

ACUITY BRANDS INC

Form 10-K

November 02, 2006

Table of Contents

Index to Financial Statements

---

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

Washington, D.C. 20549

---

**FORM 10-K**

---

(Mark One)

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

For the fiscal year ended August 31, 2006.

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 001-16583.

---

**ACUITY BRANDS, INC.**

(Exact name of registrant as specified in its charter)

---

Delaware  
(State or other jurisdiction of incorporation or organization)

1170 Peachtree Street, N.E., Suite 2400,

Atlanta, Georgia

58-2632672  
(I.R.S. Employer Identification Number)

30309-7676

Edgar Filing: ACUITY BRANDS INC - Form 10-K

(Address of principal executive offices)

(404) 853-1400

(Zip Code)

(Registrant's telephone number, including area code)

---

Securities registered pursuant to Section 12(b) of the Securities Exchange Act of 1934:

Title of Each Class	Name of Each Exchange on which Registered
Common Stock (\$0.01 Par Value)	New York Stock Exchange
Preferred Stock Purchase Rights	New York Stock Exchange

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

---

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

Indicate by checkmark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the 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, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

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

Based on the closing price of the Registrant's common stock of \$39.49 as quoted on the New York Stock Exchange on February 28, 2006, the aggregate market value of the voting stock held by nonaffiliates of the registrant, was \$1,757,733,348.

The number of shares outstanding of the registrant's common stock, \$0.01 par value, was 43,047,906 shares as of October 25, 2006.

---

**DOCUMENTS INCORPORATED BY REFERENCE**

Location in Form 10-K	Incorporated Document
Part II, Item 5	Proxy Statement for 2006 Annual Meeting of Stockholders
Part III, Items 10, 11, 12, 13, and 14	Proxy Statement for 2006 Annual Meeting of Stockholders

**Table of Contents**

**Index to Financial Statements**

**ACUITY BRANDS, INC.**

**Table of Contents**

	<b>Page No.</b>
Part I	
Item 1. <u>Business</u>	3-11
Item 1a. <u>Risk Factors</u>	12-13
Item 2. <u>Properties</u>	13-14
Item 3. <u>Legal Proceedings</u>	14-15
Item 4. <u>Submission of Matters to a Vote of Security Holders</u>	15
Part II	
Item 5. <u>Market for Registrant's Common Equity, Related Stockholder Matters, and Issuer Purchases of Equity Securities</u>	16
Item 6. <u>Selected Financial Data</u>	17
Item 7. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	18-32
Item 7a. <u>Quantitative and Qualitative Disclosures about Market Risk</u>	32
Item 8. <u>Financial Statements and Supplementary Data</u>	32-69
Item 9. <u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	70
Item 9a. <u>Controls and Procedures</u>	70
Part III	
Item 10. <u>Directors and Executive Officers of the Registrant</u>	71
Item 11. <u>Executive Compensation</u>	71
Item 12. <u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	71
Item 13. <u>Certain Relationships and Related Transactions</u>	71
Item 14. <u>Principal Accounting Fees and Services</u>	71
Part IV	
Item 15. <u>Exhibits</u>	72-82
<u>Signatures</u>	83
<u>Financial Statement Schedules</u>	84

---

**Table of Contents**

**Index to Financial Statements**

**PART I**

**Item 1. Business**

Acuity Brands, Inc. ( Acuity Brands or the Company ) is a holding company that owns and manages two businesses that serve distinctive markets lighting equipment and specialty products. The lighting equipment segment designs, produces, and distributes a broad array of indoor and outdoor lighting fixtures for commercial and institutional, industrial, infrastructure, and residential applications for various markets throughout North America and select international markets. The specialty products segment formulates, produces, and distributes specialty chemical products including cleaners, deodorizers, sanitizers, and pesticides for industrial and institutional, commercial, and residential applications primarily for various markets throughout North America and Europe. Of the Company's fiscal 2006 net sales of approximately \$2.4 billion, the lighting equipment segment generated approximately 77% of total net sales while the specialty products segment provided the remaining 23%. Financial information relating to the Company's two segments for the past three fiscal years is included in Note 12 of the *Notes to Consolidated Financial Statements* included in this report.

**Business Segments**

***Lighting Equipment***

The lighting equipment business of Acuity Brands is operated by Acuity Brands Lighting ( ABL ). ABL is one of the world's leading providers of lighting fixtures for new construction, renovation, and facility maintenance applications. Products include a full range of indoor and outdoor lighting for commercial and institutional ( C&I ), industrial, infrastructure, and residential applications. ABL manufactures and procures lighting products in the United States, Mexico, Europe, and China. These products are marketed under numerous brand names, including Lithonia Lighting®, Holophane®, Gotham®, Hydrel®, Peerless®, Antique Street Lamps, Carandini®, American Electric Lighting®, SpecLight®, and Metal Optics®. ABL manufactures products in 13 plants in North America and three plants in Europe.

Principal customers include electrical distributors, retail home improvement centers, national accounts, electric utilities, municipalities, and lighting showrooms located in North America and select international markets. In North America, ABL's products are sold through independent sales agents and factory sales representatives who cover specific geographic areas and market segments. Products are delivered through a network of distribution centers, regional warehouses, and commercial warehouses using both common carriers and a company-owned truck fleet. To serve international customers, ABL employs a sales force that utilizes distribution methods to meet specific individual customer or country requirements. In fiscal 2006, North American sales accounted for approximately 97% of ABL's net sales. See Note 12 of the *Notes to Consolidated Financial Statements* for more information concerning the domestic and international net sales of the Company.

***Specialty Products***

The specialty products business of Acuity Brands is operated by Acuity Specialty Products ( ASP ). ASP is a leading provider of specialty chemical products in the industrial and institutional ( I&I ) and retail markets. Products include cleaners, sanitizers, disinfectants, polishes, floor finishes, degreasers, deodorizers, pesticides, insecticides, and herbicides. ASP manufactures products in four North American plants and two European plants.

Acuity Specialty Products sells products to customers primarily in North America and Western Europe. In fiscal 2006, North American sales accounted for approximately 93% of the net sales of ASP. ASP serves a broad range of industrial and institutional customers, including municipalities and businesses ranging from small sole proprietorships to the largest corporations in the U.S. The core I&I business is made up of customers to whom cleaning chemicals are important to the business and, typically, where the decision to purchase is local. While ASP services a wide array of business segments, individual markets in the I&I channel include food processing

**Table of Contents**

**Index to Financial Statements**

and preparation, transportation, education, automotive, government, and hospitality. Retail channels include large and small home improvement centers, mass merchandisers, and hardware stores. ASP sells numerous products under such well-known brands as Zep<sup>®</sup>, Enforcer<sup>®</sup>, Zep Commercial<sup>®</sup>, and Selig .

**Industry Overview**

***Lighting Equipment***

The current size of the North American lighting fixture market is estimated at \$10.4 billion. The North American lighting fixture market consists of non-portable lighting fixtures as defined by the National Electrical Manufacturers Association and lighting related products such as emergency lighting equipment, poles, controls, and modular wiring systems. The U.S. market represents approximately 85% of the North American market. The Company estimates that the top four manufacturers (including Acuity Brands Lighting) represent approximately 55% of the total North American lighting market. The remainder of the market is made up of an estimated 1,200 lighting manufacturers.

The primary demand driver for ABL's core businesses is non-residential construction, which includes a broad range of commercial, institutional, and industrial buildings. Construction spending on infrastructure projects such as highways, streets, and downtown developments also has a material impact on ABL's infrastructure-focused segments. ABL's retail lighting segments are highly dependent on economic drivers such as consumer spending and discretionary income, along with housing construction and home improvement spending.

Based on industry data for 2006, new construction accounts for approximately 82% of non-residential contract award values, while renovations account for approximately 18%, though this mix can vary depending on economic conditions. Major trends that can impact the industry include the development of new technologies for lamps and ballasts, new product trends, federal and state regulatory requirements, energy tax legislation, and sustainable design trends.

There has been a significant increase in the size and relative presence of the retail home improvement center segment in the past several years. In addition, imports of foreign-sourced lighting fixtures continue to grow, driven by both the foreign production of U.S. manufacturers and imports of low-cost fixtures primarily from Asian manufacturers. Consolidation remains a key trend in the electrical industry. Recent announcements of combinations among electrical distributors are evidence of this continuing trend. Additionally, certain significant retail home improvement businesses are expanding into the wholesale electrical distribution market through acquisitions.

***Specialty Products***

The Company estimates that the U.S. I&I cleaning chemicals market is \$9.1 billion and is highly fragmented. The Company believes that six major players (including Acuity Specialty Products) represents approximately 50% of the total U.S. I&I market with the remainder divided among hundreds of regional players. In general, the Company estimates that the U.S. I&I market grows at a rate approximating Gross Domestic Product ( GDP ). To some extent, consumption of janitorial cleaning and sanitation products is discretionary, but in a health-driven, sophisticated market such as the U.S., the Company believes that health and safety regulations and customer expectations somewhat buffer demand downturns. Increasing legislation in the areas of food and occupational health that require increased ranges of application and frequency of use is fueling growth in demand. In addition to the U.S. I&I market, there is a U.S. retail cleaning chemical market that is estimated at \$4.4 billion.

The Company believes that several major trends are affecting the industry. Health and safety regulations are shrinking the pool of available chemicals while at the same time increasing total usage rates. These trends have pushed development of improved product formulations and application methods. Increased centralized corporate

## Table of Contents

### Index to Financial Statements

buying and consolidation of the supply chain are threatening reselling distributors and requiring a reexamination of the supply chain processes and services to ensure they are adding value for their customers. More recently, significant increases in commodity costs are requiring manufacturers to increase selling prices, which the Company believes to be having a dampening effect on customer demand.

## Products

### *Lighting Equipment*

Acuity Brands Lighting produces a wide variety of lighting fixtures used in the following applications:

**Commercial & Institutional** Applications are represented by stores, hotels, offices, schools, and hospitals, as well as other government and public buildings. Products that serve these applications include recessed, surface and suspended fluorescent lighting products, recessed downlighting, and track lighting, as well as special application lighting products. The outdoor areas associated with these application segments are addressed by a variety of outdoor lighting products, such as area and flood lighting, decorative site lighting, and landscape lighting.

**Industrial** Applications primarily include warehouses and manufacturing facilities. The lighting equipment business serves these applications with a variety of glass and acrylic high intensity discharge ( HID ) and fluorescent lighting products.

**Infrastructure** Applications include highways, tunnels, airports, railway yards, and ports. Products that serve these applications include street, area, high-mast, off-set roadway, and sign lighting.

**Residential** Applications are addressed with a combination of decorative fluorescent and downlighting products, as well as utilitarian fluorescent products.

**Other Applications & Products** Other products include emergency lighting fixtures, which are primarily used in non-residential buildings, and lighting control and flexible wiring systems.

Lighting fixtures for numerous applications in a multitude of industry segments accounted for approximately 67% of total consolidated net sales for Acuity Brands in fiscal year 2006, and approximately 65% of total consolidated net sales during fiscal years 2005 and 2004. This does not include sales related to items such as wiring products, controls, and emergency lighting.

### *Specialty Products*

ASP produces and supplies a wide variety of specialty chemical products that are used in numerous applications in a broad range of markets. These include:

**Food Processing** Applications include integrated and customized dispensing systems and innovative approaches to antimicrobial control.

**Food Preparation** Applications include a suite of cleaning products designed specifically for the prepared food industry.

## Edgar Filing: ACUITY BRANDS INC - Form 10-K

**Transportation** Applications include cleaning and maintenance products for automobiles, aircraft, public transport, trucks, trains, and construction vehicles.

**Industrial** Applications include cleaning and maintenance products used by professional maintenance staff.

**Hospitality** Applications include products and dispensing solutions for customers to supply maintenance, housekeeping, and laundry services.

**Government** Applications include a suite of products and maintenance solutions for cities, school districts, military, and police and fire departments.

**Table of Contents**

**Index to Financial Statements**

***Contractors and Homeowners*** Applications include products for contract cleaners, small business owners, and homeowners and are supplied through retail channels. Products include a comprehensive range of floor care, general-purpose cleaners and sanitizers, drain maintenance, and pest control in convenient ready-to-use packaging.

Sales of specialty chemical products, excluding items sold to facilitate the use of chemicals, accounted for approximately 19% of total consolidated net sales for Acuity Brands during fiscal year 2006 and 20% of total consolidated net sales during fiscal years 2005 and 2004.

**Sales and Marketing**

***Lighting Equipment***

***Sales.*** ABL calls on customers in the North American market with separate sales forces targeted at delivering appropriate products and services to specific customer, channel, and geographic segments. These sales forces consist of approximately 200 company-employed salespeople and a network of approximately 160 independent sales agencies, each of which employs numerous salespeople. ABL also operates two separate European sales forces and an international sales group coordinating export sales outside of North America and Europe.

***Marketing.*** ABL markets its products to a multitude of end users through a broad spectrum of marketing and promotional vehicles, including direct customer contact, on-site training, print advertising in industry publications, product brochures, and other literature, as well as the internet and other electronic media. On-site training is conducted at dedicated product training facilities in Conyers, Georgia; Newark, Ohio; and Austin, Texas.

***Specialty Products***

***Sales.*** The sales organization at ASP consists of approximately 1,700 sales representatives worldwide. The compensation model in the I&I channel is primarily commission-based. Net sales are largely dependent on the hiring, training, and retention of the commissioned sales representatives.

The ASP sales organization covers the U.S., Canada, Italy, Belgium, Luxemburg, and the Netherlands, and certain other smaller markets. The I&I market is serviced primarily through 1,230 sales representatives in the United States, 150 sales representatives in Canada and 270 sales representatives throughout Europe, supplemented by a complement of customer and technical service personnel. The retail sales division utilizes approximately 50 salaried sales and management personnel to focus on the home center and hardware channels.

***Marketing.*** ASP's marketing efforts are focused on supporting a sell-through program from ASP through the sales organization and to the customer. ASP's marketing focus is in four distinct areas: market planning, product management, market-based pricing, and marketing services. Market planning includes comprehensive strategic and tactical plan development and support emphasizing financial objectives and accountability. Product management includes new product development and chemical dispensing equipment management. Market-based pricing takes into account competitive analysis and leverages the flexibility of the ASP operating platform. Marketing services provides sales support tools and collateral sales information to ASP's worldwide sales force and customer base.

**Customers**

A single customer in the home improvement channel, The Home Depot, accounted for approximately 13% of net sales of Acuity Brands during fiscal years 2006 and 2005, and 12% of net sales in fiscal year 2004. The loss of that customer could temporarily adversely affect the Company's results of operations.



---

**Table of Contents**

**Index to Financial Statements**

***Lighting Equipment***

Customers of Acuity Brands Lighting include electrical distributors, retail home improvement centers, national accounts, electric utilities, utility distributors, municipalities, contractors, catalogs, and lighting showrooms. In addition, there are a variety of other buying influences, which for any given project could represent a significant influence in the product specification process. These generally include engineers, architects, and lighting designers.

***Specialty Products***

Customers of ASP consist of I&I customers (approximately 84% of ASP net sales in 2006) and retail customers (approximately 16% of ASP net sales in 2006). I&I customers range from sole proprietorships to the largest corporations in the U.S. and government agencies. These customers are in various markets, including food processing and preparation, transportation, industrial, hospitality, government, and contractors and homeowners. The core I&I business is made up of varying sized customers to whom cleaning chemicals are important to the business and, typically, where the decision to purchase is local. Retail customers primarily include large and small home improvement centers, mass merchandisers, and hardware stores.

**Manufacturing**

Acuity Brands, through its two businesses, operates 22 manufacturing facilities, including 10 facilities in the United States, six facilities in Mexico, five facilities in Europe, and one facility in Canada.

***Lighting Equipment***

ABL utilizes a blend of internal and outsourced manufacturing processes and capabilities to fulfill a variety of customer needs in the most cost-effective manner. Critical processes, such as reflector forming and anodizing and high-end glass production, are primarily performed at company-owned facilities, offering the ability to differentiate end-products through superior capabilities. Other critical components, such as ballasts, are purchased primarily from outside vendors. Investment is focused on improving capabilities, product quality, and manufacturing efficiency. The integration of local suppliers' factories and warehouses also provides an opportunity to lower ABL-owned component inventory while maintaining high service levels through frequent just-in-time deliveries. ABL also utilizes contract manufacturing from U.S., Asian, and European sources for certain products and purchases certain finished goods, including poles, to complement its area lighting fixtures and a variety of residential and commercial lighting equipment. Net sales of product manufactured by others currently accounts for approximately 22% of the total net sales of ABL. Of total product manufactured by ABL, U.S. operations produce approximately 40%; Mexico produces approximately 56%; and Europe produces approximately 4%. ABL has one supplier of significance and a loss of that supplier could have a material adverse impact on operations for up to approximately six months. ABL purchased approximately \$65.3 million in finished goods from this supplier in 2006.

During fiscal 2006, management continued to focus on initiatives to make the Company more globally competitive. One of these initiatives at ABL related to enhancing its global supply chain and included the consolidation of certain manufacturing facilities into more efficient locations. Since 2002, ABL has closed ten facilities as part of this initiative. This initiative, the Manufacturing Network Transformation ( MNT ), has resulted in increased production in international locations, primarily Mexico, and greater sourcing from its network of worldwide vendors. Total square footage used for manufacturing at ABL has been reduced by approximately 23% over the past four fiscal years as a result of MNT and other programs.

***Specialty Products***

ASP manufactures products at six facilities located in the United States, Canada, Holland, and Italy. The three U.S. facilities produce approximately 89% of manufactured product; the Canadian facility produces

## **Table of Contents**

### **Index to Financial Statements**

approximately 6%; and the two European facilities produce approximately 5%. Certain finished goods purchased from contract manufacturers and finished goods suppliers supplement the manufactured product line. Sales of outsourced product currently account for approximately 25% of the net sales volume of ASP. Outsourced product is predominately manufactured in the U.S. Management does not believe the loss of any one supplier of outsourced product would have a material adverse impact on the results of operations of ASP.

### **Distribution**

#### ***Lighting Equipment***

Products are delivered through a network of strategically located distribution centers, regional warehouses, and commercial warehouses in North America using both common carriers and a company-owned truck fleet. For international customers, distribution methods are adapted to meet individual customer or country requirements.

#### ***Specialty Products***

Products sold to I&I markets are shipped from strategically located distribution centers and local branch warehouses throughout North America and in Europe, while retail products are distributed nationwide from the Georgia and Dallas plants and warehouses. Products are primarily delivered through common carriers.

### **Research and Development**

#### ***Lighting Equipment***

Research and development efforts at ABL are targeted toward the development of products with an ever-increasing performance-to-cost ratio and energy efficiency, while close relationships with lamp and ballast manufacturers are maintained to understand technology enhancements and incorporate them in ABL's fixture designs. ABL operates five separate product development model facilities, incorporating eight photometers for testing and optimizing fixture photometric performance. The Conyers, Georgia lab is approved by the National Voluntary Laboratory Accreditation Program for both fluorescent and high intensity discharge fixtures. For fiscal years 2006, 2005, and 2004, research and development expense at ABL was \$30.0 million, \$27.1 million, and \$27.9 million, respectively.

#### ***Specialty Products***

At ASP, research and development is directed at developing product systems that provide comprehensive solutions for broad-based customer applications. Additionally, efforts to enhance existing formulations by utilizing new raw materials or combinations of raw materials have resulted in both new and improved products. Special emphasis has been placed on the development of green products based on renewable and environmentally preferred raw materials. Technical expertise is employed to move proven technologies into new applications. Research and development expense at ASP for fiscal years 2006, 2005, and 2004, excluding technical services, was \$2.0 million, \$1.8 million, and \$2.1 million, respectively.

### **Competition**

#### ***Lighting Equipment***

The lighting equipment industry served by ABL is highly competitive, with the largest suppliers serving many of the same markets and competing for the same customers. Competition is based on numerous factors, including brand name recognition, price, product quality and design, customer relationships, and service capabilities. Primary competitors in the lighting industry include Cooper Industries Ltd., The Genlyte Group Incorporated, and Hubbell Incorporated. The Company estimates that the four largest lighting manufacturers (including ABL) have approximately a 55% share of the total North American lighting market.

---

**Table of Contents**

**Index to Financial Statements**

***Specialty Products***

The specialty products industry served by ASP is highly competitive. Overall, competition is fragmented, with numerous local and regional operators selling directly to customers, distributors, and a few national competitors. Many of these competitors offer products in some, but not all, of the markets served by ASP. Competition is based primarily on brand name recognition, price, product quality, and customer service. Competitors in the specialty products industry include but are not limited to NCH Corporation, Rochester Midland Corporation, State Chemical Manufacturing Company, JohnsonDiversey, Inc., and Ecolab, Inc. Management estimates ASP and its major competitors have approximately 50% of the total U.S. I&I market and the remainder is divided among hundreds of regional competitors.

**Environmental Regulation**

The operations of the Company are subject to numerous comprehensive laws and regulations relating to the generation, storage, handling, transportation, and disposal of hazardous substances as well as solid and hazardous wastes and to the remediation of contaminated sites. In addition, permits and environmental controls are required for certain of the Company's operations to limit air and water pollution, and these permits are subject to modification, renewal, and revocation by issuing authorities. On an ongoing basis, Acuity Brands allocates considerable resources including investments in capital and operating costs relating to environmental compliance. Environmental laws and regulations have generally become stricter in recent years. The cost of responding to future changes may be substantial. See Item 3: *Legal Proceedings* below for a discussion of certain environmental matters.

**Raw Materials**

The products produced by Acuity Brands require certain raw materials, including aluminum, plastics, electrical components, solvents, surfactants, other petroleum-based materials and components, and certain grades of steel. For example, Acuity Brands purchases approximately 115,000 tons of steel and aluminum on an annual basis depending on various factors including product mix. The Company estimates that approximately 9% of the raw materials purchased are petroleum-based. Acuity Brands purchases most raw materials on the open market and relies on third parties for the sourcing of some finished goods. Accordingly, the cost of products sold may be affected by changes in the market price of the above-mentioned raw materials or the sourcing of finished goods. Due to the mix of purchases (raw materials, components parts, and finished goods), timing of price increases, and other economic and competitive forces within the supply chain, it is not possible to determine the financial impact of changes in the market price of these raw materials.

Acuity Brands does not expect to engage in significant commodity hedging transactions for raw materials, though the Company has and will continue to commit to purchase certain materials for a period of up to twelve months. Significant increases in the prices of Acuity Brands products due to increases in the cost of raw materials could have a negative effect on demand for products and on profitability. While the Company has generally been able to pass along these increases in cost in the form of higher selling prices for its products, the higher selling prices have lagged behind the increases in cost seen in fiscal 2005. There can be no assurance that future disruptions in either supply or price of these materials will not negatively affect future results.

Each business constantly monitors and investigates alternative suppliers and materials based on numerous attributes including quality, service, and price. Additionally, each business has conducted internet auctions as a method of competitive bidding. The Company's ongoing efforts to improve the cost effectiveness of its products and services may result in a reduction in the number of its suppliers. A reduction in the number of suppliers could cause increased risk associated with reliance on a limited number of suppliers for certain raw materials, component parts (such as ballasts), and finished goods.

## **Table of Contents**

### **Index to Financial Statements**

#### **Backlog Orders**

The Company produces and stocks quantities of inventory at key distribution centers and warehouses throughout North America. ASP satisfies a significant portion of customer demand within 24 to 48 hours from the time a customer's order is placed and, therefore, sales order backlogs for the specialty products business are not material. ABL ships approximately 40% of sales orders during the month that those orders are placed. Sales order backlogs of the lighting equipment business, believed to be firm as of August 31, 2006 and 2005, were \$176.0 million and \$152.2 million, respectively. This increase in backlog is net of a decrease in past due backlog resulting from improved delivery performance.

#### **Patents, Licenses and Trademarks**

Acuity Brands owns or has licenses to use various domestic and foreign patents and trademarks related to its products, processes, and businesses. These intellectual property rights, particularly the trademarks relating to the products of Acuity Brands, are important factors for its businesses. To protect these proprietary rights, Acuity Brands relies on copyright, patent, trade secret, and trademark laws. Despite these protections, unauthorized parties may attempt to infringe on the intellectual property of Acuity Brands. Management of Acuity Brands is not aware of any such material unauthorized use or of any pending claims where Acuity Brands does not have the right to use any intellectual property material to the businesses of Acuity Brands. While patents and patent applications in the aggregate are important to the competitive position of Acuity Brands, no single patent or patent application is material to the Company.

#### **Seasonality and Cyclicity**

The businesses of Acuity Brands exhibit some seasonality, with net sales being affected by the impact of weather and seasonal demand on construction and installation programs, as well as the annual budget cycles of major customers. Because of these seasonal factors, Acuity Brands has experienced, and generally expects to experience, its highest sales in the last two quarters of each fiscal year.

A significant portion of the net sales of ABL relates to customers in the new construction and renovation industries, primarily for commercial and institutional applications. These industries are cyclical in nature and subject to changes in general economic conditions. Volume has a major impact on the profitability of ABL and Acuity Brands as a whole. In addition, net sales at ASP are dependent on the retail, wholesale, and industrial markets and demand for these markets is generally associated with GDP in the United States. Economic downturns and the potential decline in key construction markets and demand for specialty chemicals may have a material adverse effect on the net sales and operating income of Acuity Brands.

#### **International Operations**

Acuity Brands manufactures and assembles products at numerous facilities, some of which are located outside the United States. Approximately 60% and 11% of the products manufactured by the lighting equipment and specialty products segments, respectively, are manufactured outside the United States.

Of total product manufactured by ABL, approximately 56% is produced in Mexico. Most of these operations are authorized to operate as Maquiladoras by the Ministry of Economy of Mexico. Maquiladora status allows Acuity Brands to import certain items from the United States into Mexico duty-free, provided that such items, after processing, are re-exported from Mexico within 18 months. Maquiladora status, which is renewed every year, is subject to various restrictions and requirements, including compliance with the terms of the Maquiladora program and other local regulations. Many companies have established Maquiladora operations, increasing demand for labor, particularly skilled labor and professionals. This increase in demand, from new and existing Maquiladora operations, has resulted in increased labor costs and could result in increased labor costs in the future. Acuity Brands may be required to make additional investments in automated equipment to partially offset potential increase in labor and wage costs.

**Table of Contents**

**Index to Financial Statements**

The Company's initiatives to become more globally competitive include streamlining each segment's global supply chain by reducing the number of manufacturing facilities and enhancing the Company's worldwide procurement and sourcing capabilities. Management believes these initiatives will result in increased production in international locations, primarily Mexico, and will result in increased worldwide procurement and sourcing of certain raw materials, component parts, and finished goods. As a consequence, economic, political, military, or other events in a country where the Company manufactures, procures, or sources a significant amount of raw materials, component parts, or finished goods, could interfere with the Company's operations and negatively impact the Company's business.

For fiscal year 2006, net sales outside the U.S. represented approximately 10% and 19% of the total net sales of the lighting equipment and specialty products businesses, respectively. See Note 12 of the *Notes to Consolidated Financial Statements* for additional information regarding the geographic distribution of net sales, operating profit, and long-lived assets.

**Information Concerning Acuity Brands**

The Company makes its Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K (and all amendments to these reports), together with all reports filed pursuant to Section 16 of the Securities Exchange Act of 1934 by the Company's officers, directors, and beneficial owners of 10% or more of the Company's common stock, available free of charge through the SEC Filings link on the Company's website, located at [www.acuitybrands.com](http://www.acuitybrands.com), as soon as reasonably practicable after they are filed with or furnished to the SEC. Information included on the Company's website is not incorporated by reference into this Annual Report on Form 10-K.

Additionally, the Company has adopted a written Code of Ethics and Business Conduct that applies to all of the Company's directors, officers, and employees, including its principal executive officer and senior financial officers. This Code of Ethics and Business Conduct is being filed as Exhibit 14 to this Annual Report on Form 10-K. The Code of Ethics and Business Conduct and the Company's Corporate Governance Guidelines are available free of charge through the Corporate Governance link on the Company's website. Additionally, the Statement of Responsibilities of Committees of the Board and the Statement of Rules and Procedures of Committees of the Board, which contain the charters for the Company's Audit Committee, Compensation Committee, and Governance Committee and the rules and procedures relating thereto, are available free of charge through the Corporate Governance link on the Company's website. Each of the Code of Ethics and Business Conduct, the Corporate Governance Guidelines, the Statement of Responsibilities of Committees of the Board, and the Statement of Rules and Procedures of Committees of the Board is available in print to any stockholder of the Company that requests such document by contacting the Company's Investor Relations department.

**Employees**

Acuity Brands employs approximately 10,600 people, of whom approximately 6,600 are employed in the United States, 3,100 in Mexico, 350 in Canada, and 550 in other international locations, including Europe and the Asia/Pacific region. Union recognition and collective bargaining arrangements are in place, covering approximately 5,000 persons (including approximately 2,300 in the United States). The Company believes that it has a good relationship with both its unionized and non-unionized employees.

## **Table of Contents**

### **Index to Financial Statements**

#### **Item 1a. Risk Factors**

This filing contains forward-looking statements, within the meaning of the Private Securities Litigation Reform Act of 1995. A variety of risks and uncertainties could cause the Company's actual results to differ materially from the anticipated results or other expectations expressed in the Company's forward-looking statements. The risks and uncertainties include without limitation the following:

#### **Uncertainty of General Business and Economic Conditions**

The Company operates in a highly competitive environment that is affected by a number of factors. Demand for its product offerings is sensitive to both volatility within the non-residential construction and other industrial markets, and to the effect of consolidation of the Company's competitors. Changes in interest and foreign currency exchange rates could impair the Company's ability to effectively access capital markets. The Company's primary competitors have the ability to drive both pricing and product innovation within the marketplace. These competitive pressures may affect the Company's ability to achieve desired volume growth and profitability levels under its current pricing models, which could adversely impact results from operations. See above discussion of seasonality and cyclicalities.

#### **Foreign Economic, Political, Military, or Other Events**

The Company manufactures and sources certain amounts of raw materials, component parts, or finished goods outside of the United States. The Company's operations as well as those of key vendors are therefore subject to regulatory, economic, political, military, and other events in countries where these operations are located. Barriers to trade and other uncertainties within these foreign domiciles could affect the Company's ability to continue to manufacture and source material from abroad as well as future expansion into emerging markets outside of the United States.

#### **Fluctuation in Raw Material and Component Costs**

The Company utilizes a variety of raw materials and components in its production process including petroleum based chemicals, steel, copper, ballasts, and aluminum. Failure to effectively manage future increases in the costs of these items could adversely affect the ability to achieve operating margins acceptable to shareholders. The Company sources these goods from a number of suppliers and is, therefore, reasonably insulated from risks affecting any one supplier. However, profitability and volume could be negatively impacted by limitations inherent within the supply chain of certain of these materials, including competitive governmental, legal, natural disasters, and other events that could impact both supply and price.

#### **Future Growth through Strategic Acquisition**

The Company has previously endeavored, and may again endeavor to improve the business through strategic acquisition. The Company will gain from such activity only to the extent that it can effectively leverage the assets, including personnel, and operating processes of the acquired businesses. Uncertainty is inherent within the acquisition process, and unforeseen circumstances arising from future acquisitions could offset their anticipated benefits. Any of these factors could adversely affect the Company's results of operations, including its ability to generate positive operating cash flows.

#### **Susceptibility to Disruptive Technologies**

Acuity Brands is highly engaged in the investigation, development, and implementation of new technologies. Securing key partnerships and alliances, including having access to technologies generated by others and the obtaining of appropriate patents, play a significant role in protecting Acuity Brand's intellectual property and development activities. However, the continual development of new technologies (e.g., LEDs and

**Table of Contents****Index to Financial Statements**

lamp ballast systems) by existing and new source suppliers looking for either direct market access or partnership with competing large manufacturers, coupled with significant associated exclusivity and/or patent activity, could adversely affect the Company's, and specifically ABL's, ability to sustain operating profit margin and desirable levels of volume.

**Unexpected Development of Legal and Environmental Contingencies**

Acuity Brands is subject to various legal claims arising in the normal course of business, including patent infringement, environmental, and product liability claims. The Company establishes reserves for legal claims when the costs associated with the claims become probable and can be reasonably estimated. The actual costs of resolving legal claims may be substantially higher or lower than the amounts reserved for such claims. Changes from expectations for the resolution of outstanding legal and environmental claims and assessments, including the investigation related to the operation of ASP's wastewater pretreatment plant and other waste management practices at a facility in Atlanta, Georgia, could have a material impact on the Company's financial condition, including loss of governmental and related business, disruption of production, and higher operating costs at the Atlanta facility.

**Inability to Sustain Customer Relationships**

Acuity Brands is focused on improving product quality and enhancing its customer service capabilities in each segment. Relationships forged with customers, including The Home Depot, which represents approximately 13% of the Company's total net sales, are directly impacted by the Company's ability to deliver high quality products and service. Innovation in design and technology achieved by competitors could have a negative impact on customer acceptance of the Company's products. Additionally, the Company sources many materials and components used in our production processes from third-party suppliers. The Company has recently incurred recall costs associated with faulty items purchased from third-party suppliers. While the Company anticipates reimbursement for the majority of the recall costs, the inability to effectively manage customer relationships during the recall process could have an adverse effect on the Company's ability to maintain desired levels of profitability and volume.

**Attraction and Retention of a Highly Skilled Workforce**

The success of the Company is dependent upon the continued service of its highly skilled workforce, and its ability to attract and retain new personnel. The challenge to attract top talent is a formidable one given the competition for such talent within the Company's markets. Failure to maintain a qualified workforce could have a material adverse effect on the Company's results of operations.

**Item 2. Properties**

The general corporate offices of Acuity Brands are located in Atlanta, Georgia. Because of the diverse nature of operations and the large number of individual locations, it is neither practical nor meaningful to describe each of the operating facilities owned or leased by the Company. The following listing summarizes the significant facility categories by business:

Division	Owned	Leased	Nature of Facilities
Lighting Equipment	12	4	Manufacturing Facilities
		6	Warehouses
	1	5	Distribution Centers
	7	23	Offices
Specialty Products	4	2	Manufacturing Facilities
	4	37	Warehouses/Branches
		2	Distribution Centers
		9	Offices

**Table of Contents****Index to Financial Statements**

The following table provides additional geographic information related to Acuity Brands' manufacturing facilities:

	United				Total
	States	Canada	Mexico	Europe	
<b>Lighting Equipment</b>					
Owned	6		5	1	12
Leased	1		1	2	4
<b>Specialty Products</b>					
Owned	3			1	4
Leased		1		1	2
<b>Total</b>	<b>10</b>	<b>1</b>	<b>6</b>	<b>5</b>	<b>22</b>

None of the individual properties of Acuity Brands is considered to have a value that is significant in relation to the assets of Acuity Brands as a whole. Though a loss at certain facilities could have an impact on the Company's ability to serve the needs of its customers, the Company believes that the financial impact would be partially mitigated by various insurance programs in place. Acuity Brands believes that its properties are well maintained and are in good operating condition and that its properties are suitable and adequate for its present needs. The Company believes that it has additional capacity available at most of its production facilities and that it could increase production without substantial capital expenditures. As noted above, initiatives related to enhancing the global supply chain in the lighting equipment segment may continue to result in the consolidation of certain manufacturing facilities. However, the Company believes that the remaining facilities will have sufficient capacity to serve the current and projected needs of the customers of ABL.

**Item 3. Legal Proceedings****General**

Acuity Brands is subject to various legal claims arising in the normal course of business, including patent infringement and product liability claims. Based on information currently available, it is the opinion of management that the ultimate resolution of pending and threatened legal proceedings will not have a material adverse effect on the financial condition, results of operations, or cash flows of Acuity Brands. However, in the event of unexpected future developments, it is possible that the ultimate resolution of any such matters, if unfavorable, could have a material adverse effect on the financial condition, results of operations, or cash flows of Acuity Brands in future periods. Acuity Brands establishes reserves for legal claims when the costs associated with the claims become probable and can be reasonably estimated. The actual costs of resolving legal claims may be substantially higher than the amounts reserved for such claims. However, the Company cannot make a meaningful estimate of actual costs to be incurred that could possibly be higher or lower than the amounts reserved.

**Environmental Matters**

The operations of the Company are subject to numerous comprehensive laws and regulations relating to the generation, storage, handling, transportation, and disposal of hazardous substances as well as solid and hazardous wastes and to the remediation of contaminated sites. In addition, permits and environmental controls are required for certain of the Company's operations to limit air and water pollution, and these permits are subject to modification, renewal, and revocation by issuing authorities. On an ongoing basis, Acuity Brands invests capital and incurs operating costs relating to environmental compliance. Environmental laws and regulations have generally become stricter in recent years. The cost of responding to future changes may be substantial. Acuity Brands establishes reserves for known environmental claims when the costs associated with the claims become probable and can be reasonably estimated. The actual cost of environmental issues may be substantially higher or lower than that reserved due to difficulty in estimating such costs.



**Table of Contents**

**Index to Financial Statements**

Acuity Brands is currently a party to, or otherwise involved in, legal proceedings in connection with state and federal Superfund sites. With respect to each of the currently active sites which it does not own and where it has been named as a responsible party or a potentially responsible party ( PRP ), the Company believes its liability is immaterial, based on information currently available, due to its limited involvement at the site and/or the number of viable PRPs.

With respect to the only active site involving property which Acuity Brands does own and where it has been named as a PRP an ASP property in Atlanta, Georgia the Company and the current and former owners of adjoining properties have reached agreement to share the expected costs and responsibilities of implementing an approved corrective action plan to periodically monitor the property for a period of five years. Based on information currently available, the Company believes that its liability is immaterial in connection with the property; however, adverse monitoring results could result in additional charges to earnings in future periods, which cannot be estimated at this time.

During fiscal 2006, the United States Department of Justice ( DOJ ), through the United States Attorney for the Northern District of Georgia, continued its grand jury investigation of ASP s environmental practices. The investigation has primarily focused on the operation of ASP s wastewater pretreatment plant at ASP s primary manufacturing facility, located in Atlanta, Georgia, but has also included other matters such as the handling of past releases at that facility.

In connection with the DOJ investigation, the Environmental Protection Agency and the Company each analyzed samples taken from sumps at the facility that collect stormwater and groundwater, which have in the past been treated in the wastewater pretreatment plant along with manufacturing process wastewater from ASP s manufacturing operations. The sample results from the Company s tests indicated the presence of hazardous substances. As a result, the Company notified the Georgia Environmental Protection Division and is evaluating the possible need to conduct additional soil and groundwater studies pursuant to the Georgia Hazardous Site Response Act.

ASP and the Company have continued to cooperate with the DOJ investigation. The Company has estimated and accrued a liability for the cost of resolution of the DOJ proceedings. The DOJ proceedings are ongoing, and developments in the investigation and the terms of any final resolution, including whether the final resolution involves a civil or criminal disposition of the matter, could result in actual costs of resolution that are substantially higher or lower than the amount reserved. However, in light of the discretion afforded prosecutors in matters such as this, the Company cannot make a meaningful estimate of the actual costs that could possibly be higher or lower than the amount reserved. In addition to the direct costs of resolving this matter, the resolution could involve loss of governmental and related business, disruption of production, and higher operating costs at the Atlanta facility. Based on information currently available, the Company believes it will be able to resolve this matter without a material adverse impact on revenue, earnings, or cash flow. However, there can be no assurance that the resolution will not have such an impact.

***Item 4. Submission of Matters to a Vote of Security Holders***

No matters were submitted for a vote of the security holders during the three months ended August 31, 2006.

**Table of Contents****Index to Financial Statements****PART II****Item 5. Market for Registrant's Common Equity, Related Stockholder Matters, and Issuer Purchases of Equity Securities**

The common stock of Acuity Brands is listed on the New York Stock Exchange under the symbol AYI. At October 25, 2006, there were 4,935 stockholders of record. The following table sets forth the New York Stock Exchange high and low sale prices and the dividend payments for Acuity Brands' common stock for the periods indicated.

	Price per Share		Dividends
	High	Low	Per Share
<b>2006</b>			
First Quarter	\$ 31.96	\$ 26.75	\$ 0.15
Second Quarter	\$ 40.42	\$ 31.00	\$ 0.15
Third Quarter	\$ 44.35	\$ 37.91	\$ 0.15
Fourth Quarter	\$ 45.18	\$ 35.31	\$ 0.15
<b>2005</b>			
First Quarter	\$ 30.34	\$ 22.75	\$ 0.15
Second Quarter	\$ 32.24	\$ 24.53	\$ 0.15
Third Quarter	\$ 29.07	\$ 23.22	\$ 0.15
Fourth Quarter	\$ 29.67	\$ 23.90	\$ 0.15
<b>2004</b>			
First Quarter	\$ 24.34	\$ 17.73	\$ 0.15