

Fortune Brands Home & Security, Inc.
Form 10-Q
November 02, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended September 30, 2016

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 1-35166

FORTUNE BRANDS HOME & SECURITY, INC.

(Exact name of Registrant as specified in its charter)

DELAWARE
(State or other jurisdiction of

incorporation or organization)

520 Lake Cook Road, Deerfield, Illinois
(Address of principal executive offices)

62-1411546
(I.R.S. Employer

Identification No.)

60015-5611
(Zip Code)

Registrant's telephone number, including area code: (847) 484-4400

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

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

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

Large accelerated filer ☒

Accelerated filer ☐

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

Smaller reporting company ☐

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

The number of shares outstanding of the registrant's common stock, par value \$0.01 per share, at October 21, 2016 was 154,306,932.

PART I. FINANCIAL INFORMATION
Item 1. FINANCIAL STATEMENTS.**FORTUNE BRANDS HOME & SECURITY, INC.****CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME****For the Nine and Three Months Ended September 30, 2016 and 2015**

(In millions, except per share amounts)

(Unaudited)

| | Nine Months Ended September 30, | | Three Months Ended September 30, | |
|---|------------------------------------|------------|-------------------------------------|------------|
| | 2016 | 2015 | 2016 | 2015 |
| Net sales | \$ 3,683.3 | \$ 3,354.7 | \$ 1,279.0 | \$ 1,238.8 |
| Cost of products sold | 2,352.8 | 2,192.9 | 801.0 | 804.3 |
| Selling, general and administrative expenses | 831.4 | 778.1 | 284.5 | 265.7 |
| Amortization of intangible assets | 20.4 | 15.3 | 7.3 | 6.7 |
| Restructuring charges | 12.4 | 12.6 | 3.1 | 1.8 |
| Operating income | 466.3 | 355.8 | 183.1 | 160.3 |
| Interest expense | 37.5 | 20.5 | 11.8 | 11.1 |
| Other (income) expense, net | (0.1) | 3.7 | 0.6 | 0.5 |
| Income from continuing operations before income taxes | 428.9 | 331.6 | 170.7 | 148.7 |
| Income taxes | 120.9 | 112.7 | 48.8 | 48.7 |
| Income from continuing operations, net of tax | 308.0 | 218.9 | 121.9 | 100.0 |
| Income from discontinued operations, net of tax | 1.5 | 8.6 | 1.5 | 7.8 |
| Net income | 309.5 | 227.5 | 123.4 | 107.8 |
| Less: Noncontrolling interests | (0.1) | 0.3 | | 0.3 |
| Net income attributable to Fortune Brands | \$ 309.6 | \$ 227.2 | \$ 123.4 | \$ 107.5 |
| Basic earnings per common share | | | | |
| Continuing operations | \$ 2.00 | \$ 1.37 | \$ 0.79 | \$ 0.62 |
| Discontinued operations | 0.01 | 0.06 | 0.01 | 0.05 |
| Net income attributable to Fortune Brands common shareholders | \$ 2.01 | \$ 1.43 | \$ 0.80 | \$ 0.67 |
| Diluted earnings per common share | | | | |

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| | | | | | | | | |
|---|----|-------|----|-------|----|-------|----|------|
| Continuing operations | \$ | 1.95 | \$ | 1.34 | \$ | 0.77 | \$ | 0.61 |
| Discontinued operations | | 0.01 | | 0.05 | | 0.01 | | 0.05 |
| Net income attributable to Fortune Brands common shareholders | \$ | 1.96 | \$ | 1.39 | \$ | 0.78 | \$ | 0.66 |
| Comprehensive income | \$ | 309.8 | \$ | 195.1 | \$ | 110.5 | \$ | 93.2 |

See notes to condensed consolidated financial statements.

FORTUNE BRANDS HOME & SECURITY, INC.**CONDENSED CONSOLIDATED BALANCE SHEETS**

(In millions)

(Unaudited)

| | September 30, 2016 | December 31, 2015 |
|--|-----------------------|----------------------|
| Assets | | |
| Current assets | | |
| Cash and cash equivalents | \$ 278.6 | \$ 238.5 |
| Accounts receivable, net | 568.8 | 502.6 |
| Inventories | 562.5 | 555.6 |
| Other current assets | 129.8 | 121.3 |
| Total current assets | 1,539.7 | 1,418.0 |
| Property, plant and equipment, net of accumulated depreciation | 642.9 | 627.9 |
| Goodwill | 1,835.0 | 1,755.3 |
| Other intangible assets, net of accumulated amortization | 1,113.9 | 996.7 |
| Other assets | 81.1 | 77.8 |
| Total assets | \$ 5,212.6 | \$ 4,875.7 |
| Liabilities and equity | | |
| Current liabilities | | |
| Notes payable to banks | \$ | \$ 0.8 |
| Accounts payable | 361.9 | 344.2 |
| Other current liabilities | 414.8 | 412.9 |
| Total current liabilities | 776.7 | 757.9 |
| Long-term debt | 1,585.8 | 1,168.7 |
| Deferred income taxes | 170.6 | 201.7 |
| Accrued defined benefit plans | 208.0 | 218.4 |
| Other non-current liabilities | 111.3 | 75.2 |
| Total liabilities | 2,852.4 | 2,421.9 |
| Commitments and contingencies (see Note 17) | | |
| Equity | | |
| Fortune Brands stockholders' equity | | |
| Common stock ^(a) | 1.7 | 1.7 |
| Paid-in capital | 2,645.5 | 2,602.2 |
| Accumulated other comprehensive loss | (52.2) | (52.5) |
| Retained earnings | 738.4 | 501.6 |
| Treasury stock | (974.6) | (602.1) |

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| | | |
|---|------------|------------|
| Total Fortune Brands stockholders' equity | 2,358.8 | 2,450.9 |
| Noncontrolling interests | 1.4 | 2.9 |
| Total equity | 2,360.2 | 2,453.8 |
| Total liabilities and equity | \$ 5,212.6 | \$ 4,875.7 |

^(a) Common stock, par value \$0.01 per share; 177.7 million shares and 175.2 million shares issued at September 30, 2016 and December 31, 2015, respectively.

See notes to condensed consolidated financial statements.

FORTUNE BRANDS HOME & SECURITY, INC.**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****For the Nine Months Ended September 30, 2016 and 2015**

(In millions)

(Unaudited)

| | 2016 | 2015 |
|---|----------|-----------|
| Operating activities | | |
| Net income | \$ 309.5 | \$ 227.5 |
| Non-cash pre-tax expense (income): | | |
| Depreciation | 69.3 | 66.5 |
| Amortization | 20.4 | 15.3 |
| Stock-based compensation | 24.3 | 20.6 |
| Recognition of actuarial losses | 1.9 | 8.9 |
| Deferred income taxes | (23.0) | (22.7) |
| Restructuring charges | | 0.9 |
| Amortization of deferred financing costs | 3.0 | 0.4 |
| Pre-tax loss on sale of discontinued operations | | 16.9 |
| Loss (income) on sale of property, plant and equipment | 1.2 | (0.7) |
| Changes in assets and liabilities: | | |
| Increase in accounts receivable | (53.1) | (57.7) |
| Decrease (increase) in inventories | 22.6 | (52.7) |
| Increase in accounts payable | 28.7 | 5.6 |
| Increase in other assets | (11.6) | (11.2) |
| (Decrease) increase in accrued expenses and other liabilities | (12.0) | 35.6 |
| (Decrease) increase in accrued taxes | (0.6) | 24.6 |
| Net cash provided by operating activities | 380.6 | 277.8 |
| Investing activities | | |
| Capital expenditures ^(a) | (106.1) | (86.9) |
| Proceeds from the disposition of assets | 2.3 | 2.5 |
| Proceeds from sale of discontinued operations | | 12.2 |
| Cost of acquisitions, net of cash acquired | (230.5) | (652.8) |
| Net cash used in investing activities | (334.3) | (725.0) |
| Financing activities | | |
| Decrease in short-term debt, net | (1.0) | |
| Issuance of long-term debt | 880.0 | 1,748.9 |
| Repayment of long-term debt | (465.0) | (1,080.0) |
| Proceeds from the exercise of stock options | 24.8 | 22.6 |
| Treasury stock purchases ^(b) | (362.7) | (15.7) |

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| | | |
|---|----------|----------|
| Excess tax benefit from the exercise of stock-based compensation | | 23.0 |
| Employee withholding taxes paid related to stock-based compensation | (9.8) | (13.8) |
| Dividends to stockholders | (73.7) | (67.1) |
| Other financing, net | (2.1) | (1.1) |
| Net cash (used in) provided by financing activities | (9.5) | 616.8 |
| Effect of foreign exchange rate changes on cash | 3.3 | (10.9) |
| Net increase in cash and cash equivalents | \$ 40.1 | \$ 158.7 |
| Cash and cash equivalents at beginning of period | \$ 238.5 | \$ 191.9 |
| Cash and cash equivalents at end of period | \$ 278.6 | \$ 350.6 |

- (a) Capital expenditures of \$4.7 million and \$5.1 million that have not been paid as of September 30, 2016 and 2015, respectively, were excluded from the Statements of Cash Flows.
- (b) Treasury stock purchases exclude purchases of \$20.3 million of shares of common stock in September 2015 that were not settled until October 2015.

See notes to condensed consolidated financial statements.

FORTUNE BRANDS HOME & SECURITY, INC.**CONDENSED CONSOLIDATED STATEMENTS OF EQUITY****For the Nine Months Ended September 30, 2016 and 2015**

(In millions)

(Unaudited)

| | Common Stock | Paid-In Capital | Accumulated Other Comprehensive Income (Loss) | Retained Earnings | Treasury Stock | Non- controlling Interests | Total Equity |
|--|-----------------|--------------------|---|----------------------|-------------------|----------------------------------|-----------------|
| Balance at December 31, 2014 | \$ 1.7 | \$ 2,517.3 | \$ (6.7) | \$ 279.5 | \$ (532.3) | \$ 3.6 | \$ 2,263.1 |
| Comprehensive income: | | | | | | | |
| Net income | | | | 227.2 | | 0.3 | 227.5 |
| Other comprehensive income | | | (32.4) | | | | (32.4) |
| Stock options exercised | | 22.7 | | | | | 22.7 |
| Stock-based compensation | | 20.5 | | | (13.8) | | 6.7 |
| Tax benefit on exercise of stock options | | 21.2 | | | | | 21.2 |
| Treasury stock purchase | | | | | (36.0) | | (36.0) |
| Dividends (\$0.36 per common share) | | | | (67.3) | | | (67.3) |
| Dividends paid to noncontrolling interests | | | | | | (1.2) | (1.2) |
| Balance at September 30, 2015 | \$ 1.7 | \$ 2,581.7 | \$ (39.1) | \$ 439.4 | \$ (582.1) | \$ 2.7 | \$ 2,404.3 |
| Balance at December 31, 2015 | \$ 1.7 | \$ 2,602.2 | \$ (52.5) | \$ 501.6 | \$ (602.1) | \$ 2.9 | \$ 2,453.8 |
| Comprehensive income: | | | | | | | |
| Net income | | | | 309.6 | | (0.1) | 309.5 |
| Other comprehensive income | | | 0.3 | | | | 0.3 |
| Stock options exercised | | 24.8 | | | | | 24.8 |
| Stock-based compensation | | 24.3 | | | (9.8) | | 14.5 |
| Treasury stock purchase | | | | | (362.7) | | (362.7) |
| Dividends (\$0.28 per common share) | | | | (72.8) | | | (72.8) |
| Dividends paid to noncontrolling interests | | | | | | (1.4) | (1.4) |
| Other (see Note 9) | | (5.8) | | | | | (5.8) |
| Balance at September 30, 2016 | \$ 1.7 | \$ 2,645.5 | \$ (52.2) | \$ 738.4 | \$ (974.6) | \$ 1.4 | \$ 2,360.2 |

See notes to condensed consolidated financial statements.

FORTUNE BRANDS HOME & SECURITY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation and Principles of Consolidation

References to Fortune Brands, the Company, we, our and us refer to Fortune Brands Home & Security, Inc. and consolidated subsidiaries as a whole, unless the context otherwise requires.

The Company is a leading home and security products company with a portfolio of leading branded products used for residential home repair, remodeling, new construction and security applications.

The condensed consolidated balance sheet as of September 30, 2016, the related condensed consolidated statements of comprehensive income for the nine and three-month periods ended September 30, 2016 and 2015 and the related condensed consolidated statements of cash flows and equity for the nine-month periods ended September 30, 2016 and 2015 are unaudited. In the opinion of management, all adjustments (consisting of normal recurring accruals) necessary for a fair statement of the financial statements have been included. Interim results may not be indicative of results for a full year.

The condensed consolidated financial statements and notes are presented pursuant to the rules and regulations of the Securities and Exchange Commission and do not contain certain information included in our annual consolidated financial statements and notes. The December 31, 2015 condensed consolidated balance sheet was derived from the audited financial statements, but does not include all disclosures required by U.S. generally accepted accounting principles (GAAP). This Quarterly Report on Form 10-Q should be read in conjunction with the audited consolidated financial statements and notes included in our Annual Report on Form 10-K for the year ended December 31, 2015.

The condensed consolidated financial statements included in this Quarterly Report on Form 10-Q were derived principally from the consolidated financial statements of the Company. In May 2015, we acquired Norcraft Companies, Inc. (Norcraft). The financial results of Norcraft were included in the Company's condensed consolidated statements of comprehensive income and statements of cash flow for the nine and three months ended September 30, 2016 and 2015 and the condensed consolidated balance sheet as of September 30, 2016 and December 31, 2015. In September 2015, we completed the sale of Waterloo Industries, Inc. (Waterloo), our tool storage business. In accordance with Accounting Standards Codification (ASC) requirements, the results of operations of Waterloo were classified and separately stated as discontinued operations in the accompanying condensed consolidated statements of comprehensive income for the nine and three months ended September 30, 2015. The cash flows from discontinued operations for the nine months ending September 30, 2015 were not separately classified on the accompanying condensed consolidated statements of cash flows. Information on Business Segments was revised to exclude these discontinued operations.

FORTUNE BRANDS HOME & SECURITY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

2. Recently Issued Accounting Standards

Classification of Certain Cash Receipts and Cash Payments

In September 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-15 that will change how an entity classifies certain cash receipts and cash payments on its statement of cash flows. The key changes that may potentially impact our financial statements include the following: 1) Cash payments for debt prepayment or extinguishment costs should be classified as financing cash outflows; 2) Contingent consideration payments that are not made within three months after the consummation of a business combination would be classified as financing (if payment made is up to the acquisition date fair value of liability) or operating outflows (if in excess of acquisition fair value). Cash payments made soon after the consummation of a business combination generally will be classified as cash outflows for investing activities; 3) Insurance settlement proceeds, would be classified based on the nature of the loss; and 4) Company-owned life insurance settlement proceeds would be presented as investing cash inflows, and premiums could be classified as investing or operating cash outflows, or a combination of both. The new standard is effective beginning January 1, 2018 and should be adopted retrospectively. Early adoption is permitted. We are assessing the impact the adoption of this standard will have on our financial statements.

Financial Instruments Credit Losses

In June 2016, the FASB issued ASU 2016-13 that changes the impairment model for most financial assets and certain other instruments that are not measured at fair value through net income. The new guidance applies to most financial assets measured at amortized cost, including trade and other receivables and loans as well as off-balance-sheet credit exposures (e.g., loan commitments, standby letters of credit). The standard will replace the incurred loss approach under the current guidance with an expected loss model that requires an entity to estimate its lifetime expected credit loss . The new standard is effective beginning January 1, 2020 and early application is permitted but not earlier than January 1, 2019. We are assessing the impact the adoption of this standard will have on our financial statements.

FORTUNE BRANDS HOME & SECURITY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

2. Recently Issued Accounting Standards (Continued)

Improvements to Employee Share-Based Payment Accounting

In March 2016, the FASB issued ASU 2016-09 that requires entities to recognize the income tax effects of share-based awards in the income statement when the awards vest or are settled. The new standard also allows entities to withhold an amount up to an employee's maximum individual tax rate in the relevant jurisdiction without resulting in liability classification of the award. The new standard is effective for annual and interim periods beginning January 1, 2017. We early adopted this standard as of June 30, 2016.

We have reclassified \$9.8 million and \$13.8 million of employee withholding taxes paid from operating into financing activities in the statement of cash flows for the nine months ended September 30, 2016 and September 30, 2015, respectively, as required by ASU 2016-09 (adopted retrospectively).

FORTUNE BRANDS HOME & SECURITY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

2. Recently Issued Accounting Standards (Continued)

Simplifying the Transition to the Equity Method of Accounting

In March 2016, the FASB issued ASU 2016-07, which eliminates the requirement to apply the equity method of accounting retrospectively when an entity obtains significant influence over a previously held investment. Previously, entities were required to retrospectively apply the equity method of accounting when obtaining significant influence over an investment (for example due to an increase in ownership). The new standard is effective beginning January 1, 2017. Earlier application is permitted, however we elected not to early adopt. We do not expect this standard to have a material effect on our financial statements.

Leases

In February 2016, the FASB issued ASU 2016-02, *Leases* that requires lessees to recognize almost all leases on their balance sheet as a right-of-use asset and lease liability but recognize related expenses in a manner similar to current accounting. The guidance also eliminates current real estate-specific provisions for all entities. The new standard is effective for annual periods beginning after December 15, 2018 (calendar year 2019 for Fortune Brands) and earlier application is permitted. We are assessing the impact the adoption of this standard will have on our financial statements.

Recognition and Measurement of Financial Assets and Financial Liabilities

In January 2016, the FASB issued final guidance ASU 2016-01 that requires entities to measure investments in unconsolidated entities (other than those accounted for using the equity method of accounting) at fair value through the income statement. There will no longer be an available-for-sale classification (with changes in fair value reported in Other Comprehensive Income). In addition, the cost method is eliminated for equity investments without readily determinable fair values. The new standard is effective beginning January 1, 2018. Earlier application is permitted for certain provisions of the standard, however we elected not to early adopt. We do not expect this standard to have a material effect on our financial statements.

FORTUNE BRANDS HOME & SECURITY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

2. Recently Issued Accounting Standards (Continued)

Simplifying Subsequent Measurement of Inventory

In July 2015, the FASB issued a final standard that simplifies the subsequent measurement of inventory by replacing the current standard of lower of cost or market test. Under the current guidance the subsequent measurement of inventory is measured at the lower of cost or market, where market may have multiple possible outcomes. The new guidance requires subsequent measurement of inventory at the lower of cost or net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs to sell (completion, disposal, and transportation). This new standard is effective for the annual period beginning January 1, 2017. Earlier application is permitted, however we elected not to early adopt. We do not expect this standard to have a material effect on our financial statements.

Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern

In August 2014, the FASB issued ASU 2014-15, Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. This ASU provides guidance about management's responsibility to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and to provide related footnote disclosures. This amendment is effective for the annual period ending after December 15, 2016 (calendar year 2017 for Fortune Brands), and for annual periods and interim periods thereafter. Early application is permitted, however we elected not to early adopt. We do not expect this standard to have a material effect on our financial statements.

Revenue from Contracts with Customers

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. This ASU clarifies the accounting for revenue arising from contracts with customers and specifies the disclosures that an entity should include in its financial statements. The standard is effective for annual reporting periods beginning after December 15, 2017 (calendar year 2018 for Fortune Brands). During the first half of 2016, the FASB issued the final amendments to the standard relating to the principal versus agent guidance, accounting for licenses of intellectual property and identifying performance obligations as well as the guidance on transition, collectability, noncash consideration and the presentation of sales and other similar taxes. The effective date and transition requirements for these amendments are the same as those of the new revenue standard. We expect to complete our assessment of the impact of adoption in the second quarter of 2017 and finalize the adoption process of the new revenue standard by the end of 2017.

FORTUNE BRANDS HOME & SECURITY, INC.**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****3. Balance Sheet Information**

Supplemental information on our balance sheets is as follows:

| (In millions) | September 30, 2016 | December 31, 2015 |
|---|-----------------------|----------------------|
| Inventories: | | |
| Raw materials and supplies | \$ 215.5 | \$ 237.8 |
| Work in process | 51.6 | 60.2 |
| Finished products | 295.4 | 257.6 |
| Total inventories | \$ 562.5 | \$ 555.6 |
| Property, plant and equipment, gross | \$ 1,613.7 | \$ 1,551.7 |
| Less: accumulated depreciation | 970.8 | 923.8 |
| Property, plant and equipment, net | \$ 642.9 | \$ 627.9 |

4. Acquisitions

In September 2016, we acquired ROHL, a California-based luxury plumbing company. In a related transaction, we also acquired TCL Manufacturing Ltd, which gave us 100% ownership of Perrin & Rowe, a UK manufacturer and designer of luxury kitchen and bathroom plumbing products. The total combined purchase price was approximately \$166 million (including \$3 million of liabilities assumed), subject to certain post-closing adjustments. We financed the transaction using cash on hand and borrowings under our existing credit facilities. Net sales and operating income in the three months ended September 30, 2016 were not material to the Company. The results of operations are included in the Plumbing segment.

In May 2016, we acquired Riobel, a Canadian plumbing company specializing in premium showroom bath and shower fittings, for a total purchase price of \$88.4 million in cash, subject to certain post-closing adjustments. We financed the transaction using cash on hand and borrowings under our existing credit facilities. Net sales and operating income in the nine and three months ended September 30, 2016 were not material to the Company. The results of operations are included in the Plumbing segment.

In May 2015, we completed our tender offer to purchase all of the outstanding shares of common stock of Norcraft, a leading publicly-owned manufacturer of kitchen and bathroom cabinetry, for a total purchase price of \$648.6 million in cash. We financed the transaction using cash on hand and borrowings under our existing credit facilities. This transaction is expected to strengthen our overall product offering, round out our regional market penetration and enhance our frameless cabinetry capabilities. The results of operations of Norcraft are included in the Cabinets segment. We incurred \$15.1 million of Norcraft acquisition-related transaction costs during the year ended December 31, 2015. The goodwill deductible for income tax purposes is \$66.2 million.

FORTUNE BRANDS HOME & SECURITY, INC.**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****4. Acquisitions (Continued)**

During the third quarter of 2016 and following the completion of the Norcraft purchase accounting measurement period, the Company identified certain immaterial prior period balance sheet misstatements relating to calculation of deferred tax liabilities as disclosed in the purchase price allocation related to the Norcraft acquisition. The correction of the cumulative misstatement during the third quarter of 2016 resulted in a \$24.3 million and \$15.4 million reduction in Norcraft's deferred tax liabilities and the carrying value of goodwill, respectively, and an offsetting increase of \$8.9 million in the uncertain tax positions accrual. The Company assessed the materiality of these misstatements on previously issued financial statements and concluded that the misstatements were not material to the Consolidated Financial Statements for any interim or annual periods taken as a whole.

The following table summarizes the final allocation of the purchase price to the fair values of assets acquired and liabilities assumed as of the date of the Norcraft acquisition.

| | |
|--|-----------------|
| (In millions) | |
| Accounts receivable | \$ 30.8 |
| Inventories | 28.6 |
| Property, plant and equipment | 45.3 |
| Goodwill | 290.6 |
| Identifiable intangible assets | 360.0 |
| Other assets | 9.4 |
| Total assets | 764.7 |
| Deferred tax liabilities | 75.6 |
| Other liabilities and accruals | 40.5 |
| Net assets acquired^(a) | \$ 648.6 |

^(a) *Net assets exclude \$15.5 million of cash transferred to the Company as the result of the Norcraft acquisition.* Goodwill includes expected sales and cost synergies. Identifiable intangible assets consist of an indefinite-lived tradename of \$150 million and customer relationships of \$210 million. The useful life of the customer relationships identifiable intangible asset was estimated to be 20 years.

The following unaudited pro forma summary presents consolidated financial information as if Norcraft had been acquired on January 1, 2014. The unaudited pro forma financial information is based on historical results of operations and financial position of the Company and Norcraft. The pro forma results include:

estimated amortization of a definite-lived customer relationship intangible asset (amortized using the straight-line method),

the estimated cost of the inventory adjustment to fair value,

interest expense associated with debt that would have been incurred in connection with the acquisition,

the reclassification of Norcraft transaction costs from 2015 to the first quarter of 2014, and

adjustments to conform accounting policies.

FORTUNE BRANDS HOME & SECURITY, INC.**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****4. Acquisitions (Continued)**

The unaudited pro forma financial information does not necessarily represent the results that would have occurred had the Norcraft acquisition occurred on January 1, 2014. In addition, the unaudited pro forma information should not be deemed to be indicative of future results.

| | Nine Months Ended Three Months Ended | |
|---|--------------------------------------|---------------|
| | September 30, | September 30, |
| (In millions, except per share amounts) | 2015 | 2015 |
| Net sales | \$ 3,497.0 | \$ 1,238.7 |
| Income from continuing operations | 235.0 | 100.1 |
| Basic earnings per common share | \$ 1.47 | \$ 0.62 |
| Diluted earnings per common share | \$ 1.44 | \$ 0.61 |

In March 2015, we acquired a Cabinets component company for approximately \$6 million in cash. This acquisition did not have a material impact on our financial statements.

5. Discontinued Operations

In September 2015, we completed the sale of Waterloo for approximately \$14 million in cash, subject to certain post-closing adjustments. We recorded a pre-tax loss of \$16.9 million as the result of this sale. Transaction and other sale-related costs were approximately \$2.8 million. The estimated tax benefit on the sale was \$26.5 million with the after-tax gain of \$7.0 million recorded within discontinued operations. The estimated tax benefit resulted primarily from a tax loss in excess of the financial reporting loss as a result of prior period nondeductible asset impairments. Waterloo is presented as a discontinued operation in our financial statements beginning January 1, 2015 and through the date of sale in accordance with ASC 205 requirements. Prior to classifying Waterloo as a discontinued operation, it was reported in the Security segment.

The condensed consolidated statements of comprehensive income and condensed consolidated balance sheets for all prior periods have been adjusted to reflect the presentation of Waterloo as discontinued operations.

The following table summarizes the results of discontinued operations for the nine and three months ended September 30, 2015.

| | Nine Months Ended Three Months Ended | |
|---------------|--------------------------------------|---------------|
| | September 30, | September 30, |
| (in millions) | 2015 | 2015 |
| Net sales | \$ 78.2 | \$ 27.8 |

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| | | | | |
|---|----|--------|----|--------|
| Loss from discontinued operations before income taxes | \$ | (15.6) | \$ | (17.2) |
| Income taxes | | (24.2) | | (25.0) |
| Income from discontinued operations, net of tax | \$ | 8.6 | \$ | 7.8 |

FORTUNE BRANDS HOME & SECURITY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

6. Goodwill and Identifiable Intangible Assets

We had goodwill of \$1,835.0 million and \$1,755.3 million as of September 30, 2016 and December 31, 2015, respectively. The \$79.7 million increase was primarily due to the acquisitions in the Plumbing segment partially offset by the correction of Norcraft tax misstatements as discussed in Note 4. The change in the net carrying amount of goodwill by segment was as follows:

| (In millions) | Cabinets | Plumbing | Doors | Security | Total Goodwill |
|---|----------|----------|----------|----------|----------------|
| Goodwill at December 31, 2015 ^(a) | \$ 937.7 | \$ 578.6 | \$ 143.0 | \$ 96.0 | \$ 1,755.3 |
| Year-to-date translation adjustments | 1.8 | (1.5) | | 0.7 | 1.0 |
| Acquisition-related adjustments | (14.2) | 92.9 | | | 78.7 |
| Goodwill at September 30, 2016 ^(a) | \$ 925.3 | \$ 670.0 | \$ 143.0 | \$ 96.7 | \$ 1,835.0 |

^(a) Net of accumulated impairment losses of \$399.5 million in the Doors segment.

We also had identifiable intangible assets, principally tradenames, of \$1,113.9 million and \$996.7 million, net of accumulated amortization, as of September 30, 2016 and December 31, 2015, respectively. The \$140.7 million increase in gross identifiable intangible assets was primarily due to the acquisitions in our Plumbing segment.

The gross carrying value and accumulated amortization by class of identifiable intangible assets as of September 30, 2016 and December 31, 2015 were as follows:

| (In millions) | As of September 30, 2016 | | | As of December 31, 2015 | | |
|--|--------------------------|--------------------------|----------------|-------------------------|--------------------------|----------------|
| | Gross Carrying Amounts | Accumulated Amortization | Net Book Value | Gross Carrying Amounts | Accumulated Amortization | Net Book Value |
| Indefinite-lived tradenames | \$ 679.1 | \$ | \$ 679.1 | \$ 638.6 | \$ | \$ 638.6 |
| Amortizable intangible assets | | | | | | |
| Tradenames | 16.4 | (7.6) | 8.8 | 19.1 | (8.6) | 10.5 |
| Customer and contractual relationships | 605.9 | (197.2) | 408.7 | 511.2 | (177.4) | 333.8 |
| Patents/proprietary technology | 62.9 | (45.6) | 17.3 | 54.7 | (40.9) | 13.8 |
| Total | 685.2 | (250.4) | 434.8 | 585.0 | (226.9) | 358.1 |
| Total identifiable intangibles | \$ 1,364.3 | \$ (250.4) | \$ 1,113.9 | \$ 1,223.6 | \$ (226.9) | \$ 996.7 |

FORTUNE BRANDS HOME & SECURITY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

6. Goodwill and Identifiable Intangible Assets (Continued)

Amortizable identifiable intangible assets, principally tradenames and customer relationships, are subject to amortization over their estimated useful life, ranging from 3 to 30 years, based on the assessment of a number of factors that may impact useful life. These factors include historical tradename performance with respect to consumer name recognition, geographic market presence, market share, plans for ongoing tradename support and promotion, customer attrition rates, and other relevant factors.

During the first nine months of 2016, no events or circumstances occurred that would have required us to perform interim impairment tests of goodwill or indefinite-lived intangible assets.

7. External Debt and Financing Arrangements

In June 2016, the Company amended and restated its credit agreement to combine and rollover the existing revolving credit facility and term loan into a new standalone \$1.25 billion revolving credit facility. This amendment of the credit agreement was a non-cash transaction for the Company. Terms and conditions of the credit agreement, including the total commitment amount, essentially remained the same. The revolving credit facility matures in June 2021 and borrowings thereunder will be used for general corporate purposes. On September 30, 2016 and December 31, 2015, our outstanding borrowings under these facilities, net of debt issuance costs relating to the term loan balance, were \$695.0 million and \$279.0 million, respectively. At September 30, 2016 and December 31, 2015, the current portion of long-term debt was zero. Interest rates under the facility are variable based on LIBOR at the time of the borrowing and the Company's long-term credit rating and can range from LIBOR + 0.9% to LIBOR + 1.5%. As of September 30, 2016, we were in compliance with all covenants under this facility. As a result of the refinancing, we wrote-off prepaid debt issuance costs of approximately \$1.3 million as of June 30, 2016. We retrospectively adopted ASU 2015-03, *Simplifying the Presentation of Debt Issuance Costs*, on January 1, 2016, resulting in the reclassification of approximately \$3 million of debt issuance costs from other current assets and other assets to long-term debt as of December 31, 2015. Adoption of this new guidance did not impact the Company's equity, results of operations or cash flows.

In June 2015, we issued \$900 million of unsecured senior notes (*Senior Notes*) in a registered public offering. The Senior Notes consist of two tranches: \$400 million of five-year notes due 2020 with a coupon of 3% and \$500 million of ten-year notes due 2025 with a coupon of 4%. We used the proceeds from the Senior Notes offering to pay down our revolving credit facility and for general purposes. On September 30, 2016 and December 31, 2015, the outstanding amount of the Senior Notes, net of underwriting commissions, price discounts and debt issuance costs, was \$890.8 million and \$889.7 million, respectively.

FORTUNE BRANDS HOME & SECURITY, INC.**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****7. External Debt and Financing Arrangements (Continued)**

We currently have uncommitted bank lines of credit in China, which provide for unsecured borrowings for working capital of up to \$25.7 million in aggregate, of which zero and \$0.8 million was outstanding, as of September 30, 2016 and December 31, 2015, respectively. There were no borrowings in the nine and three-month periods ended September 30, 2015.

8. Financial Instruments

We do not enter into financial instruments for trading or speculative purposes. We principally use financial instruments to reduce the impact of changes in foreign currency exchange rates and commodity prices used as raw materials in our products. The principal derivative financial instruments we enter into on a routine basis are foreign exchange contracts. Derivative financial instruments are recorded at fair value. The counterparties to derivative contracts are major financial institutions. Management currently believes that the risk of incurring material losses is unlikely and that the losses, if any, would be immaterial to the Company. In addition, from time to time, we enter into commodity swaps.

Our primary foreign currency hedge contracts pertain to the Canadian dollar, the Mexican peso and the Chinese yuan. The gross U.S. dollar equivalent notional amount of all foreign currency derivative hedges outstanding at September 30, 2016 was \$212.2 million, representing a net settlement liability of \$2.6 million. Based on foreign exchange rates as of September 30, 2016, we estimate that \$2.4 million of net foreign currency derivative losses included in other comprehensive income as of September 30, 2016 will be reclassified to earnings within the next twelve months.

The fair values of derivative instruments on the consolidated balance sheets as of September 30, 2016 and December 31, 2015 were:

| (In millions) | | Fair Value | |
|----------------------------|---------------------------|--------------------|-------------------|
| | Location | September 30, 2016 | December 31, 2015 |
| <u>Assets</u> | | | |
| Foreign exchange contracts | Other current assets | \$ 1.2 | \$ 6.7 |
| Net investment hedges | Other current assets | | 0.1 |
| | Total assets | \$ 1.2 | \$ 6.8 |
| <u>Liabilities</u> | | | |
| Foreign exchange contracts | Other current liabilities | \$ 3.6 | \$ 3.1 |
| Net investment hedges | Other current liabilities | 0.2 | |

| | | | |
|-------------------|-------|----|-----|
| Total liabilities | \$3.8 | \$ | 3.1 |
|-------------------|-------|----|-----|

FORTUNE BRANDS HOME & SECURITY, INC.**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****8. Financial Instruments (Continued)**

The effects of derivative financial instruments on the statements of comprehensive income for the nine and three months ended September 30, 2016 and 2015 were:

| (In millions) | | Gain (Loss) Recognized in Income Nine Months Ended September 30, | |
|---------------|--------------------------------|---|---------------|
| Type of hedge | Location | 2016 | 2015 |
| Cash flow | Cost of products sold | \$ (2.6) | \$ 3.0 |
| Fair value | Other (income) expense, net | 1.3 | 5.9 |
| Total | | \$ (1.3) | \$ 8.9 |

| (In millions) | | Gain (Loss) Recognized in Income Three Months Ended September 30, | |
|---------------|--------------------------------|--|---------------|
| Type of hedge | Location | 2016 | 2015 |
| Cash flow | Cost of products sold | \$ (1.2) | \$ 1.0 |
| Fair value | Other (income) expense, net | 0.3 | 3.2 |
| Total | | \$ (0.9) | \$ 4.2 |

The effective portion of cash flow hedges recognized in other comprehensive income were net (losses) gains of \$(8.0) million and \$4.4 million in the nine months ended September 30, 2016 and 2015, respectively. The effective portion of cash flow hedges recognized in other comprehensive income were net (losses) gains of zero and \$2.4 million in the three months ended September 30, 2016 and 2015, respectively. In the nine and three months ended September 30, 2016 and 2015, the ineffective portion of cash flow hedges recognized in other (income) expense, net, was insignificant.

9. Fair Value Measurements

ASC requirements for Fair Value Measurements and Disclosures establish a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three levels. Level 1 inputs, the highest priority, are quoted prices in active markets for identical assets or liabilities. Level 2 inputs reflect inputs other than quoted prices included in level 1 that are either observable directly or through corroboration with observable market data. Level 3 inputs are unobservable inputs, due to little or no market activity for the asset or liability, such as internally-developed valuation models.

FORTUNE BRANDS HOME & SECURITY, INC.**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****9. Fair Value Measurements (Continued)**

The carrying value, net of underwriting commissions, price discounts and debt issuance costs and fair value of debt as of September 30, 2016 and December 31, 2015 were as follows:

| (In millions) | September 30, 2016 | | December 31, 2015 | |
|---|-----------------------|---------------|-------------------|---------------|
| | Carrying Value | Fair Value | Carrying Value | Fair Value |
| Revolving credit facility | \$ 695.0 | \$ 695.0 | \$ | \$ |
| Notes payable to bank | | | 0.8 | 0.8 |
| Term loan | | | 279.0 | 280.0 |
| Senior Notes, net of underwriting commissions and price discounts | 890.8 | 944.5 | 889.7 | 894.1 |

The estimated fair value of our Senior notes and term loan is determined primarily using broker quotes, which are level 2 inputs.

Assets and liabilities measured at fair value on a recurring basis as of September 30, 2016 and December 31, 2015 were as follows:

| (In millions) | Fair Value | |
|--|-----------------------|----------------------|
| | September 30, 2016 | December 31, 2015 |
| Assets | | |
| Derivative financial instruments (level 2) | \$ 1.2 | \$ 6.8 |
| Deferred compensation program assets (level 2) | 3.3 | 3.1 |
| Total assets | \$ 4.5 | \$ 9.9 |
| Liabilities | | |
| Derivative financial instruments (level 2) | \$ 3.8 | \$ 3.1 |

During the second quarter of 2016, we entered into a joint venture arrangement with a partner to operate a manufacturing facility in China. Under the arrangement, we are required to make certain fixed payments to our partner each year starting in June 2017 and through June 2024 (final year of the agreement) and also purchase the outstanding preferred shares of our partner in 2024. During the second quarter of 2016, we recognized the fair value of \$8.2 million of these contractual payments, including a redemption of the preferred shares (\$7.2 million within other non-current liabilities and \$1.0 million due within one year in other current liabilities). We have also recognized the excess of \$5.2 million of this liability fair value over the \$3.0 million cash contributed by our partner within paid-in capital.

FORTUNE BRANDS HOME & SECURITY, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
10. Accumulated Other Comprehensive Loss

Total accumulated other comprehensive loss consists of net income and other changes in business equity from transactions and other events from sources other than shareholders. It includes currency translation gains and losses, unrealized gains and losses from derivative instruments designated as cash flow hedges, and defined benefit plan adjustments. The components of and changes in accumulated other comprehensive loss, net of tax, were as follows:

| (In millions) | Foreign Currency Adjustments | Derivative Hedging Gain (Loss) | Defined Benefit Plan Adjustments ^(a) | Accumulated Other Comprehensive Loss |
|--|------------------------------------|---|---|---|
| Balance at December 31, 2014 | \$ 31.0 | \$ (0.6) | \$ (37.1) | \$ (6.7) |
| Amounts classified into accumulated other comprehensive loss | (29.0) | 2.6 | (3.8) | (30.2) |
| Amounts reclassified from accumulated other comprehensive loss | | (1.5) | (0.7) | (2.2) |
| Net current-period other comprehensive loss | (29.0) | 1.1 | (4.5) | (32.4) |
| Balance at September 30, 2015 | \$ 2.0 | \$ 0.5 | \$ (41.6) | \$ (39.1) |
| Balance at December 31, 2015 | \$ (13.3) | \$ 2.1 | \$ (41.3) | \$ (52.5) |
| Amounts classified into accumulated other comprehensive loss | 0.9 | (7.3) | 9.0 | 2.6 |
| Amounts reclassified from accumulated other comprehensive loss | | 2.8 | (5.1) | (2.3) |
| Net current-period other comprehensive loss | 0.9 | (4.5) | 3.9 | 0.3 |
| Balance at September 30, 2016 | \$ (12.4) | \$ (2.4) | \$ (37.4) | \$ (52.2) |

^(a) See Note 11, *Defined Benefit Plans*, for further information on the adjustments related to defined benefit plans.

FORTUNE BRANDS HOME & SECURITY, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**10. Accumulated Other Comprehensive Loss (Continued)**

The reclassifications out of accumulated other comprehensive loss for the nine and three months ended September 30, 2016 and 2015 were as follows:

(In millions)

| Affected Line Item in | | | |
|---|--------------------------------------|----------------------|------------------------|
| Details about Accumulated Other Comprehensive Amount Reclassified from the Statement of | Accumulated Other Comprehensive Loss | Comprehensive Income | |
| Loss Components | Nine Months Ended September 30, | | |
| | 2016 | 2015 | |
| <u>Cumulative translation adjustments</u> | \$ | \$ | |
| <u>(Losses) gains on cash flow hedges</u> | | | |
| Foreign exchange contracts | \$ (2.5) | \$ 3.3 | Cost of products sold |
| Commodity contracts | (0.1) | (0.3) | Cost of products sold |
| | (2.6) | 3.0 | Total before tax |
| | (0.2) | (1.5) | Tax expense |
| | \$ (2.8) | \$ 1.5 | (Loss) gain net of tax |
| <u>Defined benefit plan items</u> | | | |
| Recognition of prior service credits | \$ 10.0 | \$ 10.2 | (a) |
| Recognition of actuarial losses | (1.9) | (2.8) | (a) |
| Recognition of prior service costs in discontinued operations | | (0.2) | (b) |
| Recognition of actuarial losses in discontinued operations | | (6.1) | (b) |
| | 8.1 | 1.1 | Total before tax |
| | (3.0) | (0.4) | Tax expense |
| | \$ 5.1 | \$ 0.7 | Gains net of tax |
| Total reclassifications for the period | \$ 2.3 | \$ 2.2 | Gains net of tax |

FORTUNE BRANDS HOME & SECURITY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

10. Accumulated Other Comprehensive Loss (Continued)

(In millions)

| Details about Accumulated Other Comprehensive | Amount Reclassified from Accumulated Other Comprehensive Three Months Ended September 30, 2016 2015 | | Affected Line Item in the Statement of Comprehensive Income |
|---|---|----------|--|
| Loss Components | | | |
| <u>Cumulative translation adjustments</u> | \$ | \$ | |
| <u>Gains (losses) on cash flow hedges</u> | | | |
| Foreign exchange contracts | \$ (1.3) | \$ 1.2 | Cost of products sold |
| Commodity contracts | 0.1 | (0.2) | Cost of products sold |
| | (1.2) | 1.0 | Total before tax |
| | | (0.5) | Tax expense |
| | \$ (1.2) | \$ 0.5 | (Loss) gain net of tax |
| <u>Defined benefit plan items</u> | | | |
| Recognition of prior service credits | \$ 3.8 | \$ 3.2 | (a) |
| Recognition of actuarial losses | (1.0) | (2.8) | (a) |
| Recognition of prior service costs in discontinued operations | | (0.2) | (b) |
| Recognition of actuarial losses in discontinued operations | | (6.1) | (b) |
| | 2.8 | (5.9) | Total before tax |
| | (1.0) | 2.3 | Tax expense |
| | \$ 1.8 | \$ (3.6) | Gain (loss) net of tax |
| Total reclassifications for the period | \$ 0.6 | \$ (3.1) | Gain (loss) net of tax |

(a) These accumulated other comprehensive loss components are included in the computation of net periodic benefit cost. Refer to Note 11, *Defined Benefit Plans*, for additional information.

(b) These accumulated other comprehensive loss components are included in discontinued operations.

FORTUNE BRANDS HOME & SECURITY, INC.**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****11. Defined Benefit Plans**

The components of net periodic benefit cost for pension and postretirement benefits for the nine and three months ended September 30, 2016 and 2015 were as follows:

| (In millions) | Nine Months Ended September 30, | | | |
|--|---------------------------------|--------|-------------------------|-----------|
| | Pension Benefits | | Postretirement Benefits | |
| | 2016 | 2015 | 2016 | 2015 |
| Service cost | \$ 7.2 | \$ 8.7 | \$ | \$ |
| Interest cost | 25.8 | 25.2 | 0.2 | 0.4 |
| Expected return on plan assets | (27.9) | (30.3) | | |
| Recognition of prior service costs (credits) | | 0.1 | (10.0) | (10.3) |
| Recognition of actuarial losses (gains) | | 2.9 | 1.9 | (0.1) |
| Net periodic benefit cost (income) | \$ 5.1 | \$ 6.6 | \$ (7.9) | \$ (10.0) |

| (In millions) | Three Months Ended September 30, | | | |
|--|----------------------------------|--------|-------------------------|----------|
| | Pension Benefits | | Postretirement Benefits | |
| | 2016 | 2015 | 2016 | 2015 |
| Service cost | \$ 1.6 | \$ 2.3 | \$ | \$ |
| Interest cost | 8.4 | 8.3 | (0.1) | 0.1 |
| Expected return on plan assets | (8.9) | (9.9) | | |
| Recognition of prior service costs (credits) | | 0.1 | (3.8) | (3.3) |
| Recognition of actuarial losses (gains) | | 2.9 | 1.0 | (0.1) |
| Net periodic benefit cost (income) | \$ 1.1 | \$ 3.7 | \$ (2.9) | \$ (3.3) |

In the first quarter of 2013, the Company communicated a plan amendment to reduce health benefits to certain retired employees. Due to the risk of litigation at the time of the initial communication, the Company elected to defer the full recognition of the benefit arising from the plan amendment. Following a favorable court decision in the first quarter of 2016, the Company determined that it was now probable that it would realize the benefit from the plan amendment. As a result, the Company performed a re-measurement of the affected retiree plan liability as of March 31, 2016. This remeasurement resulted in a \$10.7 million reduction of accrued retiree benefit plan liabilities and a corresponding increase in prior service credits. These prior service credits will be amortized over the next eight months after September 30, 2016. In addition, we recorded a \$0.9 million actuarial loss during the first quarter of 2016.

In the third quarter of 2015, we recognized actuarial losses of \$6.1 million related to the sale of the Waterloo tool storage business in discontinued operations in addition to the \$2.8 million of actuarial losses reflected above.

FORTUNE BRANDS HOME & SECURITY, INC.**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****12. Income Taxes**

The effective income tax rates for the nine months ended September 30, 2016 and 2015 were 28.2% and 34.0%, respectively. In 2016, the effective income tax rate was favorably impacted by a tax benefit related to the adoption of ASU 2016-09, the new accounting guidance relating to share-based compensation. The effective income tax rate for 2015 was unfavorably impacted by the tax cost related to the final settlement of a federal income tax audit covering the 2010 and nine months ended September 30, 2011 tax years, non-deductible acquisition costs associated with the Norcraft acquisition, and restructuring charges for which the Company could not recognize a tax benefit. In addition, the effective income tax rates in 2016 and 2015 were favorably impacted by the tax benefit attributable to the Domestic Production Activity (Internal Revenue Code Section 199) Deduction, favorable tax rates in foreign jurisdictions, and a benefit associated with the U.S. research and development credit, offset by state and local taxes and increases to uncertain tax positions.

The effective income tax rates for the three months ended September 30, 2016 and 2015 were 28.6% and 32.8%, respectively. In 2016, the effective income tax rate was favorably impacted by a tax benefit related to the adoption of ASU 2016-09, the new accounting guidance relating to share-based compensation. In addition, the effective income tax rates in 2016 and 2015 were favorably impacted by the tax benefit attributable to the Domestic Production Activity (Internal Revenue Code Section 199) Deduction, favorable tax rates in foreign jurisdictions, and a benefit associated with the U.S. research and development credit, offset by state and local taxes and increases to uncertain tax positions.

It is reasonably possible that, within the next 12 months, total unrecognized tax benefits may decrease in the range of \$1 million to \$5 million, primarily as a result of the conclusion of pending U.S. federal, state and foreign income tax proceedings.

13. Product Warranties

We generally record warranty expense at the time of sale. We offer our customers various warranty terms based on the type of product that is sold. Warranty expense is determined based on historic claim experience and the nature of the product category. The following table summarizes activity related to our product warranty liability for the nine months ended September 30, 2016 and 2015, respectively.

| (In millions) | Nine Months Ended September 30, | |
|---------------------------------------|---------------------------------------|---------|
| | 2016 | 2015 |
| Reserve balance at January 1, | \$ 16.0 | \$ 13.0 |
| Provision for warranties issued | 23.8 | 21.6 |
| Settlements made (in cash or in kind) | (22.8) | (20.3) |
| Acquisitions | 0.4 | 1.5 |
| Reserve balance at September 30, | \$ 17.4 | \$ 15.8 |

FORTUNE BRANDS HOME & SECURITY, INC.**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****14. Information on Business Segments**

Net sales and operating income for the nine and three months ended September 30, 2016 and 2015 by segment were as follows:

| | Nine Months Ended September 30, | | |
|--|---------------------------------|------------|----------------------------|
| (In millions) | 2016 | 2015 | % Change vs. Prior Year |
| <u>Net Sales</u> | | | |
| Cabinets | \$ 1,797.2 | \$ 1,565.3 | 14.8% |
| Plumbing | 1,108.0 | 1,056.0 | 4.9 |
| Doors | 351.3 | 324.6 | 8.2 |
| Security | 426.8 | 408.8 | 4.4 |
| Net sales | \$ 3,683.3 | \$ 3,354.7 | 9.8% |
| <u>Operating Income</u> | | | |
| Cabinets | \$ 194.0 | \$ 132.1 | 46.9% |
| Plumbing | 242.6 | 214.6 | 13.0 |
| Doors | 46.1 | 30.7 | 50.2 |
| Security | 44.7 | 43.1 | 3.7 |
| Less: Corporate expenses | (61.1) | (64.7) | 5.6 |
| Operating income | \$ 466.3 | \$ 355.8 | 31.1% |
| <u>Corporate expenses</u> | | | |
| General and administrative expense | \$ (61.3) | \$ (51.7) | |
| Defined benefit plan income | 2.1 | 4.9 | |
| Recognition of defined benefit plan actuarial losses | (1.9) | (2.8) | |
| Norcraft transaction costs ^(a) | | (15.1) | |
| Total Corporate expenses | \$ (61.1) | \$ (64.7) | 5.6% |

^(a) Represents external costs directly related to the acquisition of Norcraft and primarily includes expenditures for banking, legal, accounting and other similar services.

FORTUNE BRANDS HOME & SECURITY, INC.**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****14. Information on Business Segments (Continued)**

| (In millions) | Three Months Ended September 30, | | |
|--|----------------------------------|------------|----------------------------|
| | 2016 | 2015 | % Change vs. Prior Year |
| <u>Net Sales</u> | | | |
| Cabinets | \$ 602.1 | \$ 603.3 | (0.2)% |
| Plumbing | 391.1 | 364.4 | 7.3 |
| Doors | 129.2 | 123.8 | 4.4 |
| Security | 156.6 | 147.3 | 6.3 |
| Net sales | \$ 1,279.0 | \$ 1,238.8 | 3.2% |
| <u>Operating Income</u> | | | |
| Cabinets | \$ 74.8 | \$ 64.2 | 16.5% |
| Plumbing | 84.0 | 80.9 | 3.8 |
| Doors | 22.3 | 16.7 | 33.5 |
| Security | 22.9 | 16.6 | 38.0 |
| Less: Corporate expenses | (20.9) | (18.1) | (15.5) |
| Operating income | \$ 183.1 | \$ 160.3 | 14.2% |
| <u>Corporate expenses</u> | | | |
| General and administrative expense | \$ (20.5) | \$ (16.7) | |
| Defined benefit plan income | 0.6 | 1.6 | |
| Recognition of defined benefit plan actuarial losses | (1.0) | (2.8) | |
| Norcraft transaction costs ^(a) | | (0.2) | |
| Total Corporate expenses | \$ (20.9) | \$ (18.1) | (15.5)% |

^(a) Represents external costs directly related to the acquisition of Norcraft and primarily includes expenditures for banking, legal, accounting and other similar services.

FORTUNE BRANDS HOME & SECURITY, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**15. Restructuring and Other Charges**

Pre-tax restructuring and other charges for the nine and three months ended September 30, 2016 and 2015 are shown below.

| (In millions) | Nine Months Ended September 30, 2016 | | | |
|---------------|--------------------------------------|-----------------------|---------------------|---------------|
| | Other Charges ^(a) | | | Total Charges |
| | Restructuring Charges | Cost of Products Sold | SG&A ^(b) | |
| Cabinets | \$ 1.8 | \$ | | \$ 1.8 |
| Plumbing | 1.1 | 0.8 | | 1.9 |
| Security | 9.5 | 3.5 | | 13.0 |
| Total | \$ 12.4 | \$ 4.3 | \$ | \$ 16.7 |

| (In millions) | Nine Months Ended September 30, 2015 | | | |
|---------------|--------------------------------------|-----------------------|---------------------|---------------|
| | Other Charges ^(a) | | | Total Charges |
| | Restructuring Charges | Cost of Products Sold | SG&A ^(b) | |
| Cabinets | \$ 0.6 | \$ (0.1) | \$ | \$ 0.5 |
| Plumbing | 6.3 | 0.1 | 0.4 | 6.8 |
| Security | 4.8 | 2.7 | | 7.5 |
| Corporate | 0.9 | | | 0.9 |
| Total | \$ 12.6 | \$ 2.7 | \$ 0.4 | \$ 15.7 |

^(a) *Other Charges* represent charges directly related to restructuring initiatives that cannot be reported as restructuring under GAAP. Such costs may include losses on disposal of inventories, trade receivables allowances from exiting product lines, accelerated depreciation resulting from the closure of facilities and gains or losses on the sale of previously closed facilities.

^(b) *Selling, general and administrative.*

Restructuring and other charges in the first nine months of 2016 primarily related to severance costs and charges associated with the relocation of a manufacturing facility within our Security segment.

Restructuring and other charges in the first nine months of 2015 related to severance costs to relocate a plumbing facility in China and severance costs and accelerated depreciation to relocate a manufacturing facility within our Security segment, as well as severance costs in the Security segment and Corporate.

FORTUNE BRANDS HOME & SECURITY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

15. Restructuring and Other Charges (Continued)

| | | | | |
|---------------|---------------------------------------|----------|---------------------|---------|
| (In millions) | Three Months Ended September 30, 2016 | | | |
| | Other Charges ^(a) | | | |
| | Cost of | | | |
| | Restructuring | Products | SG&A ^(b) | Total |
| | Charges | Sold | | Charges |
| Plumbing | \$ 0.4 | \$ 0.6 | \$ (0.1) | \$ 0.9 |
| Security | 2.7 | 1.0 | | 3.7 |
| Total | \$ 3.1 | \$ 1.6 | \$ (0.1) | \$ 4.6 |

| | | | | |
|---------------|---------------------------------------|----------|---------------------|----------|
| (In millions) | Three Months Ended September 30, 2015 | | | |
| | Other Charges ^(a) | | | |
| | Cost of | | | |
| | Restructuring | Products | SG&A ^(b) | Total |
| | Charges | Sold | | Charges |
| Cabinets | \$ (0.4) | \$ (0.1) | \$ | \$ (0.5) |
| Plumbing | 0.6 | | | 0.6 |
| Security | 1.6 | 2.7 | | 4.3 |
| Total | \$ 1.8 | \$ 2.6 | \$ | \$ 4.4 |

^(a) *Other Charges* represent charges directly related to restructuring initiatives that cannot be reported as restructuring under GAAP. Such costs may include losses on disposal of inventories, trade receivables allowances from exiting product lines, accelerated depreciation resulting from the closure of facilities and gains or losses on the sale of previously closed facilities.

^(b) *Selling, general and administrative.*

Restructuring and other charges in the third quarter of 2016 primarily related to the relocation of a manufacturing facility within our Security segment. Restructuring and other charges in the third quarter of 2015 primarily resulted from severance charges and accelerated depreciation to relocate a manufacturing facility within our Security segment.

Reconciliation of Restructuring Liability

| | | | | | |
|---------------------------|------------|-----------|-----------------------------|---------------------------|------------|
| (In millions) | Balance at | 2016 | Cash | Non-Cash | Balance at |
| | 12/31/15 | Provision | Expenditures ^(a) | Write-offs ^(b) | 9/30/16 |
| Workforce reduction costs | \$ 10.4 | \$ 8.7 | \$ (15.0) | \$ 0.2 | \$ 4.3 |
| Other | 0.5 | 3.7 | (3.0) | (0.6) | 0.6 |

| | | | | | | | | | |
|----|------|----|------|----|--------|----|-------|----|-----|
| \$ | 10.9 | \$ | 12.4 | \$ | (18.0) | \$ | (0.4) | \$ | 4.9 |
|----|------|----|------|----|--------|----|-------|----|-----|

- (a) *Cash expenditures primarily related to severance charges.*
- (b) *Non-cash write-offs primarily include long-lived asset impairment charges attributable to restructuring actions.*

FORTUNE BRANDS HOME & SECURITY, INC.**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****16. Earnings Per Share**

The computations of earnings per common share were as follows:

| (In millions, except per share data) | Nine Months Ended September 30, | | Three Months Ended September 30, | |
|--|------------------------------------|----------|-------------------------------------|----------|
| | 2016 | 2015 | 2016 | 2015 |
| Income from continuing operations, net of tax | \$ 308.0 | \$ 218.9 | \$ 121.9 | \$ 100.0 |
| Less: Noncontrolling interest | (0.1) | 0.3 | | 0.3 |
| Income from continuing operations for EPS | 308.1 | 218.6 | 121.9 | 99.7 |
| Income from discontinued operations | 1.5 | 8.6 | 1.5 | 7.8 |
| Net income attributable to Fortune Brands | \$ 309.6 | \$ 227.2 | \$ 123.4 | \$ 107.5 |
| Earnings per common share | | | | |
| Basic | | | | |
| Continuing operations | \$ 2.00 | \$ 1.37 | \$ 0.79 | \$ 0.62 |
| Discontinued operations | 0.01 | 0.06 | 0.01 | 0.05 |
| Net income attributable to Fortune Brands common stockholders | | | | |
| | \$ 2.01 | \$ 1.43 | \$ 0.80 | \$ 0.67 |
| Diluted | | | | |
| Continuing operations | \$ 1.95 | \$ 1.34 | \$ 0.77 | \$ 0.61 |
| Discontinued operations | 0.01 | 0.05 | 0.01 | 0.05 |
| Net income attributable to Fortune Brands common stockholders | | | | |
| | \$ 1.96 | \$ 1.39 | \$ 0.78 | \$ 0.66 |
| Basic average shares outstanding | 154.4 | 159.5 | 154.2 | 160.0 |
| Stock-based awards | 3.6 | 3.5 | 3.4 | 3.4 |
| Diluted average shares outstanding | 158.1 | 163.0 | 157.6 | 163.4 |
| Antidilutive stock-based awards excluded from weighted-average number of shares outstanding for diluted earnings per share | 0.5 | 0.8 | | 0.7 |

FORTUNE BRANDS HOME & SECURITY, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Concluded)

17. Contingencies

Litigation

We are defendants in lawsuits associated with the normal conduct of our businesses and operations. It is not possible to predict the outcome of the pending actions, and, as with any litigation, it is possible that these actions could be decided unfavorably to the Company. The Company believes that there are meritorious defenses to these actions and that these actions will not have a material adverse effect upon our results of operations, cash flows or financial condition, and where appropriate, these actions are being vigorously contested.

Environmental

Compliance with federal, state and local laws regulating the discharge of materials into the environment, or otherwise relating to the protection of the environment, did not have a material effect on capital expenditures, earnings or the competitive position of Fortune Brands during the nine months ended September 30, 2016 and 2015. We are involved in remediation activities to clean up hazardous wastes as required by federal and state laws. Liabilities for remediation costs of each site are based on our best estimate of undiscounted future costs, excluding possible insurance recoveries or recoveries from other third parties. We believe compliance with current environmental protection laws (before taking into account estimated recoveries from third parties) will not have a material adverse effect upon our results of operations, cash flows or financial condition. Uncertainties about the status of laws, regulations, technology and information related to individual sites make it difficult to develop estimates of environmental remediation exposures.

Item 2.

FORTUNE BRANDS HOME & SECURITY, INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our unaudited condensed consolidated financial statements and the notes thereto, which are included in this report, as well as our audited consolidated financial statements for the year ended December 31, 2015, which are included in our Annual Report on Form 10-K for the year ended December 31, 2015.

This discussion contains forward-looking statements that are made pursuant to the safe harbor provisions of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Act of 1934, as amended (the Exchange Act), regarding business strategies, market potential, future financial performance, pension contributions, impact of acquisitions and other matters. Statements preceded by, followed by or that otherwise include the words believes, expects, anticipates, intends, projects, estimates, plans and similar expressions or future conditional verbs such as will, should, would, may and could are generally forward-looking in nature and not historical facts. Where, in any forward-looking statement, we express an expectation or belief as to future results or events, such expectation or belief based on current expectations, estimates, assumptions and projections about our industry, business and future financial results, based on information available at the time this report is filed with the Securities and Exchange Commission, or with respect to any document incorporated by reference, available as of the time such document was prepared. Our actual results could differ materially from the results contemplated by these forward-looking statements due to a number of factors, including but not limited to: (i) our reliance on the North American home improvement, repair and new home construction activity levels, (ii) the North American and global economies, (iii) risk associated with entering into potential strategic acquisitions and integrating acquired property, (iv) our ability to remain competitive, innovative and protect our intellectual property, (v) our reliance on key customers and suppliers, (vi) the cost and availability associated with our supply chains and the availability of raw materials, (vii) risk of increases in our defined benefit-related costs and funding requirements, (viii) compliance with tax, environmental and federal, state and international laws and industry regulatory standards and (ix) the risk of doing business internationally. These and other factors are discussed in Part I, Item 1A Risk Factors of our Annual Report on Form 10-K for the year ended December 31, 2015. We undertake no obligation to, and expressly disclaim any such obligation to, update or clarify any forward-looking statements to reflect changed assumptions, the occurrence of anticipated or unanticipated events, new information or changes to future results over time or otherwise, except as required by law.

OVERVIEW

References to Fortune Brands, the Company, we, our and us refer to Fortune Brands Home & Security, Inc. and consolidated subsidiaries as a whole, unless the context otherwise requires. The Company is a leader in home and security products focused on the design, manufacture and sale of market-leading branded products in the following categories: kitchen and bath cabinetry, plumbing and accessories, entry door systems and security products.

OVERVIEW (Continued)

We believe the Company has certain competitive advantages including market-leading brands, a diversified mix of channels, and lean and flexible supply chains, as well as a tradition of strong innovation and customer service. We are focused on outperforming our markets in growth, profitability and returns in order to drive increased shareholder value. We believe the Company's track record reflects the long-term attractiveness and potential of our categories and our leading brands. As consumer demand and the housing market grow, we expect the benefits of operating leverage and strategic spending will help us continue to achieve profitable organic growth.

We believe our most attractive opportunities are to invest in profitable organic growth initiatives. We also believe that as the market recovers, we have the potential to generate additional growth from leveraging our cash flow and balance sheet strength by pursuing accretive strategic acquisitions and joint ventures, and returning cash to shareholders through a combination of dividends and common stock repurchases under our share repurchase programs as explained in further detail under "Liquidity and Capital Resources" below.

The U.S. market for our home products consists of spending on both new home construction and repair and remodel activities within existing homes, with the substantial majority of the markets we serve consisting of repair and remodel spending. We believe that the U.S. market for our home products is in the midst of a multi-year recovery from the U.S. economic recession that ended in mid-2009 and that a continued recovery will largely depend on consumer confidence, employment, home prices, stable mortgage rates and credit availability. Over the long term, we believe that the U.S. home products market will benefit from favorable population and immigration trends, which will drive demand for new housing units, and from aging existing housing stock that will continue to need to be repaired and remodeled.

We may be impacted by fluctuations in raw material and transportation costs, changes in foreign exchange, and promotional activity among our competitors. We strive to offset the potential unfavorable impact of these items with productivity initiatives and price increases.

During the third quarter of 2016, we announced the creation of the Global Plumbing Group (GPG), which was designed to support the growth of multiple plumbing brands, with an enhanced set of products and brands while leveraging Moen's existing global supply chain and broad distribution network.

In September 2016, we acquired ROHL, a California-based luxury plumbing company. In a related transaction, we also acquired TCL Manufacturing Ltd, which gave us 100% ownership of Perrin & Rowe, a UK manufacturer and designer of luxury kitchen and bathroom plumbing products. The total combined purchase price was approximately \$166 million, subject to certain post-closing adjustments. We financed both acquisitions using cash on hand and borrowings under our existing credit facilities. These transactions broadened the plumbing portfolio and enhanced future growth opportunities.

In May 2016, we acquired Riobel, a Canadian plumbing company specializing in premium showroom bath and shower fittings, for a total purchase price of \$88.4 million in cash, subject to certain post-closing adjustments. We financed the transaction using cash on hand and borrowings under our existing credit facilities.

OVERVIEW (Continued)

In June 2016, we amended and restated our credit agreement to combine and rollover the existing revolving credit facility and term loan into a new standalone \$1.25 billion revolving credit facility. Terms and conditions of the credit agreement, including the total commitment amount, essentially remained the same. The revolving credit facility matures in June 2021 and borrowings thereunder will be used for general corporate purposes.

In September 2015, we completed the sale of Waterloo Industries, Inc. (Waterloo) for approximately \$14 million in cash, subject to certain post-closing adjustments.

In June 2015, we issued \$900 million of unsecured senior notes (Senior Notes) in a registered public offering. We used the proceeds from the Senior Notes offering to pay down our revolving credit facility and for general purposes.

In May 2015, we acquired Norcraft Companies, Inc. (Norcraft), a leading publicly-owned manufacturer of kitchen and bathroom cabinetry, for a total purchase price of \$648.6 million. We financed the transaction using cash on hand and borrowings under our existing credit facilities. This acquisition is expected to strengthen our overall product offering, round out our regional market penetration and enhance our frameless cabinetry capabilities.

In March 2015, we acquired a Cabinets component company for approximately \$6 million in cash. This acquisition did not have a material impact on our financial statements.

RESULTS OF OPERATIONS**Nine Months Ended September 30, 2016 Compared To Nine Months Ended September 30, 2015**

| (In millions) | Net Sales | | |
|---------------|------------|------------|----------------------------|
| | 2016 | 2015 | % Change vs. Prior Year |
| Cabinets | \$ 1,797.2 | \$ 1,565.3 | 14.8% |
| Plumbing | 1,108.0 | 1,056.0 | 4.9 |
| Doors | 351.3 | 324.6 | 8.2 |
| Security | 426.8 | 408.8 | 4.4 |
| Net sales | \$ 3,683.3 | \$ 3,354.7 | 9.8% |

| | Operating Income | | |
|--------------------------|------------------|----------|----------------------------|
| | 2016 | 2015 | % Change vs. Prior Year |
| Cabinets | \$ 194.0 | \$ 132.1 | 46.9% |
| Plumbing | 242.6 | 214.6 | 13.0 |
| Doors | 46.1 | 30.7 | 50.2 |
| Security | 44.7 | 43.1 | 3.7 |
| Less: Corporate expenses | (61.1) | (64.7) | 5.6 |
| Operating income | \$ 466.3 | \$ 355.8 | 31.1% |

The following discussion of consolidated results of operations and segment results refers to the nine months ended September 30, 2016 compared to the nine months ended September 30, 2015. Consolidated results of operations should be read in conjunction with segment results of operations.

Net sales

Net sales increased \$328.6 million, or 10%. The increase was due to the benefits of the acquisitions in our Cabinets and Plumbing segments, higher sales volume primarily from the continuing improvement in U.S. market conditions for home products, price increases to help mitigate cumulative raw material cost increases and favorable mix. These benefits were partially offset by unfavorable foreign exchange of approximately \$23 million.

Cost of products sold

Cost of products sold increased \$159.9 million, or 7%, due to higher net sales including the impact of the acquisitions in our Cabinets and Plumbing segments, partially offset by the benefit of productivity improvements.

Selling, general and administrative expenses

Selling, general and administrative expenses increased \$53.3 million, or 7%, primarily due to the impact of the acquisitions in our Cabinets and Plumbing segments and higher employee-related costs, partially offset by the absence of Norcraft transaction costs in 2016 (\$15.1 million in 2015).

RESULTS OF OPERATIONS (Continued)

Amortization of intangible assets

Amortization of intangible assets increased \$5.1 million due to the recognition of certain intangible assets from the acquisition of Norcraft and acquisitions in the Plumbing segment.

Restructuring charges

Restructuring charges of \$12.4 million in the nine months ended September 30, 2016 primarily related to severance costs and charges associated with the relocation of a manufacturing facility within our Security segment. Restructuring charges in the nine months ended September 30, 2015 were \$12.6 million.

Operating income

Operating income increased \$110.5 million, or 31% primarily due to higher net sales, productivity improvements and favorable mix. These benefits were partially offset by higher employee-related costs, higher sales rebates and advertising costs. Operating income in 2015 was also impacted by \$15.1 million of Norcraft transaction costs, which did not recur in 2016.

Interest expense

Interest expense increased \$17.0 million to \$37.5 million due to higher average borrowings and higher average interest rates.

Other (income) expense, net

Other (income) expense, net, was income of \$0.1 million in the nine months ended September 30, 2016, compared to expense of \$3.7 million in the nine months ended September 30, 2015. The change was due to favorable foreign currency adjustments.

Income taxes

The effective income tax rates for the nine months ended September 30, 2016 and 2015 were 28.2% and 34.0%, respectively. In 2016, the effective income tax rate was favorably impacted by a tax benefit related to the adoption of ASU 2016-09, the new accounting guidance relating to share-based compensation. The effective income tax rate for 2015 was unfavorably impacted by the tax cost related to the final settlement of a federal income tax audit covering the 2010 and nine months ended September 30, 2011 tax years, non-deductible acquisition costs associated with the Norcraft acquisition, and restructuring charges for which the Company could not recognize a tax benefit. In addition, the effective income tax rates in 2016 and 2015 were favorably impacted by the tax benefit attributable to the Domestic Production Activity (Internal Revenue Code Section 199) Deduction, favorable tax rates in foreign jurisdictions, and a benefit associated with the U.S. research and development credit, offset by state and local taxes and increases to uncertain tax positions.

RESULTS OF OPERATIONS (Continued)

Net income from continuing operations

Net income from continuing operations was \$308.0 million in the nine months ended September 30, 2016 compared to \$218.9 million in the nine months ended September 30, 2015. The increase of \$89.1 million was due to higher operating income partially offset by higher interest expense and higher income taxes.

Income from discontinued operations

Income from discontinued operations was \$1.5 million and \$8.6 million in the nine months ended September 30, 2016 and 2015, respectively. The discontinued operations for the nine months ended September 30, 2016 includes the effect of tax adjustments relating to the Waterloo business. The discontinued operations for the nine months ended September 30, 2015 consist of the results of operations of Waterloo and the gain associated with the sale of the business.

Results By Segment

Cabinets

Net sales increased \$231.9 million, or 15%, due to the benefit of the Norcraft acquisition, the benefit of price increases to help mitigate cumulative raw material cost increases, favorable mix and higher sales volume including the impact of new product introductions. These benefits were partially offset by approximately \$6 million of unfavorable foreign exchange.

Operating income increased \$61.9 million, or 47%, due to higher net sales, productivity improvements and favorable mix. These benefits were partially offset by higher employee-related costs.

Plumbing

Net sales increased \$52 million, or 5%, due to higher sales volume in the U.S. driven by improving U.S. market conditions and new product introductions, price increases to help mitigate cumulative raw material cost increases and the benefits of the acquisitions of Riobel, ROHL and TCL Manufacturing Ltd. These benefits were partially offset by unfavorable mix, unfavorable foreign exchange of approximately \$14 million and higher sales rebates.

Operating income increased \$28.0 million, or 13%, due to higher net sales as well as the benefits of productivity improvements. These benefits were partially offset by higher employee-related costs and unfavorable foreign exchange of approximately \$7 million. Operating income in 2016 was also favorably impacted by lower restructuring and other charges (\$4.9 million impact). These charges primarily related to severance costs to relocate a facility in China.

RESULTS OF OPERATIONS (Continued)

Results By Segment (Continued)

Doors

Net sales increased \$26.7 million, or 8%, due to higher sales volume driven primarily by improved conditions in the U.S. home products market, favorable mix and price increases to help mitigate cumulative raw material cost increases.

Operating income increased \$15.4 million, or 50%, due to higher net sales, the benefits of productivity improvements and approximately \$2 million of favorable foreign exchange. These benefits were partially offset by higher employee-related costs.

Security

Net sales increased \$18.0 million, or 4%, due to higher sales volume in the U.S. and Europe and price increases to help mitigate cumulative raw material cost increases. These benefits were partially offset by the impact of exiting certain product lines and unfavorable foreign exchange of approximately \$2 million.

Operating income increased \$1.6 million, or 4% due to higher net sales as well as the benefits of productivity improvements. These benefits were partially offset by \$5.5 million of higher restructuring and other charges primarily associated with the relocation of a manufacturing facility, and unfavorable foreign exchange of approximately \$2 million.

RESULTS OF OPERATIONS (Continued)**Results By Segment (Continued)****Corporate**

Corporate expenses decreased \$3.6 million predominantly due to the absence in 2016 of \$15.1 million of transaction costs associated with the Norcraft acquisition, partially offset by higher employee-related costs and lower defined benefit plan income.

| (In millions) | Nine Months Ended September 30, | |
|--|------------------------------------|------------------|
| | 2016 | 2015 |
| General and administrative expense | \$ (61.3) | \$ (51.7) |
| Defined benefit plan income | 2.1 | 4.9 |
| Defined benefit plan recognition of actuarial losses | (1.9) | (2.8) |
| Norcraft transaction costs ^(a) | | (15.1) |
| Total Corporate expenses | \$ (61.1) | \$ (64.7) |

^(a) Represents external costs directly related to the acquisition of Norcraft and primarily includes expenditures for banking, legal, accounting and other similar services.

In future periods the Company may record, in the Corporate segment, material expense or income associated with actuarial gains and losses arising from periodic remeasurement of our liabilities for defined benefit plans. At a minimum the Company will remeasure its defined benefit plan liabilities in the fourth quarter of each year. Remeasurements due to plan amendments and settlements may also occur in interim periods during the year. Remeasurement of these liabilities attributable to updating our liability discount rates and expected return on assets may, in particular, result in material income or expense recognition.

Based on current relevant interest rate benchmarks and year-to-date pension asset returns, the Company may incur additional defined benefit plan actuarial losses in the range of \$0.15 to \$0.25 per share in the fourth quarter of 2016 due to declining discount rates since December 31, 2015, the last remeasurement date. Any actuarial loss incurred in the fourth quarter will be based upon spot discount rates as of December 31, 2016 and our full year 2016 pension asset returns and may differ materially from this estimate. A 25 basis point change in our discount rate impacts our defined benefit plan liabilities by approximately \$25 million.

RESULTS OF OPERATIONS (Continued)**Three Months Ended September 30, 2016 Compared To Three Months Ended September 30, 2015**

| (In millions) | Net Sales | | |
|---------------|------------|------------|----------------------------|
| | 2016 | 2015 | % Change vs. Prior Year |
| Cabinets | \$ 602.1 | \$ 603.3 | (0.2)% |
| Plumbing | 391.1 | 364.4 | 7.3 |
| Doors | 129.2 | 123.8 | 4.4 |
| Security | 156.6 | 147.3 | 6.3 |
| Net sales | \$ 1,279.0 | \$ 1,238.8 | 3.2% |

| | Operating Income | | |
|--------------------------|------------------|---------|-------------------------------|
| | 2016 | 2015 | % Change vs. Prior Year |
| Cabinets | \$ 74.8 | \$ 64.2 | 16.5% |
| Plumbing | 84.0 | 80.9 | 3.8 |
| Doors | 22.3 | 16.7 | 33.5 |
| Security | 22.9 | 16.6 | 38.0 |
| Less: Corporate expenses | (20.9) | (18.1) | (15.5) |

| | | | |
|------------------|----------|----------|------|
| Operating income | \$ 183.1 | \$ 160.3 | 14.2 |
|------------------|----------|----------|------|

The following discussion of consolidated results of operations and segment results refers to the three months ended September 30, 2016 compared to the three months ended September 30, 2015. Consolidated results of operations should be read in conjunction with segment results of operations.

Net sales

Net sales increased \$40.2 million, or 3%. The increase was due to the price increases to help mitigate cumulative raw material cost increases, higher sales volume primarily from the continuing improvement in U.S. market conditions for home products and the benefits of the acquisitions in our Plumbing segment. These benefits were partially offset by unfavorable impact of foreign exchange (approximately \$5 million).

Cost of products sold

Cost of products sold decreased \$3.3 million. The impact of higher net sales was more than offset by lower commodity costs, productivity improvements and favorable mix.

Selling, general and administrative expenses

Selling, general and administrative expenses increased \$18.8 million, or 7%, due to higher employee-related costs and higher advertising costs.

RESULTS OF OPERATIONS (Continued)

Amortization of intangible assets

Amortization of intangible assets increased \$0.6 million due to the acquisitions in the Plumbing segment.

Restructuring charges

Restructuring charges of \$3.1 million in the three months ended September 30, 2016 primarily related to the relocation of a manufacturing facility within our Security segment. Restructuring charges in the three months ended September 30, 2015 were \$1.8 million.

Operating income

Operating income increased \$22.8 million, or 14% primarily due to higher net sales and productivity improvements. These benefits were partially offset by higher employee-related costs and higher advertising costs.

Interest expense

Interest expense increased \$0.7 million to \$11.8 million due to higher average borrowings partially offset by lower average interest rates.

Other (income) expense, net

Other (income) expense, net was \$0.6 million expense in the three months ended September 30, 2016 compared to expense of \$0.5 million in the three months ended September 30, 2015.

Income taxes

The effective income tax rates for the three months ended September 30, 2016 and 2015 were 28.6% and 32.8%, respectively. In 2016, the effective income tax rate was favorably impacted by a tax benefit related to the adoption of ASU 2016-09, the new accounting guidance relating to share-based compensation. In addition, the effective income tax rates in 2016 and 2015 were favorably impacted by the tax benefit attributable to the Domestic Production Activity (Internal Revenue Code Section 199) Deduction, favorable tax rates in foreign jurisdictions, and a benefit associated with the U.S. research and development credit, offset by state and local taxes and increases to uncertain tax positions.

Net income from continuing operations

Net income from continuing operations was \$121.9 million in the three months ended September 30, 2016 compared to \$100.0 million in the three months ended September 30, 2015. The increase of \$21.9 million was due to a higher operating income, partially offset by higher interest expense.

RESULTS OF OPERATIONS (Continued)

Income from discontinued operations

Income from discontinued operations was \$1.5 million and \$7.8 million in the three months ended September 30, 2016 and 2015, respectively. The discontinued operations for the three months ended September 30, 2016 includes the effect of tax adjustments relating to the Waterloo business. The discontinued operations for the three months ended September 30, 2015 consisted of the results of operations of Waterloo and the gain associated with the sale of the business.

Results By Segment

Cabinets

Net sales were essentially flat due to the benefit of price increases to help mitigate cumulative raw material cost increases and favorable mix which were offset by a load-in of new products into our retail distribution channel in 2015 that did not repeat in 2016.

Operating income increased \$10.6 million, or 17%, due to the benefit of price increases to help mitigate cumulative raw material cost increases and productivity improvements. These benefits were partially offset by costs associated with investments to support manufacturing capacity increases for long-term growth.

Plumbing

Net sales increased \$26.7 million, or 7%, due to higher sales volume in the U.S. driven by improving market conditions and new product introductions, the benefits of the acquisitions of Riobel, ROHL and TCL Manufacturing Ltd and price increases to help mitigate cumulative raw material cost increases, and higher international sales. These benefits were partially offset by higher sales rebates and foreign exchange of approximately \$4 million.

Operating income increased \$3.1 million, or 4%, due to higher net sales and productivity improvements. These benefits were partially offset by higher advertising costs of \$6 million and unfavorable foreign exchange of approximately \$2 million.

Doors

Net sales increased \$5.4 million, or 4%, due to higher sales volume driven primarily by improved conditions in the U.S. home products market and price increases to help mitigate cumulative raw material cost increases.

Operating income increased \$5.6 million, or 34%, due to higher net sales as well as the benefits of productivity improvements.

RESULTS OF OPERATIONS (Concluded)**Results By Segment (Concluded)****Security**

Net sales increased \$9.3 million, or 6%, due to higher sales volume in the U.S. and Europe and price increases to help mitigate cumulative raw material cost increases.

Operating income increased \$6.3 million, or 38%, due to higher net sales and as well as the benefits of productivity improvements. These benefits were partially offset by the costs related to the relocation of a manufacturing facility.

Corporate

Corporate expenses increased \$2.8 million predominantly as a result of higher employee related costs partially offset by lower actuarial losses related to changes in defined benefit plan demographic data and lower defined benefit plan income.

| (In millions) | Three Months Ended | |
|--|--------------------|------------------|
| | September 30, | |
| | 2016 | 2015 |
| General and administrative expense | \$ (20.5) | \$ (16.7) |
| Defined benefit plan income | 0.6 | 1.6 |
| Defined benefit plan recognition of actuarial losses | (1.0) | (2.8) |
| Norcraft transaction costs ^(a) | | (0.2) |
| Total Corporate expenses | \$ (20.9) | \$ (18.1) |

^(a) Represents external costs directly related to the acquisition of Norcraft and primarily includes expenditures for banking, legal, accounting and other similar services.

LIQUIDITY AND CAPITAL RESOURCES

Our primary liquidity needs are to support working capital requirements, fund capital expenditures and service indebtedness, as well as to finance acquisitions, repurchase shares of our common stock and pay dividends to stockholders, as deemed appropriate. Our principal sources of liquidity have been cash on hand, cash flows from operating activities, availability under our credit facilities and debt issuances in capital markets. Our operating income is generated by our subsidiaries. There are no legal restrictions on the ability of our subsidiaries to pay dividends or make other distributions to Fortune Brands. In December 2015, our Board of Directors increased the quarterly cash dividend by 14% to \$0.16 per share of our outstanding common stock. Our Board of Directors will continue to evaluate dividend payment opportunities on a quarterly basis. There can be no assurance as to when and if future dividends will be paid, and at what level, because the payment of dividends is dependent on our financial condition, results of operations, cash flows, capital requirements and other factors deemed relevant by our Board of Directors.

In June 2016, the Company amended and restated its credit agreement to combine and rollover the existing revolving credit facility and term loan into a new standalone \$1.25 billion revolving credit facility. This amendment of the credit agreement was a non-cash transaction for the Company. Terms and conditions of the credit agreement, including the total commitment amount, essentially remained the same. The revolving credit facility matures in June 2021 and borrowings thereunder will be used for general corporate purposes. On September 30, 2016 and December 31, 2015, our outstanding borrowings under these facilities, net of debt issuance costs relating to the term loan balance, were \$695.0 million and \$279.0 million, respectively. At September 30, 2016 and December 31, 2015, the current portion of long-term debt was zero. Interest rates under the facility are variable based on LIBOR at the time of the borrowing and the Company's long-term credit rating and can range from LIBOR + 0.9% to LIBOR + 1.5%. As of September 30, 2016, we were in compliance with all covenants under this facility. As a result of the refinancing, we wrote-off prepaid debt issuance costs of approximately \$1.3 million as of June 30, 2016. We retrospectively adopted ASU 2015-03, Simplifying the Presentation of Debt Issuance Costs, on January 1, 2016, resulting in the reclassification of approximately \$3 million of debt issuance costs from other current assets and other assets to long-term debt as of December 31, 2015. Adoption of this guidance did not impact the Company's equity, results of operations or cash flows.

In the first nine months of 2016, we repurchased 7.6 million shares of our outstanding common stock under the Company's share repurchase program for \$362.7 million. As of September 30, 2016, the Company's total remaining share repurchase authorization under the Company's repurchase program was approximately \$285 million. The share repurchase program does not obligate the Company to repurchase any specific dollar amount or number of shares and may be suspended or discontinued at any time.

Acquisitions and divestitures in 2016 and 2015 included:

In September 2016, we acquired ROHL, a California-based luxury plumbing company. In a related transaction, we also acquired TCL Manufacturing Ltd, which gave us 100% ownership of Perrin & Rowe, a UK manufacturer and designer of luxury kitchen and bathroom plumbing products. The total combined purchase price was approximately \$166 million, subject to certain post-closing adjustments. We financed the transaction using cash on hand and borrowings under our existing credit facilities.

In May 2016, we acquired Riobel, a Canadian plumbing company for a purchase price of approximately \$88 million in cash, subject to certain post-closing adjustments. We financed the transaction using cash on hand and borrowings under our existing credit facilities.

In September 2015, we completed the sale of the Waterloo tool storage business for approximately \$14 million in cash, subject to certain post-closing adjustments.

In May 2015, we acquired Norcraft, a leading manufacturer of kitchen and bathroom cabinetry, for a purchase price of \$648.6 million. We financed this transaction using cash on hand and borrowings under our existing credit facilities.

We periodically review our portfolio of brands and evaluate potential strategic transactions and other capital initiatives to increase shareholder value. However, we cannot predict whether or when we may enter into acquisitions, joint ventures or dispositions, make any purchases of shares of our common stock under our share repurchase programs, or pay dividends, or what impact any such transactions could have on our results of operations, cash flows or financial condition, whether as a result of the issuance of debt or equity securities, or otherwise. Our cash flows from operations, borrowing availability and overall liquidity are subject to certain risks and uncertainties, including those described in the section of our Annual Report on Form 10-K for the year-ended December 31, 2015 entitled Item 1A. Risk Factors.

In June 2015, we issued \$900 million of Senior Notes in a registered public offering. The Senior Notes consist of two tranches: \$400 million of five-year notes due 2020 with a coupon of 3% and \$500 million of ten-year notes due 2025 with a coupon of 4%. We used the proceeds from the Senior Notes offering to pay down our revolving credit facility and for general purposes. On September 30, 2016, the outstanding amount of the Senior Notes, net of underwriting commissions and price discounts, was \$890.8 million.

On September 30, 2016, we had cash and cash equivalents of \$278.6 million, of which \$251.3 million was held at non-U.S. subsidiaries. We manage our global cash requirements considering (i) available funds among the subsidiaries through which we conduct business, (ii) the geographic location of our liquidity needs, and (iii) the cost to access international cash balances. The undistributed earnings of foreign subsidiaries are considered indefinitely reinvested. If these funds were needed for our operations in the U.S., the repatriation of non-U.S. cash balances from certain subsidiaries could have adverse tax consequences as we may be required to pay and record income tax expense on those funds to the extent they were previously considered indefinitely reinvested.

Our operating cash flows are significantly impacted by the seasonality of our business. We typically generate most our operating cash flow in the third and fourth quarters of each year. We use operating cash in the first half of the year, particularly in the first quarter.

Cash Flows

Below is a summary of cash flows for the nine months ended September 30, 2016 and 2015.

| (In millions) | Nine Months Ended September 30, | |
|---|---------------------------------|----------|
| | 2016 | 2015 |
| Net cash provided by operating activities | \$ 380.6 | \$ 277.8 |
| Net cash used in investing activities | (334.3) | (725.0) |
| Net cash (used in) provided by financing activities | (9.5) | 616.8 |
| Effect of foreign exchange rate changes on cash | 3.3 | (10.9) |
| Net increase in cash and cash equivalents | \$ 40.1 | \$ 158.7 |

Net cash provided by operating activities was \$380.6 million in the nine months ended September 30, 2016 compared to \$277.8 million in the nine months ended September 30, 2015. The increase in cash provided of \$102.8 million was primarily due to higher net income and a lower build in working capital in 2016 compared to 2015. These benefits were partially offset by higher incentive compensation and customer program payments in the first quarter of 2016 compared to 2015.

Net cash used in investing activities was \$334.3 million in the nine months ended September 30, 2016 compared to \$725.0 million in the nine months ended September 30, 2015. The decrease of \$390.7 million was primarily due to the decrease in cost of acquisitions of \$422.3 million, partially offset by \$19 million of higher capital spending.

Net cash used in financing activities was \$9.5 million in the nine months ended September 30, 2016 compared to net cash provided by financing activities of \$616.8 million in the nine months ended September 30, 2015. The decrease in cash provided of \$626.3 million was primarily due to higher share repurchases in 2016 compared to 2015 (\$347.0 million) and lower net borrowings of \$254.9 million.

The cash flows related to discontinued operations are combined with cash flows from continuing operations within each category on the statements of cash flows.

Pension Plans

In 2016, we expect to make pension contributions of approximately \$1 million. For the foreseeable future, we believe that we have sufficient liquidity to meet the minimum funding that may be required by the Pension Protection Act of 2006.

Foreign Exchange

We have investments in various foreign countries, principally Canada, Mexico, China and France. Therefore, changes in the value of the related currencies affect our financial statements when translated into U.S. dollars.

RECENTLY ISSUED ACCOUNTING STANDARDS

Classification of Certain Cash Receipts and Cash Payments

In September 2016 the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-15 that will change how an entity classifies certain cash receipts and cash payments on its statement of cash flows. The key changes that may potentially impact our financial statements include the following: 1) Cash payments for debt prepayment or extinguishment costs should be classified as financing cash outflows; 2) Contingent consideration payments that are not made within three months after the consummation of a business combination would be classified as financing (if payment made is up to the acquisition date fair value of liability) or operating outflows (if in excess of acquisition fair value). Cash payments made soon after the consummation of a business combination generally will be classified as cash outflows for investing activities; 3) Insurance settlement proceeds, would be classified based on the nature of the loss; and 4) Company-owned life insurance settlement proceeds would be presented as investing cash inflows, and premiums could be classified as investing or operating cash outflows, or a combination of both. The new standard is effective beginning January 1, 2018 and should be adopted retrospectively. Early adoption is permitted. We are assessing the impact the adoption of this standard will have on our financial statements.

Financial Instruments Credit Losses

In June 2016, the FASB issued ASU 2016-13 that changes the impairment model for most financial assets and certain other instruments that are not measured at fair value through net income. The new guidance applies to most financial assets measured at amortized cost, including trade and other receivables and loans as well as off-balance-sheet credit exposures (e.g., loan commitments, standby letters of credit). The standard will replace the incurred loss approach under the current guidance with an expected loss model that requires an entity to estimate its lifetime expected credit loss . The new standard is effective beginning January 1, 2020 and early application is permitted but not earlier than January 1, 2019. We are assessing the impact the adoption of this standard will have on our financial statements.

RECENTLY ISSUED ACCOUNTING STANDARDS (Continued)

Improvements to Employee Share-Based Payment Accounting

In March 2016, the FASB issued ASU 2016-09 that requires entities to recognize the income tax effects of share-based awards in the income statement when the awards vest or are settled. The new standard also allows entities to withhold an amount up to an employee's maximum individual tax rate in the relevant jurisdiction without resulting in liability classification of the award. The new standard is effective for annual and interim periods beginning January 1, 2017. We early adopted this standard as of June 30, 2016.

We have reclassified \$9.8 million and \$13.8 million of employee withholding taxes paid from operating into financing activities in the statement of cash flows for the nine months ended September 30, 2016 and September 30, 2015, respectively, as required by ASU 2016-09 (adopted retrospectively).

Simplifying the Transition to the Equity Method of Accounting

In March 2016, the FASB issued ASU 2016-07, which eliminates the requirement to apply the equity method of accounting retrospectively when an entity obtains significant influence over a previously held investment. Previously, entities were required to retrospectively apply the equity method of accounting when obtaining significant influence over an investment (for example due to an increase in ownership). The new standard is effective beginning January 1, 2017. Earlier application is permitted, however we elected not to early adopt. We do not expect this standard to have a material effect on our financial statements.

Leases

In February 2016, the FASB issued ASU 2016-02, *Leases* that requires lessees to recognize almost all leases on their balance sheet as a right-of-use asset and lease liability but recognize related expenses in a manner similar to current accounting. The guidance also eliminates current real estate-specific provisions for all entities. The new standard is effective for annual periods beginning after December 15, 2018 (calendar year 2019 for Fortune Brands) and earlier application is permitted. We are assessing the impact the adoption of this standard will have on our financial statements.

RECENTLY ISSUED ACCOUNTING STANDARDS (Concluded)

Recognition and Measurement of Financial Assets and Financial Liabilities

In January 2016, the FASB issued final guidance ASU 2016-01 that requires entities to measure investments in unconsolidated entities (other than those accounted for using the equity method of accounting) at fair value through the income statement. There will no longer be an available-for-sale classification (with changes in fair value reported in Other Comprehensive Income). In addition, the cost method is eliminated for equity investments without readily determinable fair values. The new standard is effective beginning January 1, 2018. Earlier application is permitted for certain provisions of the standard, however we elected not to early adopt. We do not expect this standard to have a material effect on our financial statements.

Simplifying Subsequent Measurement of Inventory

In July 2015, the FASB issued a final standard that simplifies the subsequent measurement of inventory by replacing the current standard of lower of cost or market test. Under the current guidance the subsequent measurement of inventory is measured at the lower of cost or market, where market may have multiple possible outcomes. The new guidance requires subsequent measurement of inventory at the lower of cost or net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable costs to sell (completion, disposal, and transportation). This new standard is effective for the annual period beginning January 1, 2017. Earlier application is permitted, however we elected not to early adopt. We do not expect this standard to have a material effect on our financial statements.

Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern

In August 2014, the FASB issued ASU 2014-15, Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. This ASU provides guidance about management's responsibility to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and to provide related footnote disclosures. This amendment is effective for the annual period ending after December 15, 2016 (calendar year 2017 for Fortune Brands), and for annual periods and interim periods thereafter. Early application is permitted, however we elected not to early adopt. We do not expect this standard to have a material effect on our financial statements.

Revenue from Contracts with Customers

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. This ASU clarifies the accounting for revenue arising from contracts with customers and specifies the disclosures that an entity should include in its financial statements. The standard is effective for annual reporting periods beginning after December 15, 2017 (calendar year 2018 for Fortune Brands). During the first half of 2016, the FASB issued the final amendments to the standard relating to the principal versus agent guidance, accounting for licenses of intellectual property and identifying performance obligations as well as the guidance on transition, collectability, noncash consideration and the presentation of sales and other similar taxes. The effective date and transition requirements for these amendments are the same as those of the new revenue standard. We expect to complete our assessment of the impact of adoption in the second quarter of 2017 and finalize the adoption process of the new revenue standard by the end of 2017.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

There have been no material changes in the information provided in the section entitled Quantitative and Qualitative Disclosures about Market Risk in our Annual Report on Form 10-K for the year ended December 31, 2015.

Item 4. CONTROLS AND PROCEDURES.

(a) Evaluation of Disclosure Controls and Procedures.

The Company's management has evaluated, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this report.

(b) Changes in Internal Control Over Financial Reporting.

There have not been any changes in the Company's internal control over financial reporting that occurred during the Company's fiscal quarter ended September 30, 2016 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. The Company is in the process of reviewing the internal control structure of acquired businesses and, if necessary, will make appropriate changes as we incorporate our controls and procedures into those recently acquired businesses.

PART II. OTHER INFORMATION**Item 1. LEGAL PROCEEDINGS.****(a) Other Litigation.**

The Company is a defendant in lawsuits associated with the normal conduct of its businesses and operations. It is not possible to predict the outcome of the pending actions, and, as with any litigation, it is possible that these actions could be decided unfavorably to the Company. The Company believes that there are meritorious defenses to these actions and that these actions will not have a material adverse effect upon the Company's results of operations, cash flows or financial condition, and, where appropriate, these actions are being vigorously contested.

(b) Environmental Matters.

Compliance with federal, state and local laws regulating the discharge of materials into the environment, or otherwise relating to the protection of the environment, did not have a material effect on capital expenditures, earnings or the competitive position of Fortune Brands during the nine months ended September 30, 2016 and 2015. We are involved in remediation activities to clean up hazardous wastes as required by federal and state laws. Liabilities for remediation costs of each site are based on our best estimate of undiscounted future costs, excluding possible insurance recoveries or recoveries from other third parties. We believe compliance with current environmental protection laws (before taking into account estimated recoveries from third parties) will not have a material adverse effect upon our results of operations, cash flows or financial condition. Uncertainties about the status of laws, regulations, technology and information related to individual sites make it difficult to develop estimates of environmental remediation exposures.

Item 1A. RISK FACTORS.

There have been no material changes to the risk factors previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2015 in the section entitled "Risk Factors."

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

Below are the repurchases of common stock by the Company or any affiliated purchaser (as defined in Rule 10b-18(a)(3) under the Exchange Act) for the three months ended September 30, 2016:

Issuer Purchases of Equity Securities

| Three Months Ended September 30, 2016 | Total number of shares purchased (a) | Average price paid per share | Total number of shares purchased as part of publicly announced plans or programs (a) | Maximum dollar amount that may yet be purchased under the plans or |
|---------------------------------------|--------------------------------------|------------------------------|--|--|
|---------------------------------------|--------------------------------------|------------------------------|--|--|

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| | | programs ^(a) | |
|-------------|--------------|-------------------------|----------------|
| July 1 | July 31 | \$ | \$ 284,870,273 |
| August 1 | August 30 | | 284,870,273 |
| September 1 | September 30 | | 284,870,273 |
| Total | | \$ | |

(a) Information on the Company's share repurchase programs follows:

| <i>Authorization date</i> | <i>Announcement date</i> | <i>Authorization amount of shares of outstanding common stock</i> | <i>Expiration date</i> |
|---------------------------|--------------------------|---|--------------------------|
| <i>February 16, 2016</i> | <i>February 22, 2016</i> | <i>\$ 400 million</i> | <i>February 16, 2018</i> |

Item 6. **EXHIBITS**

- 3(i). Restated Certificate of Incorporation of Fortune Brands Home & Security, Inc. (incorporated herein by reference to Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q filed with the SEC on November 5, 2012, Commission file number 1-35166).
- 3(ii). Amended and Restated By-laws of Fortune Brands Home & Security, Inc., as adopted September 27, 2011 (incorporated herein by reference to Exhibit 3.2 to the Company's Current Report on Form 8-K filed with the SEC on September 30, 2011, Commission file number 1-35166).
- 10.1* Amendment Number One to the Fortune Brands Home & Security, Inc. 2013 Long-Term Incentive Plan.
- 31.1.* Certificate of Chief Executive Officer Required Under Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2.* Certificate of Chief Financial Officer Required Under Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.* Joint CEO/CFO Certificate Required Under Section 906 of the Sarbanes-Oxley Act of 2002.
- 101.* The following materials from the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2016 formatted in eXtensible Business Reporting Language (XBRL): (i) the Condensed Consolidated Statements of Comprehensive Income, (ii) the Condensed Consolidated Balance Sheets, (iii) the Condensed Consolidated Statements of Cash Flows, (iv) the Condensed Consolidated Statements of Equity, and (v) the Notes to the Condensed Consolidated Financial Statements.

* Filed herewith.

SIGNATURE

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

FORTUNE BRANDS HOME & SECURITY, INC.
(Registrant)

Date: November 2, 2016

/s/ E. Lee Wyatt, Jr.
E. Lee Wyatt, Jr.
Senior Vice President and Chief Financial Officer
(Duly authorized officer and principal financial officer
of the Registrant)

EXHIBIT INDEX

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* Filed herewith.