

BLACK HILLS CORP /SD/
Form S-4
November 29, 2002
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As filed with the Securities and Exchange Commission on November 29, 2002

Registration No. 333-

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

**FORM S-4
REGISTRATION STATEMENT
UNDER
THE SECURITIES ACT OF 1933**

BLACK HILLS CORPORATION

(Exact name of Registrant as specified in its charter)

South Dakota
(State or other jurisdiction of
incorporation or organization)

4911
(Primary Standard Industrial
Classification Code Number)

46-0458824
(I.R.S. Employer
Identification No.)

**625 Ninth Street
Rapid City, South Dakota 57701
(605) 721-1700**
(Address, including zip code, and telephone number, including area code, of
Registrant's principal executive offices)

**Steven J. Helmers
625 Ninth Street
Rapid City, South Dakota 57701
(605) 721-1700**
(Name, address, including zip code, and telephone number,
including area code, of agent for service)

Copies to:

**Dennis M. Jackson, Esq.
Holland & Hart LLP
555 Seventeenth Street, Suite 3200
Denver, Colorado 80202
(303) 295-8115**

**Alan P. Baden, Esq.
Vinson & Elkins L.L.P.
666 Fifth Avenue, 26th Floor
New York, New York 10103-0040
(917) 206-8001**

Approximate date of commencement of proposed sale to public: As soon as practicable after this Registration Statement becomes effective.

If the securities being registered on this form are being offered in connection with the formation of a holding company and there is compliance with General Instruction G, check the following box. " _____"

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. " _____"

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. " _____"

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the Registration Statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

CALCULATION OF REGISTRATION FEE

<u>Title of Each Class of Securities to be Registered</u>	<u>Amount to be Registered(1)</u>	<u>Proposed Maximum Offering Price Per Unit(2)</u>	<u>Proposed Maximum Aggregate Offering Price(2)</u>	<u>Amount of Registration Fee</u>
Common Stock, par value \$1.00 per share	487,576	\$ 1.03	\$ 11,413,704	\$ 1,051

- (1) Represents 487,576 shares, the maximum number of shares of Black Hills Corporation common stock, par value \$1.00 per share, issuable upon the conversion, pursuant to the merger described herein, of (i) 10,779,718 shares of common stock, par value \$.01 per share, of Mallon Resources Corporation outstanding on November 21, 2002 and (ii) up to 301,548 shares of Mallon Resources Corporation common stock that may be issued upon the exercise of outstanding options and warrants to purchase Mallon Resources Corporation common stock between November 21, 2002 and the consummation of the merger, based upon the exchange ratio of .044 of a share of Black Hills Corporation common stock for each share of Mallon Resources Corporation common stock.
- (2) Estimated solely for the purpose of calculating the registration fee pursuant to Rule 457 under the Securities Act of 1933, as amended, based upon the product of \$1.03 (the average of the high and low prices of Mallon Resources Corporation's common stock on November 21, 2002 on the OTC Bulletin Board) multiplied by (i) 10,779,718 shares of common stock of Mallon Resources Corporation common stock outstanding on November 21, 2002 plus (ii) 301,548 shares of Mallon Resources Corporation common stock that may be issued upon the exercise of outstanding options and warrants.

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The information in this prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

SUBJECT TO COMPLETION, DATED NOVEMBER 29, 2002

PROPOSED MERGER YOUR VOTE IS VERY IMPORTANT

Black Hills Corporation, or Black Hills, and Mallon Resources Corporation, or Mallon, have agreed on a merger involving our two companies. Before we can complete the merger, we must obtain the approval of Mallon's common shareholders. We are sending you this proxy statement/prospectus to ask you to vote in favor of the merger.

In the merger, Black Hills Acquisition Corp., a wholly-owned subsidiary of Black Hills, will merge with and into Mallon. Upon consummation of the merger, Mallon will be the surviving company and a wholly-owned subsidiary of Black Hills. As a Mallon shareholder, you will be entitled to receive .044 shares of Black Hills common stock for each share of Mallon common stock and cash instead of any fractional shares you would otherwise receive in the merger.

Black Hills' common stock is traded on the New York Stock Exchange under the symbol BKH. On _____, the closing price of Black Hills common stock was \$ _____ per share and the closing price of Mallon common stock was \$ _____ per share. We encourage you to obtain more recent quotations. Shares of Mallon common stock will be deregistered if the merger is consummated.

Mallon will hold a special meeting of its shareholders on _____, 2003, at 9:00 a.m. local time, at _____, located at _____, Denver, Colorado, to consider and vote on the merger agreement. At Mallon's special meeting, Mallon will ask its common shareholders to consider and vote on the merger agreement. Shareholder approval of the proposal is a prerequisite to consummation of the merger. Holders of Mallon common stock are entitled to dissenters' rights in connection with the merger, which are discussed in greater detail on page 37.

TO CAST YOUR VOTE FOR THE SPECIAL MEETING, PLEASE COMPLETE, SIGN AND DATE YOUR PROXY CARD AND RETURN IT IN THE ENCLOSED ENVELOPE.

The enclosed form of proxy, when executed and returned, will be voted as set forth therein. Any shareholder signing a proxy has the power to revoke the proxy in writing, addressed to Mallon, or in person at the meeting at any time before the proxy is exercised.

This document is a prospectus of Black Hills relating to the issuance of shares of Black Hills' common stock in connection with the merger and a proxy statement for Mallon to use in soliciting proxies for its special meeting. It contains answers to frequently asked questions and a summary description of the merger (beginning on page 24), followed by a more detailed discussion of the merger and related matters. **YOU SHOULD ALSO CONSIDER THE MATTERS DISCUSSED UNDER RISK FACTORS COMMENCING ON PAGE 11 OF THE ENCLOSED PROXY STATEMENT/PROSPECTUS. WE URGE YOU TO CAREFULLY REVIEW THIS ENTIRE DOCUMENT.**

NEITHER THE SECURITIES AND EXCHANGE COMMISSION NOR ANY STATE SECURITIES COMMISSION HAS APPROVED OR DISAPPROVED OF THESE SECURITIES OR PASSED UPON THE ADEQUACY OR ACCURACY OF THIS PROXY STATEMENT/PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

THIS PROXY STATEMENT/PROSPECTUS IS DATED _____, 2003 AND IS FIRST BEING MAILED TO SHAREHOLDERS ON OR ABOUT JANUARY _____, 2003.

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MALLON RESOURCES CORPORATION

999 18TH STREET, SUITE 1700
DENVER, COLORADO 80202
(303) 293-2333

**NOTICE OF SPECIAL MEETING OF SHAREHOLDERS
TO BE HELD ON _____, 2003**

To Shareholders of Mallon Resources Corporation:

NOTICE IS HEREBY GIVEN that a Special Meeting of Shareholders of Mallon Resources Corporation, a Colorado corporation, or Mallon, will be held at _____, on _____, 2003 at 9:00 a.m., local time, for the following purposes:

1. To consider and vote upon a proposal to approve the Agreement and Plan of Merger, dated October 1, 2002, among Black Hills Corporation, Black Hills Acquisition Corp. and Mallon.
2. To transact such other business incident to the conduct of the meeting as may properly come before the meeting or any adjournments or postponements thereof.

Only common shareholders of record at the close of business on _____, 200 are entitled to notice of and to vote at the Mallon special meeting or at any adjournments or postponements thereof. Approval of the merger agreement requires the affirmative vote of a majority of the outstanding shares of Mallon common stock. Approval of the merger agreement is a prerequisite to the completion of the merger. Holders of Mallon common stock are entitled to dissenters' rights under the Colorado Business Corporation Act in respect of the merger.

The Mallon board of directors has determined that the terms of the merger agreement and the transactions contemplated by it are advisable and in the best interests of Mallon and its shareholders. Accordingly, the members of the Mallon board of directors have unanimously approved the merger and the merger agreement and recommend that common shareholders vote at the special meeting to approve the merger agreement.

Please do not send us any Mallon stock certificates at this time. If the merger is approved by the common shareholders of Mallon, and if the other conditions to the merger agreement are satisfied or waived, forms to be used to exchange your shares of Mallon common stock for shares of Black Hills Corporation common stock will be mailed to you.

By Order of the Board of
Directors,

George O. Mallon, Jr.
Chairman

Denver, Colorado
, 2003

YOUR VOTE IS VERY IMPORTANT. EVEN IF YOU PLAN TO ATTEND THE SPECIAL MEETING IN PERSON, WE REQUEST THAT YOU SIGN AND RETURN THE ENCLOSED PROXY OR VOTING INSTRUCTION CARD AND THUS ENSURE THAT YOUR SHARES WILL BE REPRESENTED AT THE SPECIAL MEETING IF YOU ARE UNABLE TO ATTEND. IF YOU DO ATTEND THE SPECIAL MEETING AND WISH TO VOTE IN PERSON, YOU MAY WITHDRAW YOUR PROXY AND VOTE IN PERSON.

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REFERENCES TO ADDITIONAL INFORMATION

This document incorporates important business and financial information about our companies from documents we have filed with the Securities and Exchange Commission, or SEC, but have not included or delivered with this document. If you call or write us, we will send you these documents, excluding exhibits, without charge. You can contact us at:

Black Hills Corporation
625 Ninth Street
Rapid City, South Dakota

Attention: Steven J. Helmers
605-721-2300

Mallon Resources Corporation
999 18th Street, Suite 1700
Denver, Colorado 80202

Attention: Roy K. Ross
303-293-2333

PLEASE REQUEST DOCUMENTS FROM EITHER COMPANY NOT LATER THAN _____, 2003. IF YOU REQUEST ANY DOCUMENTS, WE WILL MAIL THE DOCUMENTS TO YOU BY FIRST CLASS MAIL, OR ANOTHER EQUALLY PROMPT MEANS, BY THE NEXT BUSINESS DAY AFTER WE RECEIVE YOUR REQUEST.

See [Where You Can Find More Information](#) on page 127 for more information about the documents referred to in this document.

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LIST OF ANNEXES

Annex A	Agreement and Plan of Merger dated as of October 1, 2002 by and among Black Hills Corporation, Black Hills Acquisition Corp. and Mallon Resources Corporation
Annex B	Opinion of Waterous & Co. Limited dated October 1, 2002
Annex C	Provisions of Colorado Business Corporation Act relating to dissenters rights

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QUESTIONS AND ANSWERS ABOUT THE MERGER

Q: WHY ARE THE TWO COMPANIES PROPOSING TO MERGE?

A: The proposed merger will combine the businesses of Black Hills and Mallon. Our companies are proposing the merger because we believe that the combined company, with its larger, more diverse asset base and expanded cash flow, will be better positioned to continue growing in the independent energy industry. We believe that the merger will, among other things:

support Black Hills' integrated energy strategy by substantially increasing its current natural gas production and reserves;

increase Black Hills' exploitation drilling potential;

result in administrative cost savings and operating efficiencies on a combined basis; and

improve the liquidity of Mallon's shareholders.

Please review the more detailed description of our reasons for the merger on pages 28-29.

Q: HOW WILL THE MERGER WORK?

A: Black Hills Acquisition Corp., a wholly-owned subsidiary of Black Hills, will merge with and into Mallon and Mallon will continue as the surviving corporation and will be a wholly-owned subsidiary of Black Hills. We refer to Black Hills Acquisition Corp. as Merger Sub in this document. Shareholders of Mallon will become shareholders of Black Hills.

Q: WHAT WILL HAPPEN TO MALLON COMMON STOCK AND STOCK OPTIONS IN THE MERGER?

A: Mallon shareholders will receive .044 of a share of Black Hills common stock for each share of Mallon common stock they own. Mallon shareholders will also receive cash for any fractional Black Hills shares they would otherwise receive in the merger. As of the close of business on the effective date of the merger, all outstanding options to purchase Mallon common stock that are not exercised will be cancelled and terminated automatically. Each holder of an option who exercises such option concurrently with the consummation of the merger will receive .044 of a share of Black Hills common stock for each share of Mallon common stock received upon exercise of such option.

Q: WHEN DO YOU EXPECT THE MERGER TO BE COMPLETED?

A: Subject to shareholder and regulatory approval, we hope to complete the merger in the first quarter of 2003.

Q: WHEN IS THE SPECIAL SHAREHOLDERS' MEETING?

A: Mallon's special meeting of shareholders will take place on _____, 2003. The time and location of the special meeting is specified on the cover page of this document.

Q: WHAT WILL HAPPEN AT THE SPECIAL SHAREHOLDERS' MEETING?

A: Mallon's shareholders will vote on whether to approve the merger agreement and the transactions contemplated by the merger agreement.

Q: WHAT VOTE IS REQUIRED FOR THE PROPOSAL?

A: At the Mallon special meeting, approval of the merger agreement requires the affirmative vote of a majority of the outstanding shares of Mallon common stock.

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Q: WHAT DO I NEED TO DO TO VOTE?

A: If you own Mallon common stock, after reading this document, indicate on the enclosed proxy how you want to vote, sign it and mail it in the enclosed return envelope as soon as possible so that your shares will be represented at the special meeting. If you sign and send in your proxy card and do not indicate how you want to vote, your proxy will be counted as a vote in favor of the proposals submitted at the special meeting. The failure to return your proxy card will have the same effect as voting against the merger.

You may attend the special meeting and vote your shares in person, rather than signing and mailing your proxy card. In addition, you may revoke your proxy on or before the day of the special meeting by following the instructions on page 22. You then may either change your vote or attend the special meeting and vote in person.

THE MEMBERS OF THE MALLON BOARD OF DIRECTORS HAVE UNANIMOUSLY APPROVED THE MERGER AND THE MERGER AGREEMENT AND RECOMMEND THAT MALLON SHAREHOLDERS VOTE FOR THE APPROVAL OF THE MERGER AGREEMENT.

Q: IF MY SHARES ARE HELD IN STREET NAME BY MY BROKER, WILL MY BROKER VOTE THEM FOR ME?

A: Your broker will not be able to vote your shares without instructions from you. You should instruct your broker to vote your shares, following the procedure provided by your broker.

Q: SHOULD I SEND IN MY STOCK CERTIFICATES NOW?

A: No. After the merger is completed, we will send you written instructions that explain how to exchange your stock certificates for certificates representing Black Hills common stock. Please do not send in any stock certificates until you receive these written instructions and the letter of transmittal.

Q: WILL MALLON SHAREHOLDERS BE ABLE TO TRADE THE BLACK HILLS COMMON STOCK THAT THEY RECEIVE IN THE MERGER?

A: Yes. Except for Black Hills common stock to be held by certain affiliates of Mallon, the Black Hills common stock received in the merger will be freely tradable. The Black Hills common stock issued in connection with the merger will be listed on the New York Stock Exchange under the symbol BKH.

Q: AM I ENTITLED TO DISSENTERS RIGHTS?

A: Yes. Holders of Mallon common stock are entitled to dissenters rights in connection with the merger. See the detailed description beginning on page 37.

Q: WHAT ARE THE UNITED STATES FEDERAL INCOME TAX CONSEQUENCES OF THE MERGER TO BLACK HILLS AND MALLON COMMON SHAREHOLDERS?

A: A summary of certain United States federal income tax consequences of the merger likely to be material to typical shareholders of Mallon and Black Hills is included in the section Certain Material United States Federal Income Tax Consequences of the Merger beginning on page 50.

Q: ARE THERE RISKS ASSOCIATED WITH THE MERGER THAT I SHOULD CONSIDER IN DECIDING HOW TO VOTE?

A: Yes. You should carefully read the detailed description of the risks associated with the merger and Black Hills beginning on page 11.

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A: If you have more questions about the merger you should contact:

Roy K. Ross
Mallon Resources Corporation
999 18th Street, Suite 1700
Denver, Colorado 80202

Aggregate intrinsic value (A)	\$	26million	\$	million
Weighted average remaining option term (in years)		6		7
Option shares exercisable (vested), September 30		21		17
Weighted average exercise price	\$	26	\$	26
Aggregate intrinsic value (A)	\$	million	\$	million
Weighted average remaining option term (in years)		4		5

(A) Aggregate intrinsic value is calculated using the Company's stock price at each respective date, less the exercise price (grant date price) multiplied by the number of shares.

At
September 30,
2009 and 2008,
there was
\$47 million and
\$68 million,
respectively, of
unrecognized
compensation
expense (using
the
Black-Scholes
option pricing
model) related
to unvested
stock options;
such options
had a weighted
average vesting
period of three
years in 2009
and 2008.

MASCO CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)

Note C concluded:

The weighted average grant date fair value of option shares granted and the assumptions used to estimate those values using a Black-Scholes option pricing model, were as follows:

	Nine Months Ended September 30,	
	2009	2008
Weighted average grant date fair value	\$ 2.23	\$ 3.72
Risk-free interest rate	2.59%	3.25%
Dividend yield	3.73%	4.96%
Volatility factor	39.07%	32.00%
Expected option life	6 years	6 years

D. The Company sponsors qualified defined-benefit and defined-contribution retirement plans for most of its employees. In addition to the Company's qualified defined-benefit pension plans, the Company has unfunded non-qualified defined-benefit pension plans covering certain employees, which provide for benefits in addition to those provided by the qualified pension plans. Substantially all salaried employees participate in non-contributory defined-contribution retirement plans, to which payments are determined annually by the Organization and Compensation Committee of the Board of Directors.

Net periodic pension cost for the Company's defined-benefit pension plans was as follows, in millions:

	Three Months ended September 30,			
	2009		2008	
	Qualified	Non-Qualified	Qualified	Non-Qualified
Service cost	\$ 3	\$	\$ 4	\$
Interest cost	7	2	12	3
Expected return on plan assets	(5)		(13)	
Amortization of prior service cost				
Amortization of net loss	3			
Net periodic pension cost	\$ 8	\$ 2	\$ 3	\$ 3

	Nine Months ended September 30,			
	2009		2008	
	Qualified	Non-Qualified	Qualified	Non-Qualified
Service cost	\$ 9	\$ 1	\$ 13	\$ 1
Interest cost	26	5	40	7
Expected return on plan assets	(18)		(43)	
Amortization of prior service cost		1		
Recognized curtailment loss	3	5		
Amortization of net loss	10		1	1
Net periodic pension cost	\$ 30	\$ 12	\$ 11	\$ 9

In March 2009, based on management's recommendation, the Board of Directors approved a plan to freeze all future benefit accruals under substantially all of the Company's domestic qualified and non-qualified defined-benefit pension plans. The freeze is effective January 1, 2010. As a result of this action, the liabilities for

the plans impacted by the freeze were remeasured and the Company recognized a curtailment charge of \$8 million in the first quarter of 2009. In addition, the Company expects net periodic pension costs related to the domestic defined-benefit pension plans that were remeasured to decrease by approximately \$14 million in 2009 to \$31 million from the original forecast of \$45 million at December 31, 2008.

MASCO CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)

Note D concluded:

Assumptions

Major assumptions used in accounting for the Company's domestic defined-benefit pension plans that have been frozen were as follows:

	At March 31, 2009
Discount rate for obligations	7.3%
Expected return on plan assets	8.0%
Discount rate for net periodic pension cost	6.1%

The discount rate for obligations was based upon the expected duration of each defined-benefit pension plan's liabilities matched to the March 31, 2009 Citigroup Pension Discount Curve. Such rates for the Company's domestic defined-benefit pension plans that will be frozen ranged from 7.0 percent to 7.4 percent, with the most significant portion of the liabilities having a discount rate for obligations of 7.4 percent at March 31, 2009.

The Company determined the expected long-term rate of return on plan assets by reviewing an analysis of expected and historical rates of return of various asset classes based upon the current and long-term target asset allocation of the plan assets. The measurement date used to determine the defined-benefit pension expense was March 31.

E. The changes in the carrying amount of goodwill for the nine months ended September 30, 2009, by segment, were as follows, in millions:

	At Dec. 31, 2008	Additions (A)	Other(B)	At Sep. 30, 2009
Cabinets and Related Products	\$ 225	\$ 4	\$ 2	\$ 227
Plumbing Products	248	4	10	262
Installation and Other Services	1,768			1,768
Decorative Architectural Products	294			294
Other Specialty Products	836			836
Total	\$ 3,371	\$ 4	\$ 12	\$ 3,387

(A) Additions include acquisitions.

(B) Other principally includes the effect of foreign currency translation, reclassifications and purchase

price
adjustments
related to
prior-year
acquisitions.

Other indefinite-lived intangible assets were \$196 million and \$195 million at September 30, 2009 and December 31, 2008, respectively, and principally included registered trademarks. The carrying value of the Company's definite-lived intangible assets was \$97 million (net of accumulated amortization of \$64 million) at September 30, 2009 and \$104 million (net of accumulated amortization of \$56 million) at December 31, 2008, and principally included customer relationships and non-compete agreements.

F. Depreciation and amortization expense was \$190 million and \$179 million, respectively, for the nine months ended September 30, 2009 and 2008.

MASCO CORPORATION**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)**

- G. The Company has maintained investments in available-for-sale securities and a number of private equity funds, principally as part of its tax planning strategies, as any gains enhance the utilization of any current and future tax capital losses. Financial investments included in other assets were as follows, in millions:

	September 30, 2009	December 31, 2008
Asahi Tec Corporation common and preferred stock	\$ 74	\$ 73
TriMas Corporation	13	3
Auction rate securities	22	22
Marketable securities		3
Private equity funds	125	138
Other investments	9	10
Total	\$ 243	\$ 249

The Company's investments in available-for-sale securities at September 30, 2009 and December 31, 2008 (including marketable securities, auction rate securities, Asahi Tec Corporation common and preferred stock and TriMas Corporation) were as follows, in millions:

	Cost Basis	Pre-tax Unrealized Gains	Pre-tax Unrealized Losses	Recorded Basis
September 30, 2009	\$ 72	\$37	\$	\$109
December 31, 2008	\$ 75	\$26	\$	\$101

MASCO CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)

Note G continued:

The Company's investments in private equity funds and other private investments are carried at cost. It is not practicable for the Company to estimate a fair value because the private equity funds have no quoted market price and sufficient information is not readily available for the Company to utilize a valuation model to determine the fair value for each fund. These investments are evaluated quarterly for potential other-than-temporary impairment when impairment indicators are present, or when an event or change in circumstances has occurred, that may have a significant adverse effect on the fair value of the investment. Impairment indicators the Company considers include the following: whether there has been a significant deterioration in earnings performance, asset quality or business prospects; a significant adverse change in the regulatory, economic or technological environment; a significant adverse change in the general market condition or geographic area in which the investment operates; industry and sector performance; current equity and credit market conditions; and any bona fide offers to purchase the investment for less than the carrying value. The Company also considers specific adverse conditions related to the financial health of and business outlook for the fund, including industry and sector performance. The significant assumptions utilized in analyzing a fund for potential other-than-temporary impairment include current economic conditions, market analysis for specific funds and performance indicators in the automotive and transportation, residential and commercial construction, bio-technology, health care and information technology sectors in which the applicable funds investments operate. Since there is no active trading market for these investments, they are for the most part illiquid. These investments, by their nature, can also have a relatively higher degree of business risk, including financial leverage, than other financial investments. Future changes in market conditions, the future performance of the underlying investments or new information provided by private equity fund managers could affect the recorded values of such investments and the amounts realized upon liquidation. During the nine months ended September 30, 2009, the Company determined that the decline in the estimated value of five private equity funds (with a carrying value of \$41 million prior to impairment) was other-than-temporary and, accordingly, recognized non-cash, pre-tax impairment charges of \$10 million for the nine months ended September 30, 2009.

The remaining private equity investments, with an aggregate carrying value of \$94 million and \$95 million at September 30, 2009 and December 31, 2008, respectively, were not evaluated for impairment, as there were no indicators of impairment or identified events or changes in circumstances that would have a significant adverse effect on the fair value of the investments.

MASCO CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)

Note G concluded:

Income from financial investments, net, included in other, net, within other income (expense), net, and impairment charges for financial investments were as follows, in millions:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2009	2008	2009	2008
Realized gains from marketable securities	\$	\$	\$	\$
Realized losses from marketable securities				(3)
Dividend income from marketable securities				
Income from other investments, net				3
Dividend income from other investments				
 Income from financial investments, net	 \$	 \$	 \$	 \$
 Impairment charges:				
Marketable securities	\$	\$ (1)	\$	\$ (1)
Private equity funds			(10)	(7)
TriMas Corporation				(22)
 Impairment charges	 \$	 \$ (1)	 \$ (10)	 \$ (30)

H. During 2009 and 2008, the Company entered into foreign currency exchange contracts to hedge currency fluctuations related to intercompany loans denominated in non-functional currencies. At September 30, 2009 and December 31, 2008, the Company had recorded losses of \$1 million and \$16 million, respectively, on the foreign currency exchange contracts, which is more than offset by gains related to the translation of loans and accounts denominated in non-functional currencies. Gains (losses) related to these contracts are recorded in the Company's consolidated statements of income in other income (expense), net. For the three months and nine months ended September 30, 2009, the Company had recorded gains (losses) of \$2 million and \$(1) million, respectively, related to these foreign currency exchange contracts. For the three months and nine months ended September 30, 2008, the Company had recorded losses of \$14 million and \$18 million, respectively, related to these foreign currency exchange contracts.

During 2009 and 2008, the Company, including certain European operations, also entered into foreign currency forward contracts to manage a portion of its exposure to currency fluctuations in the European euro and the U.S. dollar. At September 30, 2009, no gains had been recorded, based upon period-end market prices. At December 31, 2008, the Company had recorded gains of \$2 million on these contracts based upon period-end market prices. Gains (losses) related to these contracts are recorded in the Company's consolidated statements of income in other income (expense), net. For the three months and nine months ended September 30, 2009, the Company had recorded losses of \$1 million and \$2 million, respectively, related to these foreign currency exchange contracts. For the nine months ended September 30, 2008, the Company had recorded a gain of \$1 million related to these foreign currency exchange contracts.

MASCO CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)

Note H concluded:

In the event that the counterparties fail to meet the terms of the foreign currency forward contracts, the Company's exposure is limited to the aggregate foreign currency rate differential with such institutions.

- I. At September 30, 2009 and December 31, 2008, there were outstanding \$108 million principal amount of Zero Coupon Convertible Senior Notes due 2031, with an accreted value of \$55 million and \$54 million, respectively. The Company adopted new FASB guidance regarding accounting for convertible debt instruments that may be settled in cash upon conversion (including partial cash settlement) effective January 1, 2009. The adoption of this new guidance will have no impact on 2009 results; the Company recorded a \$1 million cumulative effect of accounting change as of January 1, 2007 and the adoption had no impact on the Company's condensed consolidated financial statements for the periods ended September 30, 2009 and 2008.

At the Company's request, in late April 2009, the Company and its Bank Group modified the terms of its Five-Year Revolving Credit Facility, which expires February 2011. After reviewing its anticipated liquidity position, the Company requested that the maximum amount the Company could borrow under this facility be reduced to \$1.25 billion from \$2.0 billion; in addition, the debt to total capitalization ratio has been increased from 60 percent to 65 percent. The debt to total capitalization ratio and the minimum net worth covenant have also been amended to allow the add-back, if incurred, of up to the first \$500 million of certain non-cash charges, including goodwill and other intangible asset impairment charges that would negatively impact shareholders equity. Under the terms of the Amended Credit Facility, any outstanding Letters of Credit reduce the Company's borrowing capacity. At September 30, 2009, the Company had \$72 million of unused Letters of Credit; accordingly, the Company's remaining borrowing capacity is approximately \$1.2 billion. The Company incurred approximately \$2 million of fees and expenses associated with the Amendment. The Company, if the facility is utilized, will incur higher borrowing costs as a result of the Amendment.

At September 30, 2009, the Company was in compliance with the requirements of the Amended Five-Year Revolving Credit Facility.

- J. On January 1, 2008, the Company adopted FASB guidance that defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements for its financial assets and liabilities. On January 1, 2009, the Company adopted this guidance for its non-financial assets and liabilities; such adoption did not have a significant effect on its condensed consolidated financial statements. The FASB guidance defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Further, it defines a fair value hierarchy, as follows: Level 1 inputs as quoted prices in active markets for identical assets or liabilities; Level 2 inputs as observable inputs other than Level 1 prices, such as quoted market prices for similar assets or liabilities or other inputs that are observable or can be corroborated by market data; and Level 3 inputs as unobservable inputs that are supported by little or no market activity and that are financial instruments whose value is determined using pricing models or instruments for which the determination of fair value requires significant management judgment or estimation.

MASCO CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)

Note J continued:

Financial investments that are available to be traded on readily accessible stock exchanges (domestic or foreign) are considered to have active markets and have been valued using Level 1 inputs. Financial investments that are not available to be traded on a public market or have limited secondary markets, or contain provisions that limit the ability to sell the investment are considered to have inactive markets and have been valued using Level 2 or 3 inputs. The Company incorporated credit risk into the valuations of financial investments by estimating the likelihood of non-performance by the counterparty to the applicable transactions. The estimate included the length of time relative to the contract, financial condition of the counterparty and current market conditions. The criteria for estimating if a market was active or inactive were based on the individual facts and circumstances.

MASCO CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)

Note J continued:

Financial assets and (liabilities) measured at fair value on a recurring basis at each reporting period and the amounts for each level within the fair value hierarchy were as follows, in millions:

	Sep. 30, 2009	Fair Value Measurements Using		
		Quoted Market Prices (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Asahi Tec Corporation:				
Preferred stock	\$ 73	\$	\$	\$ 73
Common stock	1	1		
Foreign currency exchange contracts (A)	(1)		(1)	
Auction rate securities	22			22
TriMas Corporation	13	13		
Total	\$ 108	\$ 14	\$ (1)	\$ 95

	Dec. 31, 2008	Fair Value Measurements Using		
		Quoted Market Prices (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Asahi Tec Corporation:				
Preferred stock	\$ 72	\$	\$	\$ 72
Common stock	1	1		
Foreign currency exchange contracts (A)	(14)		(14)	
Auction rate securities	22			22
Marketable securities	3	3		
TriMas Corporation	3	3		
Other investments	3		3	
Total	\$ 90	\$ 7	\$ (11)	\$ 94

(A) The foreign currency exchange contracts include

contracts entered into to hedge currency fluctuations related to intercompany loans denominated in non-functional currencies and to manage exposure to currency fluctuations in the European euro and U.S. dollar. The loss on the foreign currency exchange contracts is more than offset by gains related to the translation of loans and accounts denominated in non-functional currencies.

MASCO CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)

Note J continued:

The following table summarizes the changes in Level 3 financial assets measured at fair value on a recurring basis for the nine months ended September 30, 2009 and the year ended December 31, 2008, in millions:

	Asahi Tec Preferred Stock	Auction Rate Securities	Total
Fair value January 1, 2009	\$ 72	\$ 22	\$ 94
Total losses included in earnings			
Unrealized (losses)	1		1
Purchases, issuances, settlements			
Fair value at September 30, 2009	\$ 73	\$ 22	\$ 95

	Asahi Tec Preferred Stock	Auction Rate Securities	Total
Fair value January 1, 2008	\$ 55	\$ 22	\$ 77
Total losses included in earnings			
Unrealized gains	17		17
Purchases, issuances, settlements			
Fair value at December 31, 2008	\$ 72	\$ 22	\$ 94

The preferred stock of Asahi Tec has been valued primarily using a discounted cash flow model, because there are currently no observable prices in an active market for the same or similar securities. The significant inputs in the discounted cash flow model used to value the Asahi Tec preferred stock include: the present value of future dividends, present value of redemption rights, fair value of conversion rights and the discount rate based on credit spreads for Japanese-issued preferred securities and other market factors.

The fair values of the auction rate securities held by the Company have been estimated using a discounted cash flow model (Level 3 input). The significant inputs in the discounted cash flow model used to value the auction rate securities include: expected maturity of auction rate securities, discount rate used to determine the present value of expected cash flows and assumptions for credit defaults, since the auction rate securities are backed by credit default swap agreements.

The Company also has investments in private equity funds and other private investments which are carried at cost and are evaluated for potential impairment when impairment indicators are present, or when an event or change in circumstances has occurred, that may have a significant adverse effect on the fair value of the investment. There is no active trading market for these investments and they are for the most part illiquid. Due to the significant unobservable inputs, the fair value measurements used to evaluate impairment are a Level 3 input.

MASCO CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)

Note J concluded:

Financial investments measured at fair value on a non-recurring basis during the period and the amounts for each level within the fair value hierarchy were as follows, in millions:

	Sep. 30,	Fair Value Measurements Using Significant			Total Gains (Losses)
		Quoted Market Prices (Level 1)	Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Private equity funds	2009 \$31	\$	\$	\$ 31	\$(10)

	Dec. 31,	Fair Value Measurements Using Significant			Total Gains (Losses)
		Quoted Market Prices (Level 1)	Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Private equity funds	2008 \$ 43	\$	\$	\$ 43	\$ (23)
Other private investments	4			4	(3)
	\$ 47	\$	\$	\$ 47	\$ (26)

During 2009, the Company determined that the decline in the estimated value of several private equity fund investments was other-than-temporary and, accordingly, recognized non-cash, pre-tax impairment charges of \$10 million for the nine months ended September 30, 2009. During 2008, the Company determined that the decline in the estimated value of several private equity funds was other-than-temporary and, accordingly, recognized non-cash, pre-tax impairment charges of \$23 million for the year ended December 31, 2008.

The fair value of the Company's short-term and long-term fixed-rate debt instruments is based principally upon quoted market prices for the same or similar issues or the current rates available to the Company for debt with similar terms and remaining maturities. The aggregate estimated market value of short-term and long-term debt at September 30, 2009 was approximately \$3.7 billion, compared with the aggregate carrying value of \$4.0 billion. The aggregate estimated market value of short-term and long-term debt at December 31, 2008 was approximately \$3.0 billion, compared with the aggregate carrying value of \$3.9 billion.

MASCO CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)

K. Effective January 1, 2009, the Company adopted new FASB guidance regarding noncontrolling interests in consolidated financial statements. At September 30, 2009 and December 31, 2008, the Company owns 68 percent of Hansgrohe AG. The new FASB guidance requires the reclassification of the Company's noncontrolling interest in Hansgrohe AG to shareholders' equity from deferred income taxes and other. At December 31, 2008, the Company did not have a balance in paid-in capital due to repurchases of Company common stock. The Company's activity in shareholders' equity was as follows, in millions:

	Total	Common Shares	Paid-in- Capital	Retained Earnings	Accumulated Other Comprehensive Income	Noncontrolling Interest
Balance, January 1, 2008	\$ 4,142	\$ 359	\$	\$ 2,969	\$ 661	\$ 153
Net (loss) income	(352)			(391)		39
Cumulative translation adjustments	(221)				(210)	(11)
Unrealized gain on marketable securities, net of income tax of \$4	7				7	
Prior service cost and net loss, net of income tax benefit of \$86	(150)				(150)	
Total comprehensive (loss) income	(716)					
Shares issued	1	1				
Shares retired:						
Repurchased	(160)	(9)	(71)	(80)		
Surrendered (non-cash)	(7)		(7)			
Cash dividends declared	(357)			(336)		(21)
Stock-based compensation	78		78			
Balance, December 31, 2008	\$ 2,981	\$ 351	\$	\$ 2,162	\$ 308	\$ 160
Net income	29			2		27
Cumulative translation adjustments	40				30	10
Unrealized gain on marketable securities, net of income tax of \$11	21				21	
Prior service cost and net loss, net of income tax of \$36	62				62	
Total comprehensive income	152					

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Shares issued		2	(2)			
Shares retired:						
Repurchased	(11)	(2)	(9)			
Surrendered (non-cash)	(5)	(1)	(4)			
Cash dividends declared	(81)			(81)		
Dividend payments to noncontrolling interest	(16)					(16)
Stock-based compensation	49		49			
Balance, September 30, 2009	\$ 3,069	\$ 350	\$ 34	\$ 2,083	\$ 421	\$ 181

Noncontrolling interest includes accumulated other comprehensive income of \$35 million, \$25 million and \$36 million at September 30, 2009, and December 31, 2008 and January 1, 2008, respectively.

MASCO CORPORATION**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)**

Note K concluded:

The Company's total comprehensive income was as follows, in millions:

	Three Months Ended September 30, 2009	
	Attributable to Masco Corporation	Noncontrolling Interest
Net income	\$ 28	\$ 12
Other comprehensive income:		
Cumulative translation adjustments	18	6
Unrealized gain on marketable securities, net	16	
Prior service cost and net loss, net		
Total comprehensive income	\$ 62	\$ 18

	Three Months Ended September 30, 2008		Nine Months Ended September 30, 2008	
	Attributable to Masco Corporation	Noncontrolling Interest	Attributable to Masco Corporation	Noncontrolling Interest
Net income	\$ 33	\$ 11	\$ 117	\$ 35
Other comprehensive (loss) income:				
Cumulative translation adjustments	(143)	(15)	(46)	(1)
Unrealized gain on marketable securities, net	2		10	
Prior service cost and net loss, net			2	
Total comprehensive (loss) income	\$ (108)	\$ (4)	\$ 83	\$ 34

The unrealized gain on marketable securities, net, is net of income tax of \$8 million for the three months ended September 30, 2009, and \$1 million and \$6 million, respectively, for the three months and nine months ended September 30, 2008. The prior service cost and net loss, net, is net of income tax of \$1 million for the nine months ended September 30, 2008.

In the first quarter of 2009, the Company announced the reduction of its quarterly dividend to \$.075 per common share from \$.235 per common share. On the basis of amounts paid (declared), cash dividends per common share were \$.075 (\$.075) and \$.385 (\$.225) for the three months and nine months ended September 30, 2009, respectively. On the basis of amounts paid (declared), cash dividends per common share were \$.23 (\$.235) and \$.69 (\$.695) for the three months and nine months ended September 30, 2008, respectively.

MASCO CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)

L. Information about the Company by segment and geographic area was as follows, in millions:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2009	2008	2009	2008	2009	2008	2009	2008
	Net Sales(A)		Operating Profit (Loss)		Net Sales(A)		Operating Profit (Loss)	
The Company's operations by segment were:								
Cabinets and Related Products	\$ 434	\$ 584	\$ (16)	\$ 23	\$ 1,248	\$ 1,788	\$ (56)	\$ 88
Plumbing Products	688	788	93	92	1,922	2,422	201	299
Installation and Other Services	332	492	(34)	10	961	1,486	(104)	8
Decorative Architectural Products	474	446	122	94	1,365	1,301	313	257
Other Specialty Products	166	201	16	16	427	563	16	37
Total	\$ 2,094	\$ 2,511	\$ 181	\$ 235	\$ 5,923	\$ 7,560	\$ 370	\$ 689
The Company's operations by geographic area were:								
North America	\$ 1,630	\$ 1,975	\$ 123	\$ 193	\$ 4,694	\$ 5,935	\$ 261	\$ 542
International, principally Europe	464	536	58	42	1,229	1,625	109	147
Total	\$ 2,094	\$ 2,511	181	235	\$ 5,923	\$ 7,560	370	689
General corporate expense, net			(36)	(32)			(96)	(110)
Charge for litigation settlement (B)			(7)	(9)			(7)	(9)
Charge for defined-benefit plan curtailment (C)							(8)	
Accelerated stock compensation expense (D)							(6)	
(Loss) on corporate fixed assets, net							(2)	

Operating profit	138	194	251	570
Other income (expense), net	(49)	(56)	(157)	(196)
Income from continuing operations before income taxes	\$ 89	\$ 138	\$ 94	\$ 374

- (A) Inter-segment sales were not material.
- (B) The charge for litigation settlement in 2009 relates to a business unit in the Cabinets and Related Products segment. The charge for litigation settlement in 2008 relates to a business unit in the Installation and Other Services segment.
- (C) In March 2009, the Company recognized a curtailment loss related to the plan to freeze all future benefit accruals beginning January 1, 2010 under substantially all of the Company's domestic qualified and non-qualified defined-benefit

pension plans.

- (D) See Note C to the condensed consolidated financial statements.

MASCO CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)

M. Other, net, which is included in other income (expense), net, was as follows, in millions:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2009	2008	2009	2008
Income from cash and cash investments	\$ 2	\$ 6	\$ 6	\$ 17
Other interest income	1	1	1	1
Income from financial investments, net (Note G)				
Other items, net	4	(3)	15	(12)
Total	\$ 7	\$ 4	\$ 22	\$ 6

Other items, net, included \$5 million and \$14 million of currency gains for the three months and nine months ended September 30, 2009, respectively. Other items, net, included \$3 million and \$18 million of currency losses for the three months and nine months ended September 30, 2008, respectively.

N. Reconciliations of the numerators and denominators used in the computations of basic and diluted earnings per common share were as follows, in millions:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2009	2008	2009	2008
Numerator (basic and diluted):				
Income from continuing operations	\$ 51	\$ 35	\$ 32	\$ 132
Allocation to unvested restricted stock awards	(1)	(2)	(2)	(6)
Income from continuing operations attributable to common shareholders	50	33	30	126
(Loss) from discontinued operations, net	(23)	(2)	(30)	(15)
Net income available to common shareholders	\$ 27	\$ 31	\$	\$ 111
Denominator:				
Basic common shares (based upon weighted average)	350	352	351	354
Add:				
Contingent common shares				
Stock option dilution	1			
Diluted common shares	351	352	351	354

MASCO CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)

Note N concluded:

Effective January 1, 2009, the Company adopted FASB guidance regarding determining whether instruments granted in share-based payment transactions are participating securities. This new FASB guidance clarifies that share-based payment awards that entitle their holders to receive non-forfeitable dividends prior to vesting should be considered participating securities. The Company has granted restricted stock awards that contain non-forfeitable rights to dividends on unvested shares; such unvested restricted stock awards are considered participating securities. As participating securities, the unvested shares are required to be included in the calculation of the Company's basic earnings per common share, using the two-class method. The two-class method of computing earnings per common share is an allocation method that calculates earnings per share for each class of common stock and participating security according to dividends declared and participation rights in undistributed earnings. Unvested restricted stock awards were previously included in the Company's diluted share calculation using the treasury stock method. For the three months and nine months ended September 30, 2009 and 2008, the Company allocated dividends and income to the unvested restricted stock awards (participating securities).

At September 30, 2009 and 2008, the Company did not include any common shares related to the Zero Coupon Convertible Senior Notes (Notes) in the calculation of diluted earnings per common share, as the price of the Company's common stock at September 30, 2009 and 2008 did not exceed the equivalent accreted value of the Notes.

Additionally, 35 million and 36 million common shares for the three months and nine months ended September 30, 2009, respectively, and 32 million common shares for both the three months and nine months ended September 30, 2008 related to stock options were excluded from the computation of diluted earnings per common share due to their antidilutive effect.

In the first nine months of 2009, the Company granted two million shares of long-term stock awards. In the first nine months of 2009, the Company also repurchased and retired approximately two million shares of Company common stock, for cash aggregating \$11 million to offset the dilutive impact of these long-term stock awards. At September 30, 2009, the Company had 30 million shares of its common stock remaining under the July 2007 Board of Directors repurchase authorization.

MASCO CORPORATION**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (continued)**

- O. The Company is subject to lawsuits and pending or asserted claims with respect to matters generally arising in the ordinary course of business.

As previously disclosed, a lawsuit has been brought against the Company and a number of its insulation installation companies in the federal court in Atlanta, Georgia alleging that certain practices violate provisions of the federal antitrust laws. In February 2009, the federal court in Atlanta certified a class of 377 insulation contractors. Two additional lawsuits, seeking class action status and alleging anticompetitive conduct, were filed against the Company and a number of its insulation suppliers. One of these lawsuits was filed in a Florida state court and has been dismissed by the court with prejudice. The other lawsuit was filed in federal court in northern California and was subsequently transferred to federal court in Atlanta, Georgia. The Company is vigorously defending the pending cases. Based upon the advice of its outside counsel, the Company believes that the conduct of the Company and its insulation installation companies, which has been the subject of the above-described lawsuits, has not violated any antitrust laws. The Company is unable at this time to reliably estimate any potential liability which might occur from an adverse judgment. There cannot be any assurance that the Company will ultimately prevail in the remaining lawsuits, or, if unsuccessful, that the ultimate liability would not be material and would not have a material adverse effect on its businesses or the methods used by its insulation installation companies in doing business.

As previously disclosed, European governmental authorities are investigating possible anticompetitive business practices relating to the plumbing and heating industries in Europe. The investigations involve a number of European companies, including certain of the Company's European manufacturing divisions and a number of other large businesses. The Company believes that it will not incur material liability as a result of the matters that are subject to these investigations.

- P. Changes in the Company's warranty liability were as follows, in millions:

	Nine Months Ended September 30, 2009	Twelve Months Ended December 31, 2008
Balance at January 1	\$ 119	\$ 133
Accruals for warranties issued during the period	23	42
Accruals related to pre-existing warranties	4	6
Settlements made (in cash or kind) during the period	(32)	(53)
Other, net	(4)	(9)
Balance at end of period	\$ 110	\$ 119

- Q. Because the Company's projected pre-tax income is near break-even, small changes in projected pre-tax income may cause large changes in the estimated annual effective tax rate thereby producing potentially unreliable estimates of tax expense. Since these small changes to pre-tax income are likely to occur, the Company recorded the tax expense for the first nine months of 2009 using the actual effective tax rate on the year-to-date pre-tax income and did not use the estimated annual effective tax rate.

MASCO CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited) (concluded)

Note Q concluded:

During the first nine months of 2009, the Company's liability for unrecognized tax benefits and accrued interest and penalties decreased by \$12 million and \$3 million, respectively, due primarily to a settlement with a tax authority on various unrecognized tax benefits. As a result of tax audit closings, settlements and expiration of applicable statutes of limitations in various jurisdictions within the next 12 months, the Company anticipates that it is reasonably possible that the liability for unrecognized tax benefits could be reduced by approximately \$8 million.

MASCO CORPORATION**Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS****THIRD QUARTER 2009 AND THE FIRST NINE MONTHS 2009 VERSUS
THIRD QUARTER 2008 AND THE FIRST NINE MONTHS 2008****SALES AND OPERATIONS**

The following table sets forth the Company's net sales and operating profit margins by business segment and geographic area, dollars in millions:

	Three Months Ended		Percent (Decrease) Increase 2009 vs. 2008
	September 30, 2009	2008	
Net Sales:			
Cabinets and Related Products	\$ 434	\$ 584	(26%)
Plumbing Products	688	788	(13%)
Installation and Other Services	332	492	(33%)
Decorative Architectural Products	474	446	6%
Other Specialty Products	166	201	(17%)
Total	\$ 2,094	\$ 2,511	(17%)
North America	\$ 1,630	\$ 1,975	(17%)
International, principally Europe	464	536	(13%)
Total	\$ 2,094	\$ 2,511	(17%)
	Nine Months Ended		
	September 30, 2009	2008	
Net Sales:			
Cabinets and Related Products	\$ 1,248	\$ 1,788	(30%)
Plumbing Products	1,922	2,422	(21%)
Installation and Other Services	961	1,486	(35%)
Decorative Architectural Products	1,365	1,301	5%
Other Specialty Products	427	563	(24%)
Total	\$ 5,923	\$ 7,560	(22%)
North America	\$ 4,694	\$ 5,935	(21%)
International, principally Europe	1,229	1,625	(24%)
Total	\$ 5,923	\$ 7,560	(22%)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
Operating Profit (Loss) Margins: (A)				
Cabinets and Related Products	(3.7%)	3.9%	(4.5%)	4.9%
Plumbing Products	13.5%	11.7%	10.5%	12.3%
Installation and Other Services	(10.2%)	2.0%	(10.8%)	.5%
Decorative Architectural Products	25.7%	21.1%	22.9%	19.8%
Other Specialty Products	9.6%	8.0%	3.7%	6.6%
North America	7.5%	9.8%	5.6%	9.1%
International, principally Europe	12.5%	7.8%	8.9%	9.0%
Total	8.6%	9.4%	6.2%	9.1%
Total operating profit margin, as reported	6.6%	7.7%	4.2%	7.5%

(A) Before general corporate expense, net, the accelerated stock compensation expense, the charge for the defined-benefit plan curtailment, the (loss) on corporate fixed assets, net, and the charge for litigation settlement; see Note L to the condensed consolidated financial statements.

MASCO CORPORATION**Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The Company reports its financial results in accordance with generally accepted accounting principles (GAAP) in the United States. However, the Company believes that certain non-GAAP performance measures and ratios, used in managing the business, may provide users of this financial information with additional meaningful comparisons between current results and results in prior periods. Non-GAAP performance measures and ratios should be viewed in addition to, and not as an alternative for, the Company's reported results.

NET SALES

Net sales decreased for both the three-month and nine-month periods ended September 30, 2009 from the comparable periods of 2008. Excluding results from acquisitions and the effect of currency translation, net sales decreased 15 percent and 19 percent, respectively, for the three-month and nine-month periods ended September 30, 2009. The following table reconciles reported net sales to net sales, excluding acquisitions and the effect of currency translation, in millions:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
Net sales, as reported	\$ 2,094	\$ 2,511	\$ 5,923	\$ 7,560
Acquisitions			(9)	
Net sales, excluding acquisitions	2,094	2,511	5,914	7,560
Currency translation	38		199	
Net sales, excluding acquisitions and the effect of currency translation	\$ 2,132	\$ 2,511	\$ 6,113	\$ 7,560

Net sales from North American operations decreased in 2009, primarily due to the decline in the new home construction market, which reduced sales by 11 percent and 13 percent, respectively, in the three-month and nine-month periods ended September 30, 2009 compared to the same periods of 2008 and a decline in consumer spending for home improvement products, which reduced sales by seven percent and ten percent, respectively, in the three-month and nine-month periods ended September 30, 2009 compared to the same periods of 2008. North American net sales for both the three-month and nine-month periods ended September 30, 2009 were negatively affected by lower sales volume of installation and other services, plumbing products, cabinets and windows. Such sales declines were partially offset by increased sales of paints and stains and increased selling prices for certain products in both periods.

In local currencies, net sales from International operations decreased seven percent and 13 percent, respectively, in the three-month and nine-month periods ended September 30, 2009, primarily due to lower sales volume of International plumbing products and cabinets, partially offset by selling price increases. Net sales from International operations decreased in 2009, due to a stronger U.S. dollar, which decreased International net sales by six percent and 11 percent in the three-month and nine-month periods ended September 30, 2009, respectively, compared to the same periods of 2008.

MASCO CORPORATION

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Net sales of Cabinets and Related Products decreased in 2009, due to lower sales volume of cabinets in the new home construction and retail markets, as well as a less favorable product mix, which, combined, reduced sales in this segment by 22 percent and 26 percent, respectively, in the three-month and nine-month periods ended September 30, 2009 compared to the same periods of 2008. A stronger U.S. dollar decreased sales by two percent and three percent, respectively, in the three-month and nine-month periods ended September 30, 2009 compared to the same periods of 2008. In local currencies, net sales of International operations reduced sales in this segment by three percent and four percent, respectively, in the three-month and nine-month periods ended September 30, 2009 compared to the same periods of 2008. Segment sales declines were partially offset by selling price increases.

Net sales of Plumbing Products decreased in 2009, due to lower sales volume to North American retailers and wholesalers, which reduced sales by nine percent and 12 percent, respectively, in the three-month and nine-month periods ended September 30, 2009 compared to the same periods of 2008. A stronger U.S. dollar decreased sales by three percent and five percent, respectively, in the three-month and nine-month periods ended September 30, 2009 compared to the same periods of 2008. In local currencies, net sales of International operations reduced sales in this segment by three percent and seven percent, respectively, in the three-month and nine-month periods ended September 30, 2009 compared to the same periods of 2008. Segment sales declines were partially offset by selling price increases.

Net sales of Installation and Other Services decreased for both the three-month and nine-month periods ended September 30, 2009, primarily due to significantly lower sales volume related to the slowdown in the new home construction market, as well as selling price decreases.

Net sales of Decorative Architectural Products increased for both the three-month and nine-month periods ended September 30, 2009, primarily due to increased retail sales volume of paints and stains, which offset lower retail sales volume of builders' hardware. Sales of paints and stains benefited from new product introductions and advertising and promotional activities. The nine-month period ended September 30, 2009 also benefited from late 2008 selling price increases related to paints and stains.

Net sales of Other Specialty Products decreased in 2009, primarily due to lower sales volume of windows in the western United States, and selling price decreases which, on a combined basis, decreased sales in this segment by nine percent and 14 percent, respectively, in the three-month and nine-month periods ended September 30, 2009 compared to the same periods of 2008. Net sales in this segment also decreased due to a decline in retail sales of staple gun tackers and other fastening tools by four percent and three percent, respectively, in the three-month and nine-month periods ended September 30, 2009, compared to the same periods in 2008. A stronger U.S. dollar decreased sales by three percent and five percent, respectively, in the three-month and nine-month periods ended September 30, 2009 compared to the same periods of 2008. Sales in this segment were also negatively affected by a less favorable product mix.

MASCO CORPORATION

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

OPERATING MARGINS

The Company's gross profit margins were 27.2 percent and 25.8 percent, respectively, for the three-month and nine-month periods ended September 30, 2009 compared with 25.8 percent and 26.0 percent for the comparable periods of 2008. Selling, general and administrative expenses declined to \$432 million and \$1,272 million, respectively, for the three-month and nine-month periods ended September 30, 2009 from \$454 million and \$1,398 million, respectively, in the comparable periods of 2008; however, as a percentage of sales, such expenses were 20.6 percent and 21.5 percent, respectively, for the three-month and nine-month periods ended September 30, 2009 compared with 18.1 percent and 18.5 percent for the comparable periods of 2008, reflecting lower sales volume, as well as increased plant closure and system implementation costs. Results benefited from the improved relationship between selling prices and commodity costs, as well as the benefits associated with business rationalizations and other cost savings initiatives.

The Company has been focused on the strategic rationalization of its businesses, including business consolidations, plant closures, headcount reductions, system implementations and other initiatives. Operating profit for the three-month and nine-month periods ended September 30, 2009 includes \$21 million and \$67 million, respectively, of costs and charges related to the Company's business rationalizations and other initiatives. For the three-month and nine-month periods ended September 30, 2008, the Company incurred \$15 million and \$39 million, respectively, related to these initiatives. During the first nine months of 2009, the Company closed or sold three manufacturing facilities and reduced headcount by 4,000 employees. Based on current plans, the Company anticipates costs and charges related to the Company's business rationalizations and other initiatives to approximate \$92 million in 2009. The Company continues to evaluate its businesses and may implement additional rationalization programs based on changes in the Company's markets which could result in further costs and charges.

The operating loss in the Cabinets and Related Products segment in 2009 reflects lower sales volume in the new home construction and retail markets and the related under-absorption of fixed costs, as well as a less favorable product mix, which on a combined basis reduced operating margins by approximately ten percentage points and eight percentage points, respectively, for the three-month and nine-month periods ended September 30, 2009 compared to 2008. This segment was also negatively affected by the lower results of International operations, as well as increased severance and system implementation costs and costs to close or sell several plants in this segment. Such declines were partially offset by the improved relationship between selling prices and commodity costs as well as the benefits associated with business rationalizations and other cost savings initiatives.

The increase in operating profit margins in the Plumbing Products segment for the three-month period ended September 30, 2009 reflects a more favorable product mix, as well as the improved relationship between selling prices and commodity costs and the benefits associated with business rationalizations and other cost savings initiatives. The decrease in operating profit margins in the Plumbing Products segment for the nine-month period ended September 30, 2009 reflects lower sales volume and the related under-absorption of fixed costs, as well as a less favorable product mix of International plumbing products.

The operating loss in the Installation and Other Services segment for both the three-month and nine-month periods ended September 30, 2009 is primarily due to lower sales volume and the related under-absorption of fixed costs, as well as increased system implementation costs and selling price decreases.

MASCO CORPORATION

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The increase in operating profit margins for the Decorative Architectural Products segment for the three-month and nine-month period ended September 30, 2009 is primarily due to increased sales volume of paints and stains, which more than offset lower sales volume of builders' hardware. The operating profit margins also benefited from the improved relationship between selling prices and commodity costs related to paints and stains and builders' hardware, as well as lower promotional activities related to builders' hardware.

The increase in operating profit margins in the Other Specialty Products segment for the three-month period ended September 30, 2009 reflects the increased benefits associated with business rationalizations and other cost savings initiatives. The decrease in operating profit margins for the Other Specialty Products segment for the nine-month period ended September 30, 2009 reflects lower sales volume of windows and staple gun tackers and other fastening tools and the related under-absorption of fixed costs, as well as a less favorable product mix, partially offset by the benefits associated with business rationalizations and other cost savings initiatives.

OTHER INCOME (EXPENSE), NET

Other items, net, for the three-month and nine-month periods ended September 30, 2009 included \$5 million and \$14 million, respectively, of currency gains.

For the nine-month period ended September 30, 2009, the Company recognized non-cash, pre-tax impairment charges of \$10 million related to financial investments in private equity funds.

Other, net, for the nine-month period ended September 30, 2008 included \$3 million of realized losses, net, from the sale of marketable securities and \$3 million of income from other investments, net. Other items, net, for the three-month and nine-month periods ended September 30, 2008 included \$3 million and \$18 million, respectively, of currency losses.

For the three-month and nine-month periods ended September 30, 2008, the Company recognized non-cash, pre-tax impairment charges of \$1 million and \$30 million, respectively, related to financial investments in private equity funds and marketable securities.

Interest expense decreased \$3 million for both the three-month and nine-month periods ended September 30, 2009 from the comparable periods of 2008 to \$56 million and \$169 million, respectively.

INCOME AND EARNINGS PER COMMON SHARE FROM CONTINUING OPERATIONS

Income from continuing operations (attributable to Masco Corporation) for the three-month and nine-month periods ended September 30, 2009 was \$51 million and \$32 million, respectively, compared with \$35 million and \$132 million, respectively, for the comparable periods of 2008. Diluted earnings per common share from continuing operations (attributable to Masco Corporation) for the three-month and nine-month periods ended September 30, 2009 were \$.14 per common share and \$.09 per common share, respectively, compared with \$.09 per common share and \$.36 per common share, respectively, for the comparable periods of 2008.

MASCO CORPORATION

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

For the three-month and nine-month periods ended September 30, 2009, the Company reported tax expense of \$26 million and \$35 million, respectively. A discrete calculation was used to report tax expense rather than an estimated annual tax rate, as the estimated range of the annual income for the Company in 2009 produces significant variability and makes it difficult to reasonably estimate the annual effective tax rate. While the Company expects full-year income (loss) from continuing operations to approximate break-even, the Company expects to have tax expense for the year primarily due to income tax liabilities in certain jurisdictions and losses in other jurisdictions that provide no tax benefit. The Company's effective tax rate was 67 percent and 55 percent, respectively, for the three-month and nine-month periods ended September 30, 2008.

OTHER FINANCIAL INFORMATION

The Company's current ratio was 1.9 to 1 and 2.1 to 1, respectively, at September 30, 2009 and December 31, 2008.

For the nine months ended September 30, 2009, cash of \$415 million was provided by operating activities. Net cash used for financing activities was \$174 million, and included \$139 million for the payment of cash dividends and \$11 million for the acquisition of Company common stock in open-market transactions to offset the dilutive impact of long-term stock awards granted in 2009. Net cash used for investing activities was \$74 million and included \$70 million for capital expenditures.

The Company's cash and cash investments increased to \$1.2 billion at September 30, 2009 from \$1.0 billion at December 31, 2008. The Company's cash and cash investments consist of overnight interest bearing money market demand and time deposit accounts, money market mutual funds and government securities. While the Company attempts to diversify these investments in a prudent manner to minimize risk, it is possible that future changes in the financial markets could result in failures of additional financial institutions or other events and thereby affect the security or availability of these investments.

At September 30, 2009, the Amended Five-Year Revolving Credit Agreement contains limitations on additional borrowings. Under the terms of the Amended Credit Facility, any outstanding Letters of Credit reduce the Company's borrowing capacity. At September 30, 2009, the Company had \$72 million of unused Letters of Credit; accordingly, the Company's remaining borrowing capacity is approximately \$1.2 billion. At September 30, 2009, the Amended Five-Year Revolving Credit Agreement also contains a requirement for maintaining a certain level of net worth; the Company's net worth exceeded such requirement by \$1.1 billion.

During 2009, the Company announced the reduction of its quarterly dividend to \$.075 per common share from \$.235 per common share.

The Company is subject to lawsuits and claims pending or asserted with respect to matters generally arising in the ordinary course of business. Note O to the condensed consolidated financial statements discusses certain specific claims pending against the Company.

MASCO CORPORATION

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The Company believes that its present cash balance, cash flows from operations and, to the extent necessary, bank borrowings and future financial market activities, are sufficient to fund its working capital and other investment needs.

OUTLOOK FOR THE COMPANY

Business conditions remain difficult in the Company's markets. The Company continues to estimate that 2009 housing starts will decline 40 percent to approximately 550,000 units. The Company also anticipates that consumer spending for home improvement products in North American and International markets will continue at depressed levels in the near term.

Although the Company is confident that the long-term fundamentals for the new home construction and home improvement markets are positive, the Company expects that market conditions will be challenging over the near-term as global economies recover.

The Company believes that its strong financial position (including cash of \$1.2 billion at September 30, 2009, its ability to generate positive cash flow during 2009 and unused bank lines) together with its current strategy of re-aligning its cost structure, investing in leadership brands, driving innovation and re-engineering its supply chains, will allow it to drive long-term growth and create value for its shareholders.

FORWARD-LOOKING STATEMENTS

Certain sections of this Quarterly Report contain statements reflecting the Company's views about its future performance which may constitute forward-looking statements under the Private Securities Litigation Reform Act of 1995. These views involve risks and uncertainties that are difficult to predict and the Company's results may differ materially from the results discussed in such forward-looking statements. For further information, readers should refer to the Company's most recent Annual Report on Form 10-K (Risk Factors and Management's Discussion and Analysis of Financial Condition and Results of Operations sections) and to any subsequent Quarterly Reports on Form 10-Q, all of which are on file with the Securities and Exchange Commission. The Company undertakes no obligation to update publicly any forward-looking statements as a result of new information, future events or otherwise.

MASCO CORPORATION

Item 4. CONTROLS AND PROCEDURES

a. Evaluation of Disclosure Controls and Procedures.

The Company's principal executive officer and principal financial officer have concluded, based on an evaluation of the Company's disclosure controls and procedures (as defined in the Securities Exchange Act of 1934 Rules 13a-15(e) or 15d-15(e)), as required by paragraph (b) of Exchange Act Rules 13a-15 or 15d-15, that, as of September 30, 2009, the Company's disclosure controls and procedures were effective.

b. Changes in Internal Control Over Financial Reporting.

In connection with the evaluation of the Company's internal control over financial reporting that occurred during the quarter ended September 30, 2009, which is required under the Securities Exchange Act of 1934 by paragraph (d) of Exchange Rules 13a-15 or 15d-15, (as defined in paragraph (f) of Rule 13a-15), management determined that, except as noted below, there was no change that has materially affected or is reasonably likely to materially affect internal control over financial reporting.

During the third quarter of 2009, the Company continued a phased deployment of new Enterprise Resource Planning (ERP) systems at Masco Builder Cabinet Group and Masco Contractor Services, two of the Company's larger business units. These new systems represent process improvement initiatives and are not in response to any identified deficiency or weakness in the Company's internal control over financial reporting. However, these business process initiatives are significant in scale and complexity and will result in modifications to certain internal controls. These systems are designed, in part, to enhance the overall system of internal control over financial reporting through further automation and integration of various business processes.

MASCO CORPORATION
PART II. OTHER INFORMATION

Item 1. Legal Proceedings

Information regarding certain legal proceedings involving the Company is set forth in Note O to the Company's condensed consolidated financial statements included in Part I, Item 1 of this Quarterly Report.

Item 1A. Risk Factors

Information regarding risk factors of the Company is set forth in Item 1A, Risk Factors in the Company's Annual Report on Form 10-K for the year ended December 31, 2008.

Item 6. Exhibits

- | | |
|-----|---|
| 12 | Computation of Ratio of Earnings to Combined Fixed Charges and Preferred Stock Dividends |
| 31a | Certification by Chief Executive Officer Required by Rule 13a-14(a) or 15d-14(a) of the Securities Exchange Act of 1934 |
| 31b | Certification by Chief Financial Officer Required by Rule 13a-14(a) or 15d-14(a) of the Securities Exchange Act of 1934 |
| 32 | Certification Required by Rule 13a-14(b) or 15d-14(b) of the Securities Exchange Act of 1934 and Section 1350 of Chapter 63 of Title 18 of the United States Code |
| 101 | Interactive Data File |

MASCO CORPORATION
PART II. OTHER INFORMATION, concluded
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.

MASCO CORPORATION

By: /s/ John G. Sznewajs
Name:
John G. Sznewajs
Title: Vice President, Treasurer and Chief
Financial Officer

October 29, 2009

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**MASCO CORPORATION
EXHIBIT INDEX**

Exhibit

- Exhibit 12 Computation of Ratio of Earnings to Combined Fixed Charges and Preferred Stock Dividends
- Exhibit 31a Certification by Chief Executive Officer Required by Rule 13a-14(a) or 15d-14(a) of the Securities Exchange Act of 1934
- Exhibit 31b Certification by Chief Financial Officer Required by Rule 13a-14(a) or 15d-14(a) of the Securities Exchange Act of 1934
- Exhibit 32 Certification Required by Rule 13a-14(b) or 15d-14(b) of the Securities Exchange Act of 1934 and Section 1350 of Chapter 63 of Title 18 of the United States Code
- Exhibit 101 Interactive Data File