AVON PRODUCTS INC
Form 10-Q
August 01, 2013

UNITED STATES OF AMERICA
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended June 30, 2013
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 1-4881

AVON PRODUCTS, INC.
(Exact name of registrant as specified in its charter)

New York (State or other jurisdiction of Incorporation or organization)	13-0544597 (I.R.S. Employer Identification No.)

777 Third Avenue, New York, N.Y. 10017-1307
(Address of principal executive offices) (Zip code)

(212) 282-5000
(Telephone Number, including area code)

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 Q 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 Q No ¨

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 Q	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 Q

The number of shares of Common Stock (par value $0.25) outstanding at June 30, 2013 was 433,657,188.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

AVON PRODUCTS, INC.
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	Three Months Ended	
(In millions, except per share data)	June 30, 2013	June 30, 2012
Net sales	$2,466.8	$2,518.2
Other revenue	42.1	40.0
Total revenue	2,508.9	2,558.2
Costs, expenses and other:		
Cost of sales	935.4	949.7
Selling, general and administrative expenses	1,371.3	1,479.6
Operating profit	202.2	128.9
Interest expense	31.1	24.9
Loss on extinguishment of debt	13.0	—
Interest income	(2.8)	(2.8)
Other expense, net	15.6	13.8
Total other expenses	56.9	35.9
Income from continuing operations, before taxes	145.3	93.0
Income taxes	(60.7)	(27.9)
Income from continuing operations, net of tax	84.6	65.1
Loss from discontinued operations, net of tax	(50.4)	(2.4)
Net income	34.2	62.7
Net income attributable to noncontrolling interests	(2.3)	(1.1)
Net income attributable to Avon	$31.9	$61.6
Earnings (loss) per share:		
Basic from continuing operations	$0.19	$0.15
Basic from discontinued operations	$(0.12)	$(0.01)
Basic attributable to Avon	$0.07	$0.14
Diluted from continuing operations	$0.19	$0.15
Diluted from discontinued operations	$(0.11)	$(0.01)
Diluted attributable to Avon	$0.07	$0.14
Cash dividends per common share	$0.06	$0.23

The accompanying notes are an integral part of these statements.

AVON PRODUCTS, INC.
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	Six Months Ended	
(In millions, except per share data)	June 30, 2013	June 30, 2012
Net sales	$4,873.9	$5,019.4
Other revenue	91.0	79.2
Total revenue	4,964.9	5,098.6
Costs, expenses and other:		
Cost of sales	1,860.8	1,944.4
Selling, general and administrative expenses	2,727.9	2,952.6
Operating profit	376.2	201.6
Interest expense	60.5	49.5
Loss on extinguishment of debt	86.0	—
Interest income	(4.8)	(6.7)
Other expense, net	59.9	23.8
Total other expenses	201.6	66.6
Income from continuing operations, before taxes	174.6	135.0
Income taxes	(101.5)	(41.7)
Income from continuing operations, net of tax	73.1	93.3
Loss from discontinued operations, net of tax	(51.5)	(3.0)
Net income	21.6	90.3
Net income attributable to noncontrolling interests	(3.4)	(2.2)
Net income attributable to Avon	$18.2	$88.1
Earnings (loss) per share:		
Basic from continuing operations	$0.16	$0.21
Basic from discontinued operations	$(0.12)	$(0.01)
Basic attributable to Avon	$0.04	$0.20
Diluted from continuing operations	$0.16	$0.21
Diluted from discontinued operations	$(0.12)	$(0.01)
Diluted attributable to Avon	$0.04	$0.20
Cash dividends per common share	$0.12	$0.46

The accompanying notes are an integral part of these statements.

AVON PRODUCTS, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

	Three Months Ended	
(In millions)	June 30, 2013	June 30, 2012
Net income	$34.2	$62.7
Other comprehensive loss:		
Foreign currency translation adjustments	(107.7)	(189.7)
Change in derivative losses on cash flow hedges, net of taxes of $0.2 and $0.6	0.3	0.9
Change in derivative losses on net investment hedges	—	—
Adjustments of and amortization of net actuarial loss, prior service cost, and transition obligation, net of taxes of $7.1 and $(1.3)	19.6	0.3
Total other comprehensive loss, net of taxes	(87.8)	(188.5)
Comprehensive loss	(53.6)	(125.8)
Less: comprehensive (loss) income attributable to noncontrolling interests	(0.4)	0.6
Comprehensive loss attributable to Avon	$(53.2)	$(126.4)

The accompanying notes are an integral part of these statements.

AVON PRODUCTS, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

	Six Months Ended	
(In millions)	June 30, 2013	June 30, 2012
Net income	$21.6	$90.3
Other comprehensive loss:		
Foreign currency translation adjustments	(131.1)	(64.8)
Change in derivative losses on cash flow hedges, net of taxes of $0.6 and $1.1	1.1	1.9
Change in derivative losses on net investment hedge	—	(0.3)
Adjustments of and amortization of net actuarial loss, prior service cost, and transition obligation, net of taxes of $12.1 and $3.1	29.7	9.6
Total other comprehensive loss, net of taxes	(100.3)	(53.6)
Comprehensive (loss) income	(78.7)	36.7
Less: comprehensive income attributable to noncontrolling interests	0.5	1.2
Comprehensive (loss) income attributable to Avon	$(79.2)	$35.5

The accompanying notes are an integral part of these statements.

AVON PRODUCTS, INC.
CONSOLIDATED BALANCE SHEETS
(Unaudited)

(In millions)	June 30, 2013	December 31, 2012
Assets		
Current Assets		
Cash and cash equivalents	$873.2	$1,206.9
Accounts receivable, net	691.7	752.1
Inventories	1,154.3	1,101.1
Prepaid expenses and other	707.6	827.0
Current assets of discontinued operations	36.1	41.8
Total current assets	3,462.9	3,928.9
Property, plant and equipment, at cost	2,496.7	2,684.8
Less accumulated depreciation	(1,102.8)	(1,158.8)
Property, plant and equipment, net	1,393.9	1,526.0
Goodwill	311.3	330.3
Other intangible assets, net	36.4	40.6
Other assets	1,413.4	1,407.9
Noncurrent assets of discontinued operations	67.4	148.8
Total assets	$6,685.3	$7,382.5
Liabilities and Shareholders' Equity		
Current Liabilities		
Debt maturing within one year	$263.2	$572.0
Accounts payable	861.1	914.3
Accrued compensation	241.1	264.7
Other accrued liabilities	564.7	645.3
Sales and taxes other than income	187.7	210.6
Income taxes	46.4	73.6
Current liabilities of discontinued operations	16.1	24.1
Total current liabilities	2,180.3	2,704.6
Long-term debt	2,634.8	2,623.8
Employee benefit plans	568.3	637.6
Long-term income taxes	49.8	52.0
Other liabilities	119.0	131.1
Noncurrent liabilities of discontinued operations	0.1	0.1
Total liabilities	$5,552.3	$6,149.2
Contingencies (Note 6)		
Shareholders' Equity		
Common stock	$189.3	$188.3
Additional paid-in capital	2,159.5	2,119.6
Retained earnings	4,323.8	4,357.8
Accumulated other comprehensive loss	(977.0)	(876.7)
Treasury stock, at cost	(4,579.3)	(4,571.9)
Total Avon shareholders' equity	1,116.3	1,217.1
Noncontrolling interests	16.7	16.2
Total shareholders' equity	$1,133.0	$1,233.3
Total liabilities and shareholders' equity	$6,685.3	$7,382.5

The accompanying notes are an integral part of these statements.

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AVON PRODUCTS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Six Months Ended	
(In millions)	June 30, 2013	June 30, 2012
Cash Flows from Operating Activities		
Net income	$21.6	$90.3
Loss from discontinued operations, net of tax	51.5	3.0
Income from continuing operations	$73.1	$93.3
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	119.8	109.1
Provision for doubtful accounts	113.4	134.5
Provision for obsolescence	53.7	59.7
Share-based compensation	26.2	23.2
Deferred income taxes	(27.4)	(72.0)
Charge for Venezuelan monetary assets and liabilities	34.1	—
Other	30.1	20.9
Changes in assets and liabilities:		
Accounts receivable	(103.3)	(94.4)
Inventories	(154.3)	(170.4)
Prepaid expenses and other	67.6	45.6
Accounts payable and accrued liabilities	(65.8)	1.0
Income and other taxes	(28.6)	(70.8)
Noncurrent assets and liabilities	(68.9)	(43.0)
Net cash provided by operating activities of continuing operations	69.7	36.7
Cash Flows from Investing Activities		
Capital expenditures	(75.8)	(87.5)
Disposal of assets	12.8	9.5
Purchases of investments	(14.2)	(0.8)
Proceeds from sale of investments	0.2	—
Net cash used by investing activities of continuing operations	(77.0)	(78.8)
Cash Flows from Financing Activities*		
Cash dividends	(53.9)	(199.2)
Debt, net (maturities of three months or less)	31.6	(343.1)
Proceeds from debt	1,478.8	638.4
Repayment of debt	(1,796.2)	(71.2)
Interest rate swap termination	88.1	43.6
Proceeds from exercise of stock options	16.8	7.6
Excess tax benefit realized from share-based compensation	0.1	(2.6)
Repurchase of common stock	(7.6)	(8.1)
Net cash (used) provided by financing activities of continuing operations	(242.3)	65.4
Cash Flows from Discontinued Operations		
Net cash (used) provided by operating activities of discontinued operations	(0.5)	4.4
Net cash used by investing activities of discontinued operations	(0.2)	(0.1)
Net cash (used) provided by discontinued operations	(0.7)	4.3
Effect of exchange rate changes on cash and equivalents	(81.0)	3.7
Net (decrease) increase in cash and equivalents	(331.3)	31.3
Cash and equivalents at beginning of year[1]	$1,209.6	$1,245.1
Cash and equivalents at end of period[2]	$878.3	$1,276.4

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* Non-cash financing activities in the six months ended June 30, 2013 and 2012 included the change in fair market value of interest-rate swap agreements of $(.7) and $(1.1), respectively.

(1) Includes cash and cash equivalents of discontinued operations of $2.7 and $6.9 at the beginning of the year in 2013 and 2012, respectively.

(2) Includes cash and cash equivalents of discontinued operations of $5.1 and $8.0 at the end of the period in 2013 and 2012, respectively.

The accompanying notes are an integral part of these statements.

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AVON PRODUCTS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(U.S. dollars in millions, except per share data)

1. ACCOUNTING POLICIES

Basis of Presentation

We prepare our unaudited interim consolidated financial statements in conformity with accounting principles generally accepted in the United States ("GAAP"). We consistently applied the accounting policies described in our 2012 Annual Report on Form 10-K, as amended ("2012 Form 10-K") in preparing these unaudited financial statements. In our opinion, the unaudited interim consolidated financial statements reflect all adjustments of a normal recurring nature that are necessary for a fair statement of the results for the interim periods presented. Results for interim periods are not necessarily indicative of results for a full year. You should read these unaudited interim consolidated financial statements in conjunction with our consolidated financial statements contained in our 2012 Form 10-K. When used in this report, the terms "Avon," "Company," "we" or "us" mean Avon Products, Inc.

For interim consolidated financial statement purposes, our tax provision is determined using an estimate of our annual effective tax rate, adjusted for discrete items, if any, that are taken into account in the relevant period. We also provide for accruals under our various employee benefit plans for each quarter based on one quarter of the estimated annual expense.

Venezuela Currency

Effective February 13, 2013, the Venezuelan government devalued its currency by approximately 32% and as such we recorded a one-time, after-tax loss of $51 ($34 in other expense, net and $17 in income taxes) in the first quarter of 2013, primarily reflecting the write-down of monetary assets and liabilities and deferred tax benefits. In addition, as a result of using the U.S. historic dollar cost basis of non-monetary assets, such as inventory, acquired prior to the devaluation, operating profit and net income during the six months ending June 30, 2013 were negatively impacted.

New Accounting Standard Implemented

In February 2013, the FASB issued ASU 2013-02, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income. ASU 2013-02 requires entities to report, either on the face of the income statement or in the notes, the effect of significant reclassifications out of accumulated other comprehensive income ("AOCI") on the respective line items in net income if the amount being reclassified is required under GAAP to be reclassified in its entirety to net income. For other amounts that are not required under GAAP to be reclassified in their entirety from AOCI to net income in the same reporting period, an entity is required to cross-reference other disclosures required under GAAP that provide additional detail about those amounts. See Note 7, Accumulated Other Comprehensive Income, for the required disclosures. ASU 2013-02 is effective as of January 1, 2013 for Avon and did not have a significant impact on our financial statements, other than presentation.

2. EARNINGS PER SHARE AND SHARE REPURCHASES

We compute earnings (loss) per share ("EPS") using the two-class method, which is an earnings allocation formula that determines earnings per share for common stock and participating securities. Our participating securities are our grants of restricted stock and restricted stock units, which contain non-forfeitable rights to dividend equivalents. We compute basic EPS by dividing net income allocated to common shareholders by the weighted-average number of shares outstanding during the year. Diluted EPS is calculated to give effect to all potentially dilutive common shares that were outstanding during the period.

AVON PRODUCTS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in millions, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
(Shares in millions)	2013	2012	2013	2012
Numerator from continuing operations:				
Income from continuing operations less amounts attributable to noncontrolling interests	$82.3	$64.0	$69.7	$91.1
Less: Earnings allocated to participating securities	(.7)	(1.1)	(.6)	(1.9)
Income from continuing operations allocated to common shareholders	81.6	62.9	69.1	89.2
Numerator from discontinued operations:				
Loss from discontinued operations	$(50.4)	$(2.4)	$(51.5)	$(3.0)
Less: Loss (earnings) allocated to participating securities	.4	(.6)	.5	(1.1)
Loss allocated to common shareholders	(50.0)	(3.0)	(51.0)	(4.1)
Numerator attributable to Avon:				
Net income attributable to Avon	$31.9	$61.6	$18.2	$88.1
Less: Earnings allocated to participating securities	(.3)	(1.1)	(.2)	(1.9)
Income allocated to common shareholders	31.6	60.5	18.0	86.2
Denominator:				
Basic EPS weighted-average shares outstanding	433.5	432.0	433.0	431.6
Diluted effect of assumed conversion of stock options	1.1	.8	.9	.8
Diluted EPS adjusted weighted-average shares outstanding	434.6	432.8	433.9	432.4
Earnings per Common Share from continuing operations:				
Basic	$.19	$.15	$.16	$.21
Diluted	$.19	$.15	$.16	$.21
Loss per Common Share from discontinued operations:				
Basic	$(.12)	$(.01)	$(.12)	$(.01)
Diluted	$(.11)	$(.01)	$(.12)	$(.01)
Earnings per Common Share attributable to Avon:				
Basic	$.07	$.14	$.04	$.20
Diluted	$.07	$.14	$.04	$.20

Amounts in the table above may not necessarily sum due to rounding.

At June 30, 2013 and 2012, we did not include stock options to purchase 18.2 million shares and 22.2 million shares of Avon common stock, respectively, in the calculations of diluted EPS because the exercise prices of those options were greater than the average market price, and therefore, their inclusion would have been anti-dilutive.

We purchased approximately .4 million shares of Avon common stock for $7.6 during the first six months of 2013, as compared to approximately .4 million shares of Avon common stock for $8.1 during the first six months of 2012, primarily through acquisition of stock from employees in connection with tax payments upon vesting of restricted stock units and private transactions with a broker in connection with stock based obligations under our Deferred Compensation Plan. During the first three months of 2012, shares were also purchased under our previously announced share repurchase program, which expired in the fourth quarter of 2012.

3. DISCONTINUED OPERATIONS

On June 30, 2013, the Company entered into an agreement to sell its Silpada jewelry business (“Silpada”) for $85, plus an earn-out of up to $15 if Silpada achieves specific earnings targets over two years. Earlier this year, the Company disclosed that it was reviewing strategic alternatives for Silpada. The Company determined as part of this process to divest Silpada because of the timeline and investment required to return the business to historical levels of profitability. Silpada was previously reported within our North America segment and was classified within discontinued operations for all periods presented.

AVON PRODUCTS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in millions, except per share data)

The transaction closed on July 3, 2013. The Company expects that the proceeds from the sale will be used for general corporate purposes, including the repayment of outstanding debt. The benefit associated with the earn-out will be recorded in discontinued operations only when it becomes realizable by Avon. In the second quarter of 2013, the Company recorded a pre-tax charge of $79 ($50 net of tax), reflecting the expected loss on sale, which represents the difference between the carrying value of the Silpada business and the expected proceeds.

Summarized financial information for discontinued operations is shown below:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Total revenue	$24.7	$33.5	$52.3	$68.5
Operating loss(1)	(80.0)	(2.3)	(81.9)	(3.5)

(1) Operating loss for the three and six months ended June 30, 2013 includes a pre-tax charge of $79, reflecting the expected loss on sale.

2012 Impairment Assessment

Silpada was acquired in July 2010. Silpada had historically generated positive cash flows and was expected to continue to generate positive cash flows; however, the expected cash flows of the business as of the date of our impairment analysis were not at a level sufficient to support the carrying value of the business. Since the acquisition in 2010, the Silpada business did not achieve our revenue, earnings and cash flows expectations primarily due to lower consumer spending, higher silver prices and increased competition. When compared to our initial projections for the business at the time of the acquisition, the future expectations for Silpada utilized in the 2011 and 2012 impairment analyses represented a significant decrease in the future cash flows that were expected to be generated by Silpada. This reduction in future expectations led to material impairments of $263 and $209 being recorded during the fourth quarters of 2011 and 2012, respectively.

Throughout the first nine months of 2012, Silpada continued to perform generally in line with our revenue and earnings forecast and there were no significant changes to our long-term outlook for the business, which was utilized in determining the estimated fair value in our 2011 impairment analysis. Our revenue and earnings forecast for 2012 had projected improvements to the trends (i.e., a reduction of the year-over-year revenue declines) in the latter portion of 2012. In 2012, in an effort to promote sales and grow the business, we made changes to certain members of the Silpada management team, including bringing in personnel who had previously managed other Avon businesses. Among the initiatives implemented by the new Silpada management team was a recruiting incentive program which we had believed would benefit our Representative counts and Representative productivity primarily in the latter portion of 2012, and in turn improve the performance of the business. While we saw improvement in our Representative additions, the recruiting incentive program did not result in the expected Representative productivity. In the fourth quarter of 2012, which is generally the quarter with the largest dollar value of revenue for the Silpada business, it became apparent that we would not achieve our forecasted revenue and earnings for 2012, partially due to the recruiting incentive program not driving the expected Representative productivity, and as a result, Silpada experienced weaker than expected performance in the fourth quarter of 2012. The revenue performance in the fourth quarter of 2012 was approximately 19% less than the estimates utilized in our 2011 impairment analysis. Based on these continued trends, in the latter part of the fourth quarter of 2012, in conjunction with the 2013 planning process and the early stages of our evaluation of strategic alternatives for the business, we lowered our long-term revenue and earnings projections for Silpada in our discounted cash flow ("DCF") model to reflect a more moderate recovery of the business. The more moderate recovery of the business was believed to be appropriate due to the lack of sales momentum in the business and the continued inability of Silpada to achieve our financial performance expectations. The decline in the fair values of the Silpada reporting unit, the trademark, and the customer relationships was primarily driven by the reduction in the forecasted long-term growth rates and cash flows used to estimate fair value. The lower than expected results for fiscal year 2012 served as the baseline for the long-term projections of the business. Fiscal year 2012 revenue for Silpada was approximately 10% less than the estimates utilized in our 2011 impairment analysis and 19% less than fiscal year 2011 results. We forecasted revenue and the resulting cash flows over ten years using a DCF model which included a terminal value at the end of the projection period.

AVON PRODUCTS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in millions, except per share data)

4. INVENTORIES

Components of Inventories	June 30, 2013	December 31, 2012
Raw materials	$382.2	$393.4
Finished goods	772.1	707.7
Total	$1,154.3	$1,101.1

5. EMPLOYEE BENEFIT PLANS

	Three Months Ended June 30, Pension Benefits					
Net Periodic Benefit Costs	U.S. Plans		Non-U.S. Plans		Postretirement Benefits	
	2013	2012	2013	2012	2013	2012
Service cost	$3.4	$3.7	$2.8	$4.5	$.5	$.5
Interest cost	7.0	7.4	9.0	9.7	1.1	1.4
Expected return on plan assets	(9.4)	(8.8)	(10.1)	(9.8)	—	—
Amortization of prior service credit	(.1)	—	—	(.4)	(1.2)	(3.3)
Amortization of net actuarial losses	12.0	10.1	2.7	4.4	.6	1.0
Curtailments	—	—	(7.5)	—	—	(1.0)
Net periodic benefit costs	$12.9	$12.4	$(3.1)	$8.4	$1.0	$(1.4)

	Six Months Ended June 30, Pension Benefits					
Net Periodic Benefit Costs	U.S. Plans		Non-U.S. Plans		Postretirement Benefits	
	2013	2012	2013	2012	2013	2012
Service cost	$8.4	$7.5	$7.6	$9.0	$1.0	$1.0
Interest cost	13.6	14.8	18.1	19.5	2.5	2.9
Expected return on plan assets	(18.8)	(18.0)	(19.9)	(19.6)	—	—
Amortization of prior service credit	(.2)	(.1)	(.3)	(.8)	(2.4)	(6.6)
Amortization of net actuarial losses	23.3	21.9	7.3	8.8	1.4	2.0
Curtailments	—	—	(7.5)	—	—	(1.0)
Net periodic benefit costs	$26.3	$26.1	$5.3	$16.9	$2.5	$(1.7)

The curtailment gain recognized in the second quarter of 2013 is due to the decision to freeze our defined benefit pension plan in the United Kingdom.

As of June 30, 2013, we made approximately $12 and $47 of contributions to the U.S. and non-U.S. pension and postretirement plans, respectively. During the remainder of 2013, we anticipate contributing approximately $43 to $48 and $18 to $23 to fund our U.S. and non-U.S. pension and postretirement plans, respectively. The contributions made as of June 30, 2013 to the non-U.S. pension and postretirement plans include $25 as a result of our decision to freeze our defined benefit pension plan in the United Kingdom. All future pension benefits in the United Kingdom will now accrue on a defined contribution basis rather than on a defined benefit basis. Our funding requirements may be impacted by regulations or interpretations thereof.

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AVON PRODUCTS, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in millions, except per share data)

6. CONTINGENCIES

FCPA Investigations

As previously reported, we have engaged outside counsel to conduct an internal investigation and compliance reviews focused on compliance with the Foreign Corrupt Practices Act ("FCPA") and related U.S. and foreign laws in China and additional countries. The internal investigation, which is being conducted under the oversight of our Audit Committee, began in June 2008.

As previously reported in July 2009, in connection with the internal investigation, we commenced compliance reviews regarding the FCPA and related U.S. and foreign laws in additional countries in order to evaluate our compliance efforts. We are conducting these compliance reviews in a number of countries selected to represent each of the Company's international geographic segments. The internal investigation and compliance reviews are focused on reviewing certain expenses and books and records processes, including, but not limited to, travel, entertainment, gifts, use of third-party vendors and consultants and related due diligence, joint ventures and acquisitions, and payments to third-party agents and others, in connection with our business dealings, directly or indirectly, with foreign governments and their employees. The internal investigation and compliance reviews of these matters are substantially complete. In connection with the internal investigation and compliance reviews, certain personnel actions, including termination of employment of certain senior members of management, have been taken, and additional personnel actions may be taken in the future. In connection with the internal investigation and compliance reviews, we continue to enhance our ethics and compliance program, including our policies and procedures, FCPA compliance-related training, FCPA third-party due diligence program and other compliance-related resources.

As previously reported in October 2008, we voluntarily contacted the United States Securities and Exchange Commission ("SEC") and the United States Department of Justice ("DOJ") to advise both agencies of our internal investigation. We have cooperated and continue to cooperate with investigations of these matters by the SEC and the DOJ. We have, among other things, signed tolling agreements, responded to inquiries, translated and produced documents, assisted with interviews, and provided information on our internal investigation and compliance reviews, personnel actions taken and steps taken to enhance our ethics and compliance program. As previously reported in August 2012, we are in discussions with the SEC and the DOJ regarding resolving the government investigations. Our factual presentations as part of these discussions are substantially complete. In June 2013, we made an offer of settlement to the DOJ and the SEC that, among other terms, included payment of monetary penalties of approximately $12. The DOJ and the SEC have rejected the terms of our offer. Although we expect that the DOJ and the SEC will make a counterproposal to our offer, they have not yet done so. Our discussions with the DOJ and the SEC are ongoing.

There can be no assurance that a settlement with the SEC and the DOJ will be reached or, if a settlement is reached, the timing of any such settlement or the terms of any such settlement. We expect any such settlement will include civil and/or criminal fines and penalties, and may also include non-monetary remedies, such as oversight requirements and additional remediation and compliance requirements. We may be required to incur significant future costs to comply with the non-monetary terms of any settlement with the SEC and the DOJ. Under certain circumstances, we may also be required to advance significant professional fees and expenses to certain current and former Company employees in connection with these matters. Until any settlement or other resolution of these matters, we expect to continue to incur costs, primarily professional fees and expenses, which may be significant, in connection with the government investigations.

At this point we are unable to predict the developments in, outcome of, and economic and other consequences of the government investigations or their impact on our earnings, cash flows, liquidity, financial condition and ongoing business. However, based on our most recent discussions with the DOJ and the SEC, the Company believes that it is probable that the Company will incur a loss upon settlement that is higher than the offer made by the Company of approximately $12, which was accrued by the Company as of June 30, 2013. We are unable to reasonably estimate the amount of any additional loss above the amount accrued to date; however it is reasonably possible that such additional loss will be material.

Litigation Matters

In July and August 2010, derivative actions were filed in state court against certain present or former officers and/or directors of the Company (Carol J. Parker, derivatively on behalf of Avon Products, Inc. v. W. Don Cornwell, et al. and Avon Products, Inc. as nominal defendant (filed in the New York Supreme Court, Nassau County, Index No. 600570/2010); Lynne Schwartz, derivatively on behalf of Avon Products, Inc. v. Andrea Jung, et al. and Avon Products, Inc. as nominal defendant (filed in the New York Supreme Court, New York County, Index No. 651304/2010)). These actions allege breach of fiduciary duty, abuse of control, waste of corporate assets, and, in one complaint, unjust enrichment, relating to the Company's compliance with the FCPA, including the adequacy of the Company's internal controls. The relief sought against the individual defendants in one or both of these derivative complaints includes certain declaratory and equitable relief, restitution, damages, exemplary damages and interest. The Company is a nominal defendant, and no relief is sought against the Company itself. In the Parker case, plaintiff has agreed that defendants' time to file an answer, motion to dismiss or other response is adjourned until plaintiff files an amended pleading. In Schwartz, the parties have agreed to defer the filing of an amended complaint and the defendants' response thereto until the parties submit a further stipulation addressing the scheduling of proceedings. On May 14, 2012, County of York Retirement Plan ("County of York") - which had been a plaintiff in a previously-filed but now discontinued derivative action - filed a complaint against the Company seeking enforcement of its demands for the inspection of certain of the Company's books and records (County of York Retirement Plan v. Avon Products, Inc., New York Supreme Court, New York County, Index No. 651673/2012). On July 10, 2012, the Company moved to dismiss County of York's complaint. We are unable to predict the outcome of these matters.

On July 6, 2011, a purported shareholder's class action complaint (City of Brockton Retirement System v. Avon Products, Inc., et al., No. 11-CIV-4665) was filed in the United States District Court for the Southern District of New York against certain present or former officers and/or directors of the Company. On September 29, 2011, the Court appointed LBBW Asset Management Investmentgesellschaft mbH and SGSS Deutschland Kapitalanlagegesellschaft mbH as lead plaintiffs and Motley Rice LLC as lead counsel. Lead plaintiffs have filed an amended complaint on behalf of a purported class consisting of all persons or entities who purchased or otherwise acquired shares of Avon's common stock from July 31, 2006 through and including October 26, 2011. The amended complaint names the Company and two individual defendants and asserts violations of Sections 10(b) and 20(a) of the Exchange Act based on allegedly false or misleading statements and omissions with respect to, among other things, the Company's compliance with the FCPA, including the adequacy of the Company's internal controls. Plaintiffs seek compensatory damages as well as injunctive relief. Defendants moved to dismiss the amended complaint on June 14, 2012. We are unable to predict the outcome of this matter. However, it is reasonably possible that we may incur a loss in connection with this matter. We are unable to reasonably estimate the amount or range of such reasonably possible loss.

Under some circumstances, any losses incurred in connection with adverse outcomes in the litigation matters described above could be material.

In April 2012, several purported shareholders' actions were filed against the Company and certain present or former directors of the Company in New York Supreme Court, New York County (Pritika v. Jung, et al., Index No. 651072/2012; Feinman v. Avon Products, Inc., et al., Index No. 651087/2012; Gaines v. Jung, et al., Index No. 651097/2012; Schwartz v. Avon Products, Inc., et al., Index No. 651152/2012; Robaczynki, individually and on behalf of all others similarly situated and derivatively on behalf of Avon Products, Inc. v. Jung, et al., Index No. 651176/2012). On April 26, 2012, the actions were consolidated in New York Supreme Court, New York County (In re Avon Products, Inc. Shareholder Litigation, Consolidated Index No. 651087/2012E). An amended consolidated complaint was filed on May 18, 2012. The amended consolidated complaint asserts a derivative claim against the individual defendants based on alleged breaches of fiduciary duties in connection with indications of interest by Coty, Inc. in acquiring the Company. The Company is named as a nominal defendant on the purported derivative claim, and no relief appears to be sought against the Company on that claim. The amended consolidated complaint also asserts a purported direct claim on behalf of a class of shareholders against the individual defendants based on alleged breaches of such fiduciary duties. Plaintiffs seek compensatory damages as well as injunctive relief. On June 27, 2012, defendants moved to dismiss the consolidated action. By decision and order dated March 5, 2013, the court granted defendants' motion to dismiss the complaint with prejudice. On April 1, 2013, plaintiffs filed a notice of appeal from the court's order dismissing the complaint. On July 1, 2013, plaintiffs' appeal was withdrawn with prejudice.

Brazilian Tax Matters

In 2002, our Brazilian subsidiary received an excise tax (IPI) assessment from the Brazilian tax authorities for alleged tax deficiencies during the years 1997-1998. In December 2012, additional assessments were received for the year

2008 with respect to excise tax (IPI) and taxes charged on gross receipts (PIS and COFINS), totaling approximately $373, $56 and $258 each, including penalties and accrued interest, at the exchange rate on June 30, 2013. The 2002 and the 2012 assessments assert that the establishment in 1995 of separate manufacturing and distribution companies in that country was done without a valid business purpose and that Avon Brazil did not observe minimum pricing rules to define the taxable basis of excise tax. The structure adopted in 1995 is comparable to that used by many other companies in Brazil. We believe that our Brazilian corporate structure is appropriate, both operationally and legally, and that the 2002 and 2012 assessments are unfounded.

These matters are being vigorously contested. In January 2013, we filed a protest seeking a first administrative level review with respect to the 2012 assessments. In July 2013, the 2012 IPI assessment was upheld at the first administrative level (decisions regarding the 2012 PIS and COFINS assessments remain pending). We intend to appeal the decision to the second administrative level. In October 2010, the 2002 assessment was upheld at the first administrative level at an amount reduced to approximately $