrey, Mexico
 Monterrey, Mexico (2)
 Montevideo C