

AeroGrow International, Inc.
Form 10-K
July 01, 2013

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

FORM 10-K

ý ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended March 31, 2013
or
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to

(Commission File No.) 001-33531

AEROGROW INTERNATIONAL, INC.
(Exact name of registrant as specified in its charter)

Nevada
(State or other jurisdiction of
incorporation or organization)

46-0510685
(I.R.S. Employer
Identification No.)

6075 Longbow Drive, Suite 200
Boulder, Colorado 80301
(303) 444-7755

(Address, including zip code and telephone number, including area code, of registrant's of principal executive office)

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

None

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

Title of each class:

Name of each exchange on which registered:

Common Stock, par value \$0.001 per share

OTCQB

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

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Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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

Indicate by check mark 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of the Form 10-K or any amendment to the Form 10-K.

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

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

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

The aggregate market value of the voting common stock held by non-affiliates of the registrant as of September 30, 2012 was \$5,904,877, the last day of our most recent second quarter. For the purpose of the foregoing calculation only, all directors and executive officers of the registrant and owners of more than 5% of the registrant's common stock are assumed to be affiliates of the registrant. This determination of affiliate status is not necessarily conclusive for any other purpose.

The number of shares of the registrant's common stock outstanding as of June 21, 2013 is 5,904,877.

DOCUMENTS INCORPORATED BY REFERENCE

None

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Annual Report on Form 10-K
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This Annual Report on Form 10-K (“Annual Report”) for AeroGrow International, Inc. (“AeroGrow,” the “Company,” “we,” “our” or “us”), including the “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” contains forward-looking statements regarding future events and our future results that are based on current expectations, estimates, forecasts, and projections about the industry in which we operate and the beliefs and assumptions of our management. Words such as “expects,” “anticipates,” “targets,” “goals,” “projects,” “may,” “will,” “would,” “intends,” “plans,” “believes,” “seeks,” and “estimates,” as well as variations of such words and similar expressions, are intended to identify such forward-looking statements. These forward looking statements may include, among others, statements concerning our expectations regarding our business, growth prospects, revenue trends, operating costs, working capital requirements, access to funding, competition, results of operations and other statements of expectations, beliefs, future plans and strategies, anticipated events or trends, and similar expressions concerning matters that are not historical facts. These forward-looking statements are only predictions that are subject to risks, uncertainties, and assumptions that are difficult to predict. Therefore, actual results may differ materially and adversely from those expressed in any forward-looking statements. Factors that might cause or contribute to such differences include, but are not limited to, those discussed under the section entitled “Risk Factors” in Part I Item 1A of and elsewhere in this Report, and in other reports we file with the SEC, including the most recent quarterly reports on Form 10-Q and

current reports on Form 8-K. While forward-looking statements are based on reasonable expectations of our management at the time that they are made, you should not rely on them. We undertake no obligation to revise or update publicly any forward-looking statements for any reason.

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PART I

ITEM 1. BUSINESS

Our Business

AeroGrow is a developer, marketer, direct-seller, and wholesaler of advanced indoor garden systems designed for consumer use and priced to appeal to the gardening, cooking, healthy eating, and home and office décor markets. To date, we have launched multiple lines of proprietary indoor gardens, grow lights, a patented nutrient formula, and more than 30 corresponding proprietary seed kits, and various cooking, gardening and décor accessories, both nationally and internationally.

As of March 31, 2013, we have manufactured and shipped approximately 1.1 million AeroGarden® units and approximately 2.6 million seed kits to consumers and retailers worldwide. We commenced initial marketing and distribution of our products in March 2006, with an emphasis on retail distribution. In recent years, we shifted our sales and marketing efforts away from retail distribution, which generated lower margins and required much higher investments in inventory, in order to focus on higher margin “direct-to-consumer” sales channels. Our direct-to-consumer channels are principally comprised of our own in-house direct mail catalogue, e-mail marketing, and internet marketing. We have continued to sell to a limited number of retailers and international third-party distributors, and we expect to re-emphasize these sales channels in the future due to the improving economic conditions and an April 2013 strategic alliance with a subsidiary of The Scotts Miracle-Gro Company (“Scotts Miracle-Gro”). In addition to a working capital infusion of approximately \$4.5 million from Scotts Miracle-Gro, the strategic alliance affords AeroGrow the use of the globally recognized and highly trusted Miracle-Gro brand name. We believe that the strategic alliance also gives Scotts Miracle-Gro an entry into the burgeoning indoor gardening market, while providing AeroGrow a broad base of support in marketing, distribution, supply chain logistics, R&D, and sourcing.

Our principal products are indoor gardens and proprietary seed kits that allow consumers, with or without gardening experience, to grow: (i) vegetables, such as tomatoes, chili peppers and salad greens; (ii) fresh herbs, including cilantro, chives, basil, dill, oregano, and mint; and (iii) flowers, such as petunias, snapdragons, geraniums and vinca. Consumers can also plant and grow their own seeds using our proprietary “grow anything” kits, or use their AeroGardens as seed starters for their outdoor gardens with our “garden starter” systems.

Our indoor gardens are designed to be simple, consistently successful, and affordable. We believe that our products allow almost anyone, from consumers who have no gardening experience to professional gardeners, to produce year-round harvests of a variety of herbs, vegetables, and flowers, regardless of season, weather, or availability of natural light. We believe that our indoor gardening products’ unique and attractive designs make them appropriate for use in almost any location, including kitchens, living areas, and offices.

Our indoor gardening units are sold through different channels designed to match customer needs and interests with the appropriate garden unit features and benefits at list prices ranging from approximately \$90 to \$250, depending on size, design elements, light intensity and other automated features. As is customary in the direct-to-consumer channels, we frequently offer temporary discounts and targeted promotions that reduce the net price a consumer pays for our gardens, that are designed to generate higher sales volume.

Corporate History

AeroGrow International, Inc. (“AeroGrow”) was formed as a Nevada corporation on March 25, 2002. After more than three years of initial research and product development, we began sales activities in March 2006. Since that time, we

have expanded our operations and currently distribute our products through multiple sales channels. We have developed direct sales channels, including web sales and a direct mail catalogue business, with approximately 1.3 million catalogues mailed in our fiscal year ended March 31, 2013 (“Fiscal 2013”). In prior years, we have also utilized direct television sales, including infomercials and 60 and 120 second television commercials, mall kiosks, and print and radio advertisement to generate consumer sales. We also sell through approximately 72 retail storefronts in North America, and in seven countries internationally. We have expanded our product lines, and now offer four different indoor garden models, with each model available in different colors and trim styles, more than 40 seed kits, and various gardening and kitchen accessories.

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Hydroponics and Aeroponics Industry - Background

Hydroponics is the science of growing plants using nutrients suspended in water instead of soil. Used commercially worldwide, hydroponics is considered an advanced and often preferred crop production method. Hydroponics is typically used inside greenhouses to give growers the ability to better regulate and control nutrient delivery, light, air, water, humidity, pests, and temperature. Hydroponic growers benefit by producing crops faster and with higher crop yields per acre than traditional soil-based growers.

Aeroponic technology is derived from hydroponics and occurs when plant roots are suspended in an air chamber and bathed with a nutrient solution. We believe that the aeroponic technology used in our indoor gardening products is a technological advance over most hydroponic growing systems because plant roots are partially suspended in air and allowed direct access to oxygen, while being bathed in a highly oxygenated, nutrient rich solution. For these reasons, we believe the use of a well-designed and maintained aeroponic system can yield increases in growth rates and plant survival when compared to most hydroponic or soil-based systems.

Until the development of our indoor gardening products, certain barriers prevented hydroponic or aeroponic technology from being incorporated into mainstream, mass-marketed consumer products, including:

- Consumers generally lack the specialized knowledge required to select, set up, operate, and maintain the various components for a typical hydroponic or aeroponic system, including growing trays, irrigation channels, growing media, nutrient reservoirs, and nutrient delivery systems consisting of electronic timers, pumps, motors, tubing, and nozzles;
- In the absence of adequate natural light, consumers generally do not possess the specific knowledge required to select, set up, operate, and maintain the varied indoor lighting systems that are necessary to grow plants indoors;
- Consumers are often unable to properly mix and measure complex hydroponic nutrient formulas, which change depending on the plant variety and the stage of plant growth;
 - Consumers are unable to deal with the problem of nutrient spoilage; and
- Federally mandated water quality reports show that the water in many large cities is not suitable for hydroponic or aeroponic growing and requires treatments in order to sustain growth.

Our research leads us to believe that these complexities have been accepted in existing hydroponic market channels because these manufacturers have generally focused their product development and marketing efforts on satisfying the needs of the commercial greenhouse and dedicated hobbyist markets. These users are motivated to gain the specialized knowledge, equipment and experience currently required to successfully grow plants with these products. Our research also indicates that the hydroponic growing equipment currently available in these markets is bulky, expensive and comprised of many, often unintegrated, parts.

We believe that the complexities of currently available commercial hydroponic and aeroponic products fail to address the needs and wants of the mass consumer market, leaving that market unserved. We further believe that our patented and patent-pending inventions, companion technologies, and trade secrets have simplified and improved hydroponic and aeroponic technologies and have enabled us to create an indoor hydroponic and aeroponic gardening system appropriate for the mass consumer market.

Proprietary Technology and Intellectual Property

Since our inception in 2002, we have been innovating, simplifying, and integrating proprietary technologies and inventions into a family of “plug and grow” indoor gardening products and related seed kits specifically designed and priced for the mass consumer market. We have used this technology platform to develop four different models of indoor gardens, each with different features and technology groupings, with list prices ranging from approximately \$90 to \$250. Multiple patents applications have been filed in the United States and internationally to protect the inventions that are exclusively used in our indoor garden system and seed kits, and seven patents have been issued (four in the United States and three internationally). We have also obtained access to, both domestically and internationally, trademarks and certain domain name, including AeroGrow.com, AeroGarden.com, AeroGarden.net, AeroGarden.tv, AeroGarden.biz, and Getthegarden.com, among others.

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Our success and ability to compete are substantially dependent upon our exclusive access to technology and expertise. While we rely on patent, copyright, trade secret, and trademark law to protect the use of such technology, we also believe that factors such as the technological and creative skills of our personnel, new product developments, product enhancements, and reliable product maintenance are essential to establishing and maintaining a technology leadership position. There can be no assurance that others will not develop technologies that are similar or superior to our technology. Each of our employees, independent contractors, interns, and consultants has executed assignment of rights to intellectual property agreements and nondisclosure agreements. The assignment of application rights to intellectual property agreements grant us the right to own inventions and related patents which may be granted in the United States and throughout the world. The nondisclosure agreements generally provide that these people will not disclose our confidential information to any other person without our prior written consent.

April 2013 Strategic Alliance. In April 2013, we entered into a Securities Purchase Agreement and strategic alliance with a wholly owned subsidiary of Scotts Miracle-Gro. In conjunction with this transaction, we entered into several other agreements, including: (i) an Intellectual Property Sale Agreement; (ii) a Technology Licensing Agreement; (iii) a Brand License Agreement; and (iv) a Supply Chain Management Agreement. For further information on the strategic alliance with Scotts Miracle-Gro, please see Note 8 “Subsequent Events” to our financial statements.

Intellectual Property Sale Agreement. Pursuant to the Intellectual Property Agreement, we agreed to sell all intellectual property associated with our hydroponic products (the “Hydroponic IP”), other than the AeroGrow and AeroGarden trademarks, free and clear of all encumbrances, to Scotts Miracle-Gro for \$500,000. Scotts Miracle-Gro has the right to use the AeroGrow and AeroGarden trademarks in connection with the sale of products incorporating the Hydroponic IP.

Technology Licensing Agreement. Under the Technology Licensing Agreement, Scotts Miracle-Gro granted us an exclusive license to use the Hydroponic IP in North America and certain European Countries (collectively, the “AeroGrow Markets”) in return for a royalty of 2% of annual net sales, as determined at the end of each fiscal year. The initial term of the Technology Licensing Agreement is five years, and we may renew the Technology License for additional five-year terms by providing notice to Scotts Miracle-Gro at least six months in advance of the expiration of each five-year term.

Brand Licensing Agreement. Under the Brand Licensing Agreement, we may use certain of Scotts Miracle-Gro trade names, trademarks and/or service marks to rebrand the AeroGarden, and, with written consent of Scotts Miracle-Gro, other products in the AeroGrow Markets in exchange for our payment to Scotts Miracle-Gro of an amount equal to 5% of incremental growth in net sales, as compared to net sales during the fiscal year ended March 31, 2013. The initial term of the Brand Licensing Agreement is five years, and we may renew the Brand License for additional five-year terms by providing notice to Scotts Miracle-Gro at least six months in advance of the expiration of each five-year term.

Supply Chain Services Agreement. Under the Supply Chain Services Agreement, Scotts Miracle-Gro will pay AeroGrow an annual fee equal to 7% of the cost of goods of all products and services requested by Scotts Miracle-Gro during the term of the Technology Licensing Agreement (referenced above), thereby assisting AeroGrow in exploiting the Hydroponic IP internationally (outside of the AeroGrow Market).

Following is a description of the proprietary technologies, all of which were sold to Scott Miracle-Gro, and inventions that are exclusively used in our indoor garden system and seed kits.

Rainforest Nutrient Delivery System. The “rainforest” nutrient delivery system combines technologies with features from several hydroponic and aeroponic methodologies into a proprietary system that leaves plant roots suspended in an air gap. Plant roots take oxygen directly out of the air and, in testing of aeroponic systems by multiple different

sources, including lettuce studies by NASA Small Business Innovation Research, plants grow faster as a result.

Advanced Growing System. The Advanced Growing System (“AGS”) is available on several of our indoor gardens and combines features from the rainforest delivery system with technologies that deliver increased nutrient oxygenation, faster and healthier root growth, decreased consumer maintenance requirements, and increased product reliability. With AGS, plant roots are suspended in air in a 100% humid aeroponic chamber and then grow into a continuously oxygenated nutrient bath.

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Pre-Seeded Bio-Grow Seed Pods. The proprietary bio-grow seed pods include pre-implanted, specially selected seeds, a growing medium, removable bio-dome covers, and a grow basket.

Microprocessor-Based Control Panel and Nutrient Cycle Delivery System. The microprocessor-based controls include automated grow lights to ensure that plants receive the proper amount of lighting, and feature nutrient and water reminder systems that alert consumers to add water and nutrients when needed. In addition, some systems allow consumers to select from multiple plant types (for example, lettuce, herbs, tomatoes, or flowers) and the system then automatically adjusts the nutrient, water and lighting cycles to optimize growth. In addition, some systems take into account stage of growth of the specific plants when optimizing these factors. Our most recent ULTRA gardens include a display screen that walk consumers step-by-step through planting, tending and harvest, and allow for complete customization of all aspects of the grow cycle, including photo period, pump cycle and nutrient cycle.

Custom Nutrients and Automatic pH Adjustment. The patented nutrient solutions have been designed specifically to deliver the proper nutrients to plants, while offering consumers a user-friendly application methodology. Plant specific nutrients are included with each seed kit, and consumers simply add them when instructed by the microprocessor-based nutrient reminder. The pre-measured and mixed nutrients eliminate the need for mixing multi-part nutrient formulas and storing various nutrients in separate containers. A proprietary buffer has been formulated and included into the nutrients that automatically adjusts tap water from around the country to the right pH ranges for plant growth. Without this adjustment, tap water from many areas in the country will severely limit or inhibit plant growth in most aeroponic and hydroponic systems.

Integrated and Automated Lighting System. Hydroponic systems typically do not incorporate built-in lighting systems. Our indoor gardening products include built-in adjustable grow lights with ballast, reflector hood, grow bulbs and an electronic timer. The integrated lighting systems include proprietary high-output compact fluorescent light bulbs that deliver a spectrum and intensity of light designed to optimize plant growth without supplemental sunlight needed. In addition, the lighting system is fully automated and controlled by a microprocessor-based control panel described above. Variations in lighting are a differentiator in our product lines, and we have several gardens on the market with “50% more light and twice the height” of our initial gardens, allowing consumers to grow larger plants such as full-sized tomatoes in our indoor gardens, and deliver higher yields.

New Technologies in Development. We continue to develop improvements in lights, nutrients, oxygenation, seed variety selection, and style and design innovations, each of which are applied to our products on an ongoing basis.

Markets

Based on our sales experience to date and our existing channels of distribution, and supplemented by our own formal and informal market research consisting of individual consumer interviews, focus groups, blog monitoring, customer modeling, and Internet survey responses, we believe that our indoor gardening products appeal to a broad spectrum of consumers across multiple areas of interest. We believe that our products appeal to at least four major market segments:

Gardener Market. A recent study conducted by the National Gardening Association states that gardening is America’s number one hobby with more than 81 million households active in gardening. Based upon this survey, there were estimated to be 36 million households participating in food gardening and 13 million households participating in fresh herb gardening. We believe that our indoor gardening products and related products offer both expert and novice gardeners several major benefits not readily available through traditional gardening methods, including:

- the ability to grow fresh herbs, lettuces, vegetables, tomatoes, and flowers year-round, regardless of indoor light levels or seasonal weather conditions;

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- the ability to easily start plants indoors during colder months and then transplant them outdoors at the onset of the outdoor growing season;
- the ability to use stem cuttings to propagate multiple reproductions of the desired plants in our indoor gardening products; and
- the ease of growing in our indoor gardens, in contrast to the toil associated with traditional gardening, including preparing the soil, planting, thinning, weeding, watering, and removing pests.

“Want-to-be” Gardener Market. We believe that many people have an interest in gardening but lack the knowledge, confidence, available space, equipment, or time to garden. We have observed the following barriers that often prevent people from gardening:

- gardening requires an ongoing time commitment;
 - apartment, high-rise, and condominium dwellers often lack the land needed for a traditional garden;
- gardening requires physical work, which can be a significant barrier to people with limited mobility or health issues;
 - buying the necessary equipment to garden can be expensive; and
 - gardening requires knowledge and expertise.

We believe that our indoor gardening products overcome many of these barriers and provide a simple, convenient way for many current non-gardeners to begin to garden.

Cooking and Healthy Eating Market. Many Americans enjoy cooking as a hobby. Consumers in this market include:

- people interested in cooking who would appreciate the convenience and satisfaction of having a readily available supply of fresh-cut herbs to flavor soups, salads, and other dishes,
- people who prefer the distinctive texture and taste of freshly picked, vine-ripened tomatoes, basil, lettuces, and other vegetables over days-old supermarket produce, and
- people interested in healthy, pesticide-free foods for themselves and their families, reflecting both the rapidly growing interest in naturally and organically grown foods and the increasing number of people who, for health or weight concerns, include salads and fresh vegetables as part of their families’ diets.

We believe that our indoor gardening products are embraced in this market by people who understand the value of having an ongoing supply of fresh herbs and fresh produce throughout the year.

Home and Office Décor Market. Flowers are frequently used to brighten homes and offices worldwide. It is difficult to readily grow flowers indoors due to a lack of sufficient light and growing knowledge. As a result, people often use cut flowers, which are expensive, short-lived, and require ongoing maintenance. Our indoor gardening products enable colorful and fragrant flowers to be easily grown indoors year round. Flowers grown with our indoor gardening products will last for months with minimal care and maintenance. Flowers can be grown in a wide variety of indoor locations, including kitchen and bathroom countertops, living rooms, bedrooms, family rooms, offices, work stations, waiting rooms, and lobbies.

Products

AeroGarden Indoor Gardens. We currently offer four different indoor garden models with list prices ranging from approximately \$90 to \$250 and differentiated based on size, design, light intensity, degree of automation, inclusion of Adaptive Growth Technology or Advanced Growing Systems, height potential of light hoods, and inclusion of plant support systems.

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Currently, our AeroGarden product line is divided into four main categories:

1. AeroGarden 3 Series – The AeroGarden 3 series features the Advanced Growing System, grow lights, a smaller footprint, and an attractive, stylish design that makes it suitable for use as a decorative feature throughout the home or office. AeroGarden 3s fit easily on kitchen counters, night stands, and end tables. Some models include upgraded trim and designs such as the “Ladybug” garden targeted at all-family usage. List prices start at \$79.95.
 2. AeroGarden 7 Series – Includes our original products which feature the rainforest nutrient delivery system, automated lights, and reminder systems. List price is \$149.95.
3. AeroGarden Extra Series – A 7 pod garden with extended lamp arms and greater light output for growing larger vegetables. Some models also include stainless steel trim. List prices start at \$179.95.
4. AeroGarden ULTRA - The ULTRA features the new MyGarden control panel – an automated garden “brain” that makes gardening easier than ever for beginners and offers complete customization for experts. It also includes a redesigned lighting system featuring new MaxGrow Grow Lights and aluminum reflectors, the widest, easiest range of Grow Light adjustment from small to tall, an improved trellis system, 20% larger reservoir, and a “QuickPlant” button that walks users step-by-step through the planting process. List price is \$249.95.

AeroGarden Seed Kits. We currently offer more than 30 seed kits for use in our indoor gardening products. These seed kits include pre-seeded bio-grow seed pods and a three-to-six-month supply of nutrients, including our patented formula for adjusting water quality. Our seed kits have list prices ranging from \$13 to \$30, and include:

- Vegetable Gardens: cherry tomato, chili pepper, and salsa garden.
- Herb Gardens: gourmet herbs, Italian herbs, and pesto basil.
- Flower Gardens: cascading petunias, English cottage, scented blooms, and mountain meadow.
- Salad Gardens: salad greens, romaine lettuce.

Our seed kits are sold to consumers for use with our indoor gardening products. Individual seed kits are grown by consumers for three to six months and then new seed kits may be purchased for replanting.

AeroGarden Seed-Starting Kits. Our line of Garden Starter Systems and Grow Anything Kits are designed to allow consumers to plant and grow their own seeds in the AeroGarden. With our Garden Starter Systems, consumers can start up to 66 seedlings in our indoor gardens for transplant into their outdoor gardens when weather allows. With the Grow Anything Kits, consumers can grow their own seeds to maturity in the AeroGarden, or transplant seeds outdoors when weather allows, including plant nutrients, nutrient dispensers, and other products.

Other Accessories. To complement and expand the functionality of our indoor gardening products, we have developed a variety of accessory products.

Future Products. The core technology platform can be leveraged by bundling different components into new products with a wide variety of features and price points that then can be sold through a variety of direct and retail channels for use in different settings around the home or office. Examples include a side light system to further increase yields, and a reservoir product that allows users to supply additional water to the AeroGarden – even when on vacation or away for extended periods.

Integrated Marketing and Sales Channel Strategy

We consider our products to be an entirely new product category. A primary objective since launch has been to maximize the exposure of the product and educate consumers on the benefits of indoor gardening through an integrated marketing and distribution strategy. We launched with a nationwide public relations campaign in 2006, and received extensive media exposure, with multiple features on national talk shows as well local television coverage, local and national print articles and blog and Internet pieces. We combined the public relations launch with a retail and direct strategy focusing on high visibility partners and media, including product sales through retailers, national cataloguers, home shopping channels, direct television commercials, our own in-house direct response catalogue, internet sales, and inbound and outbound telemarketing.

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Shift in Channel Strategy. During the last three fiscal years, we reduced our presence in the retail channel due to the downturn in the economy, capital shortages, and the high cost of maintaining inventory levels sufficient for retail customers. As of March 31, 2013, our products were being offered in approximately 72 storefronts in North America (down from approximately 575 during the fiscal year ended March 31, 2011, as well as through select online retailers.

As discussed above under the captions “Our Business” and “Proprietary Technology and Intellectual Property,” in April 2013 we entered into a Securities Purchase Agreement and strategic alliance, along with a variety of other agreements, with Scotts Miracle-Gro. The Scotts Miracle-Gro agreements include a Brand License Agreement which allows us to use certain of Scotts Miracle-Gro’s trade name, trademark and/or service mark to rebrand the AeroGarden and other products in the AeroGrow Markets in exchange for our payment to Scotts Miracle-Gro of an amount equal to 5% of incremental growth in annual net sales. We believe that this agreement will allow our products to be prominently featured and sold in selected retail stores. As a result, we believe that the collaboration and support of Scotts Miracle-Gro will enable us to expand our presence in the retail market during the coming fiscal year. For further information on the strategic alliance with Scotts Miracle-Gro, please see Note 8 “Subsequent Events” to our financial statements.

Direct Response Sales. In the fall of 2006, we launched an infomercial advertising campaign that began with 30-minute programming and was subsequently supplemented with 60-second and 120-second television commercials. Since the fall of 2006, overall spending on television advertising has decreased as a percentage of the overall marketing budget, as we have been cash constrained and therefore focused our spending on the most efficient media channels. Although we did not spend any funds on television advertising in Fiscal 2013, we may resume television advertising in the future.

In 2007, we produced and began mailing our own in-house, direct mail product catalogue, which tested successfully with a mailing of approximately 60,000 catalogues. In Fiscal 2013 we mailed approximately 1.3 million catalogues. With our catalogue sales we focus on remarketing to current customers and also prospecting for new customers using database marketing techniques.

We established our first consumer product website in the fall of 2006 and supplemented this website in late 2007 with search engine advertising, banner advertising, email campaigns and web affiliate programs. In the fall of 2008 we took on in-house management of many of these programs from third-party providers and have seen resulting increases in efficiency.

A key focus of our web and catalogue marketing is to maximize the lifetime value of AeroGrow customers through repeat sales of our seed kits, light bulbs and accessories. During Fiscal 2013, direct response sales represented 86.0% of our total net sales.

Retail Sales. Initial shipments to retailers commenced in March 2006. Over the next several years, we rapidly grew our retail distribution and as of March 31, 2009 our products were being sold through approximately 7,500 stores in North America. In Fiscal 2010 through Fiscal 2013, we reduced our sales to retailers as discussed above, and as of March 31, 2013 our products were being sold through approximately 72 stores in North America. During Fiscal 2013, sales to retailers represented 12.1% of our total net sales.

Approximately 71.8% of our total sales to retailers represented sales to Amazon.com, Inc. in Fiscal 2013. As discussed above, we plan to expand our retail sales efforts during the coming fiscal year as a result of our strategic alliance with Scotts Miracle-Gro.

International Sales. We began testing international sales opportunities in the UK and Japan in late 2007, and have since expanded internationally into Australia, South Korea, Mexico, France and several other countries. During Fiscal

2013, we sold products to third-party distributors in seven international markets, and international sales represented 1.9% of our total net sales. International efforts in Fiscal 2013 were limited to supporting distribution in existing markets. As discussed above, we plan to expand our international sales efforts during the coming fiscal year as a result of our strategic alliance with Scotts Miracle-Gro.

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Competition

Aeroponic and hydroponic technologies have historically been limited to ardent hobbyists and commercial growing facilities. We believe that we are the first company to develop and offer a simple dirt-free indoor growing system for the mass consumer market.

Typical hydroponic manufacturers offer a range of equipment and accessories through distributors or small independent “hydro-shops” in a trade-oriented manner similar to plumbing or electrical suppliers. Purchasers typically mix and match equipment from various suppliers in an “a la carte” fashion to individually customize a large system that they then assemble on their premises. We believe that these products are substantially more expensive than our products.

We believe that our simplified and complete indoor gardening products and current and planned methods of distribution offer significant benefits from these traditional hydroponic industry practices. To date, we have discovered a kitchen design firm that has tried to introduce an indoor growing system into the market. In our laboratory tests, these systems have performed at levels far below our own systems in terms of germination success, longevity, speed-of-growth and overall yields.

However, we recognize that there are other companies that are better funded and have greater experience in producing hydroponic products in commercial markets, or that have been more successful in manufacturing or selling consumer products or soil-based gardening products.

Manufacturing and Operations

We source our AeroGarden products and accessory items from contract manufacturing companies that manufacture products using tooling we own, in accordance with our specifications, and subject to our intellectual property rights. We have four Chinese manufacturers of our garden products. Each is capable of manufacturing multiple garden models. We believe the existing production capacity of these manufacturers is more than sufficient to meet our garden requirements for the short-to-medium term. In addition, capacity expansion is available in a reasonable period of time with a nominal tooling investment. We also try to have multiple, dual-sourced manufacturers of our many component parts and accessories.

In July 2008 we opened a company-operated distribution center in Indianapolis, Indiana where we also produced and assembled our seed kits. In May 2011, we closed this facility and moved all our North American distribution and seed kit assembly operations to a third-party logistics facility in Mexico, Missouri. Indoor gardening products are shipped from China to the third-party fulfillment center in Missouri, as well as to third-party distribution facilities in countries outside North America.

Product Returns and Warranties

To date, product returns have been within our expectations for both retail and direct-to-consumer sales. At retail, we generally use a “destroy in field” methodology as the cost of shipping a used product back to us often does not justify the value of the recovered unit. We record warranty liabilities at the time of sale for the estimated costs that may be incurred under our basic warranty program. The specific warranty terms and conditions vary depending upon the product sold but generally include technical support, repair parts, and labor for periods up to one year. Factors that affect our warranty liability include the number of installed units currently under warranty, historical and anticipated rates of warranty claims on those units, and cost per claim to satisfy our warranty obligation.

Governmental Regulation and Certification

We believe that we are in compliance with regulations in the United States and Canada concerning the shipping and labeling of seeds and nutrients. Currently, the components for the indoor garden system are ETL certified. These certifications confirm that the products have been tested and conform to a recognized level of fire and other safety standards for consumers. Such independent third-party certification is required for sales of products through many major retailers.

We believe that our costs of compliance with environmental laws will not be material.

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Personnel

As of March 31, 2013, AeroGrow employed 22 employees with 20 full-time and two part-time. In addition, we contract the services of part-time and project consultants on an “as needed” basis. We believe that our employee relations are good. Historically, our outsourced business also included manufacturing, some telemarketing, infomercial production, fulfillment and shipping. Additional employees and/or consultants may be hired in the future as our operations merit.

ITEM 1A. RISK FACTORS

Our business, future performance and forward-looking statements are affected by general industry and market conditions and growth rates, general economic and political conditions in the United States, Canada and worldwide, competition, interest rate and currency exchange rate fluctuations and other events. The following items are representative of the risks, uncertainties and other conditions that may impact our business.

Risks Related to our Business, Products and Markets

We have incurred substantial net losses since inception and may never achieve profitability.

Since we commenced operations in 2002, and through March 31, 2013, we incurred substantial losses, including a net loss of \$8,258,594 for the twelve month period ended March 31, 2013. As of March 31, 2013, our losses have resulted in an accumulated deficit of \$76,004,171. The future success of our business will depend on the success of the Scotts Miracle-Gro partnership, our ability to profitably expand sales of our AeroGarden indoor garden systems, seed kits and accessory products, and develop new product extensions and applications.

We are subject to many of the risks common to developing enterprises, including undercapitalization, cash shortages, limited financial and other resources, and insufficient scale to be self-sustaining. There is no assurance that we will ever attain profitability.

Our financial condition may limit our ability to borrow funds or to raise additional equity as may be required to fund our future operations.

Our ability to borrow funds or raise additional equity may be limited by our financial condition. In addition, a failure to obtain additional funding to support our working capital and operating requirements could prevent us from making expenditures that are needed to allow us to maintain our operations. We may raise additional capital by renewing our current working capital facility at its maturity, in order to support our inventory and other operating requirements during the fiscal year ending March 31, 2014. In the event we have working capital needs and cannot raise this additional funding, we will have to scale back on our operating plans for the current and future fiscal years. There can be no assurance that we will be able to secure the additional capital in an amount and in time to support all of our operating plans.

As we grow our sales into the retail channel and increase sales through individual retailers, the loss or significant reductions in orders from our top retail customers could have a material adverse impact on our business.

In Fiscal 2013, our net sales to two retail customers totaled 74.0% of our total net sales to retailers. The loss of one of these significant customers, or a significant decline in orders could materially affect our sales of indoor garden systems, seed kits and accessories, and could therefore have a material adverse effect on our business, prospects, results of operations, and financial condition.

We do not have long-term sales agreements with, or other contractual assurances as to future sales to, any of our current or planned major retail customers. In addition, our business may be negatively affected by changes in the policies of our retailers, such as payment terms, limitation to shelf space, price demands and other conditions.

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Our recent inability to invest in the growth of our database of direct-to-consumer names may limit our ability to maintain or grow this sales channel.

Our direct response sales represented 86.0% of our total net sales during Fiscal 2013. Our marketing activities via email and catalogs focus on maximizing the lifetime value of AeroGrow customers through repeat sales of our seed kits, light bulbs and accessories. Our capital-constrained lack of investment in growing the database of potential customers could materially affect our sales of indoor garden systems, seed kits and accessories, and therefore have a material adverse effect on our business, prospects, results of operations, and financial condition.

Our future success is completely dependent on our ability to market our indoor garden systems, seed kits and accessory products and generate consumer acceptance on a broader scale.

We have introduced our indoor garden systems and seed kits as new products to consumer markets unfamiliar with their use and benefits. Although we believe that we have penetrated only a small portion of the potential market for our products, our marketing efforts may not generate widespread consumer adoption. If our marketing strategies fail to attract customers, our product sales may not produce future revenue sufficient to meet our operating expenses or fund our future operations. Our business, prospects, results of operations, and financial condition will be materially and adversely affected.

If we are unable to recruit, train and retain key personnel necessary to operate our business, our ability to successfully manage our business and develop and market our products may be harmed.

To maintain our business position, we will need to attract, retain, and motivate highly skilled design, development, management, accounting, sales, merchandising, marketing, and customer service personnel. Competition for many of these types of personnel can be intense, depending on general economic conditions, alternative employment options, and job location. As a result, we may be unable to successfully attract or retain qualified personnel. Additionally, any of our officers or employees can terminate their employment with us at any time. The loss of any key employee, or our inability to attract or retain other qualified employees, could have a material adverse effect on our business, prospects, results of operations, and financial condition.

A worsening of the economy, particularly in the United States and Canada, could materially adversely affect our business.

The success of our business operations depends significantly on consumer confidence and spending, which deteriorated during the recent worldwide economic downturn. A re-occurrence of the economic downturn and the consequent impact on consumer spending, particularly in the United States and Canada, could adversely impact our revenue, ability to market our products, build customer loyalty, or otherwise implement our business strategy. In such a scenario, we would experience a material adverse effect on our business, prospects, results of operations, and financial condition.

As a result of the economic downturn, decline in consumer spending and the consequent impact on the sales of our products, we restructured our operations and implemented a substantial workforce reduction. These actions could adversely impact the morale and performance of our remaining employees and our ability to hire new personnel.

Our business was adversely impacted by the deterioration in the global economy and the consequent impact on our various channels of distribution. We restructured our business operations in order to re-size our overhead costs and streamline our distribution, fulfillment, and manufacturing operations. This resulted in a substantial decrease in the number of our full-time employees. In addition, during Fiscal 2012 we instituted a temporary furlough program that impacted most employees, and instituted a salary deferral program for our senior management. In total, these actions

could have unintended impact on our remaining employees, could lead to a decline in employee morale, and could lead to a loss of additional personnel over and above the level desired by the Company. In the event of such employee attrition, we may not be able to replace the lost personnel on a timely basis, or with individuals having the same level of skills. In either case, our business prospects, results of operations and financial condition could be materially and adversely affected.

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Our current or future manufacturers could fail to fulfill our orders for indoor garden systems, which would disrupt our business, increase our costs, and could potentially cause us to lose our market.

We currently depend on three contract manufacturers in China to produce our indoor garden systems. These manufacturers could fail to produce the indoor garden system to our specifications or in a workmanlike manner and may not deliver the systems on a timely basis. Our manufacturers must also obtain inventories of the necessary parts and tools for production. Although we own the tools and dies used by our manufacturers, our manufacturers operate in China. As a result, our manufacturers may be subject to business risks that fall outside our control, including but not limited to, political, currency, and regulatory risks, each of which may affect the manufacturer's ability to fulfill our orders for indoor garden systems. For example, a labor strike in the ports of Las Angeles and Long Beach delayed the delivery of AeroGarden inventory during the critical pre-Christmas season and caused a decline in sales during the third and fourth quarters of Fiscal 2013. In addition, weather or natural disasters in China could disrupt our supply of product. Any change in manufacturers could disrupt or delay our ability to fulfill orders for indoor garden systems while we search for alternative supply sources, provide specifications, and test initial production. Our business prospects, results of operations and financial condition would be materially and adversely affected.

Our revenue and level of business activity are highly seasonal, requiring us to staff our operations, incur overhead and marketing costs, purchase and manufacture inventory, and incur other operating costs in advance of having firm customer orders for our products. A material variance in actual orders relative to anticipated orders could have an adverse impact on our business.

For the fiscal year ended March 31, 2013, approximately 49.3% of our total net sales occurred during four consecutive calendar months (October through January). We must therefore estimate sales in advance of the anticipated peak months and operate our business during the balance of the year in such a way as to insure that we can meet the demand for our products during the peak months. This requires us to incur significant operating, marketing, and overhead expenses, and to utilize cash and other capital resources to invest in inventory in advance of having certainty as to the ultimate level of demand for our product during the peak months. Shortfalls in the supply of our products could result in a significant loss of revenue due to lack of adequate product inventory. For example, a labor strike in the ports of Las Angeles and Long Beach delayed the delivery of AeroGarden inventory during the critical pre-Christmas season and caused a decline in sales during the third and fourth quarters of Fiscal 2013. Alternatively, a shortfall in actual demand for our products, relative to forecast, during peak months could cause us to liquidate excess inventory at a loss or at substantially lower margins. In any of these cases, we may not generate enough revenue to cover expenses incurred throughout the balance of the year. Our business prospects, results of operations and financial condition would be materially and adversely affected.

We are highly reliant upon a single distribution and assembly facility. Any material disruption to the operation of this facility could adversely affect our business.

All of our North American fulfillment and distribution operations, and the entirety of our seed kit assembly operations are located in a third-party-managed facility based in Mexico, Missouri. Any material disruption to the operation of this facility, whether caused by internal or external factors could have a material adverse effect on our business prospect s, results of operations and financial condition.

We rely on third-party providers in our manufacturing, warehouse, distribution, order processing, and fulfillment operations. If these parties are unwilling to continue providing services to us, or are unable to adequately perform such services for us on a cost effective basis, our business could be materially harmed.

We engage third parties to perform certain critical functions supporting our business operations. Any disruption in our relationship with any of our vendors could cause significant disruption to our business and we may not be able to

locate another party that can provide comparable services in a manner that is timely, consistent with our business plan, or on acceptable commercial terms. Our business prospects, results of operations and financial condition would be materially and adversely affected.

We may face significant competition, and if we are unable to compete effectively, our sales may be adversely affected.

We believe that our complete indoor garden systems offer significant benefits over traditional hydroponic industry products. However, there are companies in a variety of related markets, including but not limited to, consumer electronics, commercial hydroponics, gardening wholesale, and soil-based gardening that are larger, better funded, have more recognizable brand names, and have experience in our channels of distribution. These companies could potentially decide to develop products to compete with our products. These companies could use hydroponic technologies, and could achieve better consumer acceptance. The success of any competing products may have a material adverse effect on our business prospects, results of operations and financial condition.

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Increases in energy prices, resulting from general economic conditions, or other factors, may raise our cost of goods sold and adversely affect our business, results of operations and financial condition.

Energy costs, especially gasoline and fuel costs, are significant expenses in the delivery of our products. Increased costs resulting from general economic conditions, war, acts of nature, or other factors, may result in declining margins and operating results if market conditions prevent us from passing these increased costs on to our customers through timely price increases on our products. Our business prospects, results of operations and financial condition would be materially and adversely affected.

Our current AeroGarden manufacturers are located in China and therefore our product costs may be subject to fluctuations in the value of the dollar against the Chinese currency and increases in Chinese labor rates.

Although we purchase our AeroGarden products in U.S. dollars, the prices charged by our factories are predicated upon their cost for components, labor and overhead. Therefore, changes in the valuation of the U.S. dollar in relation to the Chinese currency may cause our manufacturers to raise prices of our products, which could reduce our profit margins and have a material adverse effect on our business prospects, results of operations and financial condition.

If our indoor garden systems fail to perform properly, our business could suffer with increased costs and reduced income.

From our inception through March 31, 2013, we have sold approximately 1.1 million AeroGardens and have provided a limited warranty with each garden sold. In addition, our indoor garden systems are “guaranteed to grow.” We therefore may be required to replace or repair products or refund the purchase price to consumers. Failure of our products to meet expectations could damage our reputation, decrease sales, increase costs related to returns and repairs, delay market acceptance of our products, result in unpaid accounts receivable, and divert our resources to remedy the malfunctions. The occurrence of any of these events would have a material adverse effect on our business prospects, results of operations and financial condition.

From time to time, we may be subject to litigation that, if decided adversely to us, could have a material adverse impact on our financial condition.

From time to time, we are a party to various litigation matters, in most cases involving ordinary and routine claims incidental to our business. We cannot estimate with certainty our ultimate legal and financial liability with respect to such litigation. Although we do not believe that any current litigation poses a material threat to our business, defense of any lawsuits or proceedings, even if successful, may require management to spend a substantial time and attention on the part of our management personnel that otherwise would be spent on other aspects of our business, and may require the expenditure of significant amounts for legal fees and other related costs. Settlement of lawsuits also may result in significant payments and modifications to our operations. In addition, we also may be subject to adverse publicity as a result of litigation. Any of these events could have a material adverse effect on our business, prospects, results of operations, and financial condition.

Risks Related to the Market for our Securities

The market price of our shares may fluctuate greatly. Investors in AeroGrow bear the risk that they will not recover their investment.

Currently, trading in our common stock is limited, and the price per share is likely to be influenced by the price at which and the amount of shares that selling security holders are attempting to sell at any time. This could cause our stock price to decline. Common stock such as ours may be subject to the activities of persons engaged in short selling

securities, which generally has the effect of driving the price down. In addition, the common stock of emerging growth companies is typically subject to high price and volume volatility. Therefore, the price of our common stock has fluctuated, and may continue to fluctuate, widely. A full and stable trading market for our common stock may never develop and, as a result, stockholders may not be able to sell their shares at the time they elect, if at all.

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There may be substantial sales of our common stock by existing security holders which could cause the price of our stock to decline.

Future sales of substantial amounts of our common stock in the public market or the perception that such sales might occur, could cause the market price of our common stock to decline and could impair the value of an investment in our common stock and our ability to raise equity capital in the future.

As of March 31, 2013, we had 5,904,877, common shares issued and outstanding.

In April 22, 2013 (during the first quarter of the fiscal year 2014), we entered into a Securities Purchase Agreement with SMG Growing Media, Inc, a wholly owned subsidiary of The Scotts Miracle-Gro Company, a worldwide marketer of branded consumer lawn and garden products (“Scotts Miracle-Gro”). Pursuant to the Securities Purchase Agreement, Scotts Miracle-Gro acquired 2,649,007 shares of the Company’s Series B Convertible Preferred Stock and a warrant to purchase shares of the Company’s common stock (For further information on the strategic alliance with Scotts Miracle-Gro, please see Note 8 “Subsequent Events” to our financial statements).

Sales of our common stock by security holders, or even the appearance that such holders may make such sales, may limit the market for our common stock or depress any trading market volume and price before other investors are able to sell the common stock. Moreover, a number of shareholders have held their investment for a substantial period of time and may desire to sell their shares, which could drive down the price of our common stock.

We can issue debt securities and shares of preferred stock without stockholder approval, which could adversely affect the rights of common stockholders.

Our Articles of Incorporation allow our Board of Directors to approve the terms and conditions of debt securities and preferred stock for issuance by the Company, including but not limited to voting rights, conversion privileges and liquidation preferences, without the approval of common stockholders. The rights of the holders of our common stock may be adversely impacted as a result of the rights that could potentially be granted to holders of debt securities or preferred stock that we may issue in the future. In addition, there could be an impact on the price of our common stock because of the potential impact on the rights of common shareholders resulting from future issuances of debt or preferred stock.

For example, on April 22, 2013 (during the first quarter of fiscal year 2014), we entered into a Securities Purchase Agreement with SMG Growing Media, Inc. (“SMG”), a wholly owned subsidiary of Scotts Miracle-Gro, a worldwide marketer of branded consumer lawn and garden products. Pursuant to the Securities Purchase Agreement, SMG acquired 2,649,007 shares of the Company’s Series B Convertible Preferred Stock, par value \$0.001 per share (the “Series B Preferred Stock”), and (ii) a warrant to purchase shares of the Company’s common stock (the “Warrant”). The Series B Preferred Stock is convertible into 2,649,007 shares of common stock (\$4,000,000 divided by a conversion price of \$1.51 per share). The Warrant entitles, but does not obligate, Scotts Miracle-Gro to purchase a number of shares of common stock that, on a “fully diluted basis,” constitute 80% of the Company’s outstanding capital stock (when added to all other shares owned), as calculated as of the date or dates of exercise. The Warrant can be exercised at any time and from time to time for a period of five years between April 22, 2016 and April 22, 2021 (For further information on the strategic alliance with Scotts Miracle-Gro, please see Note 8 “Subsequent Events” to our financial statements). The exercise price of the Warrant shall be equal to the quotient obtained by dividing:

(a) an amount equal to (i) 1.34 times the trailing twelve months “Net Sales” (which includes sales of the Company’s products by Scotts Miracle-Gro and its affiliates) minus (ii) “Debt Outstanding” net of cash (as such terms are defined in the Warrant,

by

(b) the total shares of capital stock outstanding, including outstanding in-the-money options and warrants, but not the Warrant contemplated in this Private Offering.

The Warrant contains customary anti-dilution rights (for stock splits, stock dividends and sales of substantially all the Company's assets).

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Under the Securities Purchase Agreement, our Board of Directors (the “Board”) is required to consist of five members. While the Warrant is outstanding, SMG is entitled to elect one director and have one additional Board observer. Please see Note 8 Subsequent Events to our financial statements for more detailed disclosure. As a result of this transaction, your rights as a common stockholder could be adversely affected. Because the holder of Series B Preferred Stock is entitled to vote on an “as-converted” basis with the common stock, SMG controls approximately 31% of the voting power of our outstanding equity. If SMG exercises the Warrant, its voting power will increase. As a result, SMG may be deemed to have effective control over all matters requiring action by our stockholders, including the election of our entire Board. It is unlikely that a change of control of our company could be effected without SMG’s approval.

Our outstanding warrants, options and any additional future obligations to issue our securities to various parties, may dilute the value of an investment in AeroGrow. In addition, the terms and conditions of these securities could significantly impact the price of our common shares, and could adversely impact our ability to raise additional equity capital.

As of March 31, 2013, we had reserved for issuance up to approximately 3,457,178 additional shares of common stock under the terms of outstanding convertible notes, warrants, options, conversion of Series A Convertible Preferred and other arrangements.

On April 11, 2012, we completed a restructuring of our debt and equity accounts that involved the conversion of all of our outstanding secured convertible debt and all of the Series A Convertible Preferred shares into 3,928,620 shares of common stock. In addition, during the period May 10, 2012 through May 31, 2012, 1,624,477 common stock warrants were exercised pursuant to a program under which we temporarily reduced the exercise price on all of our common stock warrants to \$0.01 per share. As of May 31, 2013, we had reserved for issuance up to approximately 527,270 additional shares of common stock under the terms of the remaining warrants and options to purchase our common stock (but excluding shares issuable upon SMG’s conversion of Series B Convertible Preferred Stock and upon exercise of the warrant (as described in the risk factor above and in Note 8 “Subsequent Events” to our financial statements).

For the length of time the warrants and options are outstanding, the holders will have an opportunity to profit from a rise in the market price of our common stock without assuming all the risks of common share ownership. This may adversely affect the terms upon which we can obtain additional capital. The holders of such derivative securities would likely exercise or convert them at a time when we would be able to obtain equity capital on terms more favorable than the exercise or conversion prices provided by the notes, warrants or options.

Further, future sales of substantial amounts of these shares, or the perception that such sales might occur, could cause the market price of our common stock to decline and could impair the value of an investment in our common stock and our ability to raise equity capital in the future.

If an exemption from registration on which we have relied for any of our past offerings of common stock or warrants is challenged legally, our principals may have to spend time defending claims, and we would then risk paying expenses for defense, rescission, and/or regulatory sanctions.

To raise working capital, we offered common stock and warrants in private transactions that we believed to be exempt from registration under the Securities Act and state securities laws. In 2004, we conducted a state-registered offering in Colorado of common stock and warrants, intended to be exempt from registration under the Securities Act as an intrastate offering. However, because we are incorporated in Nevada, the offering did not satisfy all of the requirements for an intrastate offering. This could result in investors or regulators asserting that the Colorado offering and/or private offerings subsequent to the Colorado offering (if the private offerings were integrated with the

Colorado offering) violated the Securities Act. There can be no assurance that investors or regulators will not be successful in asserting a claim that these transactions should not be integrated. In the event that one or more investors seeks rescission, with resulting return of investment funds and interest at a market rate, or that state or federal regulators seeks sanctions against us or our principals, we would spend time and financial resources to pay expenses for defense, rescission awards, or regulatory sanctions. The use of funds would reduce the capital available to operate our business. No assurance can be given regarding the outcome of any such actions.

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ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. DESCRIPTION OF PROPERTY

We lease a 9,868 square foot office space in, Boulder, Colorado, with a current monthly rent of \$9,362, which is subject to 3.5% annual increases. We also pay our proportionate share of building taxes, insurance and operating expenses. The lease term continues until September 30, 2014, unless modified under specified circumstances. The agreement contains other standard office lease provisions.

While our facilities appear adequate for the foreseeable future, we may add space to meet future growth as needed. Upon expiration of our current leases, we believe that we will be able to either renew our existing leases or arrange new leases in nearby locations on acceptable terms. We believe that these properties are adequately covered by insurance.

ITEM 3. LEGAL PROCEEDINGS

From time to time, we are party to various litigation matters, in most cases involving ordinary and routine claims incidental to our business. We cannot estimate with certainty our ultimate legal and financial liability with respect to any such pending litigation matters. However, based on our examination, we believe of such matters, that our ultimate liability, if any, will not have a material adverse effect on our financial position, results of operations or cash flows.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

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PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.

Our common stock is listed on the OTCQB market tier under the symbol AERO.

Price Range of Common Stock

The following table sets forth, for the periods indicated, the high and low daily closing prices of our common stock for the two most recently completed fiscal years while trading on the markets noted above.

	Fiscal Year Ended 3/31/13		Fiscal Year Ended 3/31/12	
	High	Low	High	Low
1st Quarter -				
Ended June 30	\$ 2.00	\$ 1.00	\$ 6.00	\$ 2.00
2nd Quarter -				
Ended Sept 30	\$ 2.00	\$ 1.00	\$ 3.00	\$ 1.00
3rd Quarter -				
Ended Dec 31	\$ 1.20	\$ 0.51	\$ 6.00	\$ 1.00
4th Quarter -				
Ended Mar 31	\$ 1.30	\$ 0.82	\$ 3.00	1.00

Stock prices for the period April 1, 2011 through October 16, 2012 have been adjusted to reflect a 1-for-100 reverse stock split that became effective on October 17, 2012, as previously reported in a Current Report on Form 8-K filed with the SEC on October 16, 2012.

Holders

As of June 15, 2013, we had approximately 604 holders of record of our common stock. A substantially greater number of stockholders are "street name" or beneficial holders, whose shares are held of record by banks, brokers and other financial institutions. See "Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters," for additional information about holders of our common stock.

Dividends

We have never declared or paid cash dividends on our common stock. We currently intend to retain all available funds and any future earnings for use in the operation of our business and do not anticipate paying any cash dividends in the foreseeable future. Any future determination to declare cash dividends will be made at the discretion of our board of directors, subject to compliance with covenants under any existing financing agreements, which may restrict or limit our ability to declare or pay dividends, and will depend on our financial condition, results of operations, capital requirements, general business conditions, and other factors that our board of directors may deem relevant.

Equity Compensation Plan Information

The equity compensation plan information called for by Item 201(d) of Regulation S-K is set forth in Item 12 "Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters" of Part III of this Annual Report under the heading "Equity Compensation Plan Information."

Issuer Purchases of Equity Securities

We did not repurchase any shares of our common stock during the quarter ended March 31, 2013.

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ITEM 6. SELECTED FINANCIAL DATA

Statements of Operations Data	Fiscal Years ended March 31,	
	2013	2012
Revenues	\$ 7,330,408	\$ 8,230,424
Cost of revenue	4,000,126	4,164,676
Gross profit	3,330,282	4,065,748
Operating Expenses		
Research and development	295,882	48,669
Sales and marketing	2,325,475	2,031,043
General and administrative	1,818,094	2,278,491
Total operating expenses	4,439,451	4,358,203
Loss from operations	(1,109,169)	(292,455)
Other (income) expense	7,149,425	3,258,579
Net loss	\$ (8,258,594)	\$ (3,551,034)
Net loss per share, basic and diluted	\$ (1.55)	\$ (19.98)
Weighted average number of common shares outstanding, basic and diluted	5,344,070	177,731
Balance Sheet Data		
	2013	2012
Cash and cash equivalents	\$ 524,491	\$ 501,577
Total assets	\$ 2,971,880	\$ 4,379,004
Total liabilities	\$ 3,542,929	\$ 9,501,046
Total stockholders' equity (deficit)	\$ (571,049)	\$ (5,122,042)

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Annual Report on Form 10-K ("Annual Report"), including the "Management's Discussion and Analysis of Financial Condition and Results of Operations," contains forward-looking statements regarding future events and our future results that are based on current expectations, estimates, forecasts, and projections about the industry in which we operate and the beliefs and assumptions of our management. Words such as "expects," "anticipates," "targets," "goals," "projects," "may," "will," "would," "could," "intends," "plans," "believes," "seeks," "estimates," variations of such words, and expressions are intended to identify such forward-looking statements. These forward looking statements may include, among others, statements concerning our expectations regarding our business, growth prospects, revenue trends, operating costs, working capital requirements, access to funding, competition, results of operations and other statements of expectations, beliefs, future plans and strategies, anticipated events or trends, and similar expressions concerning matters that are not historical facts. These forward-looking statements are only predictions that are subject to risks, uncertainties, and assumptions that are difficult to predict. Therefore, actual results may differ materially and adversely from those expressed in any forward-looking statements. Factors that might cause or contribute to such differences include, but are not limited to, those discussed in this Report under the section entitled "Risk Factors" in Item 1A of Part I and elsewhere, and in other reports we file with the SEC, specifically the most recent reports on Form 10-Q. While forward-looking statements are based on reasonable expectations of our management at the time

that they are made, you should not rely on them. We undertake no obligation to revise or update publicly any forward-looking statements for any reason.

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Executive Overview

We are in the business of developing, marketing, and distributing advanced indoor aeroponic and hydroponic garden systems. After several years of initial research and product development, we began sales activities in March 2006. Since that time we have expanded our operations and currently offer four different indoor garden models, more than 40 seed kits, and various gardening and kitchen accessories. Although our business is focused on the United States and Canada, our products are available in seven other countries.

Background – Fiscal Years 2010 – 2013

Beginning in the fiscal year ended March 31, 2010 (“Fiscal 2010”), and continuing through the fiscal year ended March 31, 2013 (“Fiscal 2013”), we scaled back our operations, particularly in the retail channel, as a result of the general economic downturn and the resulting decline in consumer confidence and spending. As of March 31, 2013, our products were offered in approximately 72 stores in North America, as compared to approximately 500 as of March 31, 2012. We also re-focused our efforts towards building our direct-to-consumer business, which carries higher margin opportunity and lower upfront inventory costs. To position our business for the future, we increased the depth and breadth of our direct sales distribution channels to include a direct mail catalogue business with approximately 1.3 million catalogues mailed in Fiscal 2013, significantly increased our web-selling presence and developed a robust e-mail marketing program. In addition, we have tested print ads in national magazines, infomercials, mall kiosks, and long-form and short-form infomercials, and may increase our use of these marketing vehicles in the future. In Fiscal 2013, approximately 86.0% of our total sales were to direct customers and approximately 14.0% of our total sales were to retail customers. Amazon.com, Inc., our largest retailer customer, comprised approximately 71.8% of our sales to retailers during Fiscal 2013.

In the fiscal year ended March 31, 2012 (“Fiscal 2012”), we also recapitalized our balance sheet. Specifically, we restructured the amounts and payment timing of certain of our accounts payable, issued \$1.6 million in short-term working capital debt, restructured the payment schedule for a \$2.1 million note payable to a supplier, and received approval from our shareholders and affected creditors to convert our Series A Preferred Stock and Subordinated Secured Convertible Notes into common stock (see additional detail on these transactions below under the caption “Liquidity and Capital Resources” and in Note 7 “Stockholder’s Equity” to our financial statements). The conversions of our convertible securities were completed in April 2012, during the first quarter of Fiscal 2013. In addition, also during the first quarter of Fiscal 2013, we offered our warrant holders the opportunity to exercise their warrants at a reduced price, resulting in \$1.59 million of new common equity capital from warrant exercises.

Subsequent Event – April 2013 Strategic Alliance with Scotts Miracle-Gro

As disclosed above under the caption “Item 1. Business,” we entered into a Securities Purchase Agreement and strategic alliance in April 2013 with a wholly owned subsidiary of Scotts Miracle-Gro. Pursuant to the Securities Purchase Agreement, we issued (i) 2,649,007 shares of Series B Convertible Preferred Stock, par value \$0.001 per share (the “Series B Preferred Stock”); and (ii) a warrant to purchase shares of our common stock for an aggregate purchase price of \$4.0 million. In addition, as part of the strategic alliance, we entered into several other agreements with Scotts Miracle-Gro, including: (i) an Intellectual Property Sale Agreement; (ii) a Technology Licensing Agreement; (iii) a Brand License Agreement; and (iv) a Supply Chain Management Agreement.

In the Intellectual Property Agreement, we agreed to sell all intellectual property associated with our hydroponic products (the “Hydroponic IP”), other than the AeroGrow and AeroGarden trademarks, free and clear of all encumbrances, to Scotts Miracle-Gro for \$500,000. Scotts Miracle-Gro has the right to use the AeroGrow and AeroGarden trademarks in connection with the sale of products incorporating the Hydroponic IP. In addition to the working capital infusion of approximately \$4.5 million from the Securities Purchase Agreement and Intellectual Property Sale Agreement, the strategic alliance affords us the use of the globally recognized and highly trusted Miracle-Gro brand name. We believe that the strategic alliance also gives Scotts Miracle-Gro an entry into the

burgeoning indoor gardening market, while providing AeroGrow a broad base of support in marketing, distribution, supply chain logistics, R&D, and sourcing. We intend to use our strategic alliance with Scotts Miracle-Gro to re-establish our presence in the retail and international sales channels.

As a result of these efforts, we believe we can meet our cash requirements for the next twelve months. We may need to seek additional capital, however, to provide a cash reserve against contingencies, address the seasonal nature of our working capital needs, and to enable us to invest further in trying to increase the scale of our business. There can be no assurance we will be able to raise this additional capital, that we will be able to increase the scale of our business, or that our existing resources will be sufficient to meet all of our cash requirements. In such an event, we would reduce the scale of our operations and take such actions as are available to us to reduce our cash requirements. However, there can be no assurance that such actions would be successful.

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Our Critical Accounting Policies

Inventory

Inventories are valued at the lower of cost, determined by the first-in, first-out method, or market. Included in inventory costs where we are the manufacturer are raw materials, labor and manufacturing overhead. We record the raw materials at delivered cost. Standard labor and manufacturing overhead costs are applied to the finished goods based on normal production capacity. A majority of our products are manufactured overseas and are recorded at cost.

	March 31, 2013	March 31, 2012
Finished goods	\$ 606,101	\$ 913,267
Raw materials	623,296	871,157
	\$ 1,229,397	\$ 1,784,424

We determine an inventory obsolescence reserve based on management's historical experience and establishes reserves against inventory according to the age of the product. As of March 31, 2013 and 2012, the Company had reserved \$94,414 and \$103,401, respectively, for inventory obsolescence.

Revenue Recognition

We recognize revenue from product sales, net of estimated returns, when persuasive evidence of a sale exists: that is, a product is shipped under an agreement with a customer; risk of loss and title has passed to the customer; the fee is fixed or determinable; and collection of the resulting receivable is reasonably assured.

We record estimated reductions to revenue for customer and distributor programs and incentive offerings, including promotions and other volume-based incentives. Certain incentive programs require the Company to estimate based on industry experience the number of customers who will actually redeem the incentive. At March 31, 2013 and March 31, 2012, the Company had accrued \$42,623 and \$37,955 respectively, as its estimate for the foregoing deductions and allowances.

Warranty and Return Reserves

We record warranty liabilities at the time of sale for the estimated costs that may be incurred under its basic warranty program. The specific warranty terms and conditions vary depending upon the product sold but generally include technical support, repair parts and labor for periods up to one year. Factors that affect our warranty liability include the number of installed units currently under warranty, historical and anticipated rates of warranty claims on those units, and cost per claim to satisfy our warranty obligation. Based upon the foregoing, we have recorded as of March 31, 2013 and March 31, 2012 a provision for potential future warranty costs of \$9,514 and \$8,304, respectively.

We reserve for known and potential returns and associated refunds or credits related to such returns based upon historical experience. In certain cases, customers are provided a fixed allowance, usually in the 1% to 2% range, to cover returned goods. This allowance is deducted from payments made to us by such retailers. As of March 31, 2013 and March 31, 2012, the Company has recorded a reserve for customer returns of \$27,255 and \$27,258, respectively.

Shipping and Handling Costs

Shipping and handling costs associated with inbound freight are recorded in cost of revenue. Shipping and handling costs associated with freight out to customers are also included in cost of revenue. Shipping and handling charges paid by customers are included in product sales.

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Stock Based Compensation

We account for share-based payments in accordance with FASB Accounting Standards Codification (“ASC”) 710-10-55 (prior authoritative guidance: FASB Statement 123(R) Shared-Based Payment). We use the Black-Scholes option valuation model to estimate the fair value of stock option awards issued under ASC 710-10-55. For the years ended March 31, 2013, and 2012, equity compensation in the form of stock options and grants of restricted stock that vested totaled \$176,850 and \$258,892, respectively, and is included in the accompanying Statements of Operations in the following categories:

	Years ended	
	March 31, 2013	March 31, 2012
General and administrative	\$ 135,643	\$ 168,560
Sales and marketing	41,207	90,332
Total	\$ 176,850	\$ 258,892

Advertising and Production Costs

We expense all production costs related to advertising, including, print, television, and radio advertisements when the advertisement has been broadcast or otherwise distributed. We record media costs related to its direct-to-consumer advertisements, inclusive of postage and printing costs incurred in conjunction with mailings of direct response catalogues, and related direct response advertising costs, in accordance with ASC 340-20-25 (prior authoritative guidance: Statement of Position, “No. SOP 93-7” Reporting on Advertising Costs). In accordance with ASC 340-20-25, direct response advertising costs incurred should be reported as assets and should be amortized over the estimated period of the benefits, based on the proportion of current period revenue from the advertisement to probable future revenue. As of March 31, 2013 and March 31, 2012, the Company had deferred \$3,799 and \$2,524, respectively, related to such media costs. Advertising expenses for the years ended March 31, 2013 and March 31, 2012, were \$1,055,619 and \$751,456, respectively.

Research and Development

Research, development, and engineering costs are expensed as incurred. Research, development, and engineering expenses primarily include payroll and headcount related costs, contractor fees, infrastructure costs, and administrative expenses directly related to research and development support.

Deferred Debt Issuance Costs

We capitalize debt issuance costs that are directly attributable to realizing the proceeds of the debt issued and these costs are amortized over the contractual life of the debt using the effective interest method.

New Accounting Pronouncements

In May 2011, the FASB issued ASC Update 2011-04 (Topic 820) Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS. This ASC update results in a consistent definition of fair value and common requirements for measurement of and disclosure about fair value between U.S. GAAP and International Financial Reporting Standards (“IFRS”). The new guidance includes changes to how and when the valuation premise of highest and best use applies, clarification on the application of blockage factors and other premiums and discounts, as well as new and revised disclosure requirements. This ASC update is effective for interim and annual periods beginning after December 15, 2011. The adoption of this guidance did not have a material effect on our financial statements.

In September 2011, the FASB issued updated guidance on the periodic testing of goodwill for impairment. This guidance will allow companies to assess qualitative factors to determine if it is more-likely-than-not that goodwill

might be impaired and whether it is necessary to perform the two-step goodwill impairment test required under current accounting standards. This new guidance is effective for us beginning July 1, 2012, with early adoption permitted. This new guidance will not have a material impact on our financial statements.

In July 2012, FASB amended ASC 350, Intangibles — Goodwill and Other. This amendment is intended to simplify how an entity tests indefinite-lived assets other than goodwill for impairment by providing entities with an option to perform a qualitative assessment to determine whether further impairment testing is necessary. The amended provisions will be effective for the Company beginning in the first quarter of fiscal 2014, and early adoption is permitted. This amendment impacts impairment testing steps only, and therefore adoption will not have an impact on the Company's financial position, results of operations or cash flows.

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Seasonality and Currency Fluctuations

We do not currently expect inflation to have a significant effect on our operations. Because our indoor garden systems are designed for an indoor gardening experience, we experience slower sales in the United States and Canada during the late spring and summer months when our consumers may tend to garden outdoors. In addition, we have experienced increased sales during the holiday the third quarter of our fiscal year (October through December). We sell to our international distributors in U.S. Dollars thereby minimizing effects from currency fluctuations. We purchase our gardens and other accessory products from Chinese manufacturers, and these purchases are denominated in U.S. Dollars. However, over time, the cost of the products we procure from China may be affected by changes in the value of the U.S. Dollar relative to the Chinese currency and/or by labor and material cost increases faced by our Chinese manufacturers.

Results of Operations

The following table sets forth, as a percentage of sales, our financial results for the last two fiscal years:

	Fiscal Years Ended March 31,			
	2013		2012	
Net revenue				
Direct-to-consumer	86.0	%	89.8	%
Retail	12.1	%	8.6	%
International	1.9	%	1.6	%
Total net revenue	100.0	%	100.0	%
Cost of revenue	54.6	%	50.6	%
Gross profit	45.4	%	49.4	%
Operating expenses				
Research and development	4.0	%	0.6	%
Sales and marketing	31.7	%	24.7	%
General and administrative	24.8	%	27.7	%
Total operating expenses	60.5	%	53.0	%
Loss from operations	-15.1	%	-3.6	%
Total other (income)/expense, net	97.5	%	39.6	%
Net loss	-112.6	%	-43.2	%

Fiscal Years Ended March 31, 2013 and March 31, 2012

Summary Overview

For the fiscal year ended March 31, 2013 (“Fiscal 2013”), our net sales totaled \$7,330,408, a decrease of 10.9% from the fiscal year ended March 31, 2012 (“Fiscal 2012”).

As of March 31, 2013, our products were being carried in approximately 72 retail storefronts, as compared to approximately 486 a year earlier. The decrease is the result of the completion of a promotion program for our AeroGarden 3 units at Canadian Tire stores in Canada.

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Our direct-to-consumer sales declined, by 14.7% to \$6,303,955, principally reflecting lower sales in the fiscal third quarter caused by a labor strike in the ports of Los Angeles and Long Beach which delayed the delivery of container loads of AeroGardens in the critical pre-Christmas time period, along with an overall decline in sales of seed kits and accessory items due in part to the aging of our direct response customer file. Our sales to retailer customers increased by 24.9% to \$887,417 during Fiscal 2013. The increase in sales to retailers reflected sales to newly acquired retail accounts, particularly Amazon.com. On a product line basis, we saw a year-over-year increase in the mix of AeroGardens as a percent of total revenue. For the fiscal year ended March 31, 2013, AeroGarden sales decreased by 4.7% and represented 48.1% of total revenue, as compared to 44.9% in the prior year period. This increase reflected the combined impact of stocking orders from new retailer accounts and a shift in our marketing mix to drive trial of AeroGardens by new consumers. Seed kit and accessory sales decreased as a percent of the total to 51.9% from 55.1% in the prior year period.

We saw a 39.2% year-over-year decrease in the efficiency of our marketing efforts during Fiscal 2013, as measured by dollars of direct-to-consumer sales per dollar of advertising expense. Sales per dollar of advertising expense totaled \$5.97 during Fiscal 2013, as compared to \$9.83 per dollar of advertising expense in Fiscal 2012. Marketing efficiency declined as we moved from a reactive marketing strategy designed to conserve capital, to a proactive strategy designed to increase awareness and drive future product and seed kit sales. The \$304,163 increase in advertising spend is an initial step in our plans to reverse the long term sales decline and begin growing revenue once again, combined with lower sales attributable to a labor strike in the ports of Los Angeles and Long Beach during the critical pre-Christmas period that delayed delivery of AeroGarden inventory. Sales to international distributors increased in Fiscal 2013, by 4.5% to \$139,036. This increase is exclusively attributable to reorders from our existing customers. The combination of these factors resulted in a year-over-year decline in total net sales of 10.9% to \$7,330,408 in Fiscal 2013.

Our gross margin for Fiscal 2013 was 45.4%, down from 49.4% in the prior year, as efficiency gains in our assembly, fulfillment, and distribution operations were effectively offset by the shift in our revenue mix from higher margin direct response and seed kit sales to lower margin retailers and AeroGarden sales.

Operating expenses for Fiscal 2013 totaled \$4,439,451, 1.9% or \$81,248 higher than the prior fiscal year. Sales and marketing costs increased by 14.5%, including a \$304,163, or 40.5% increase in advertising. General and administrative expense totaled \$1,818,094 during Fiscal 2013, down 20.2%, or \$460,397 from Fiscal 2012. The lower general and administrative expense primarily reflected the impact of spending reductions in all areas, including legal expenses, administration, and facility and office-related expenses. Research and development costs also increased 507.9% year-over-year or \$247,213 in Fiscal 2013, reflecting increased product development activity relative to the prior fiscal year primarily related to the development of the AeroGarden ULTRA.

Our loss from operations totaled \$1,109,169 for Fiscal 2013, as compared to a loss of \$292,455 in the prior year. The higher loss resulted from an increase spending on marketing and product development combined with lower revenue and decreased margins during Fiscal 2013.

Other expense for Fiscal 2013 totaled \$7,149,425, as compared to \$3,258,579 in the prior year. The net other expense in the current year included \$6,648,267 in non-recurring, non-cash debt conversion costs, \$80,389 in non-recurring gains relating to adjustments in estimates of certain accounts payable accounts, and \$130,992 in non-cash amortization expense related to short-term promissory notes issued in September 2012.

Our net loss for Fiscal 2013 totaled \$8,258,594, up \$4,707,560 from the prior year. The increased net loss is primarily due to the increase in net other expense related to the non-recurring, non-cash charges resulting from the conversion of our convertible debt into common equity in April 2012 as well as to the increased operating loss.

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Revenue

The table set forth below shows quarterly revenues by sales channel for the fiscal years ended March 31, 2013, and March 31, 2012:

	Quarters ended				Year ended
	30-Jun-11	30-Sep-11	31-Dec-11	31-Mar-12	31-Mar-12
Sales – direct-to-consumer	\$1,292,889	\$1,268,479	\$2,798,393	\$2,027,086	\$7,386,847
Sales – retail	151,024	197,658	206,007	155,782	710,471
Sales – international	35,990	31,382	21,545	44,189	133,106
	\$1,479,903	\$1,497,519	\$3,025,945	\$2,227,057	\$8,230,424

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	Quarters ended				Year ended
	30-Jun-12	30-Sep-12	31-Dec-12	31-Mar-13	31-Mar-13
Sales – direct-to-consumer	\$1,332,155	\$1,113,056	\$2,322,967	1,535,777	\$6,303,955
Sales – retail	43,783	6,419	626,072	211,143	887,417
Sales – international	40,595	24,785	23,454	50,202	139,036
	\$1,416,533	\$1,144,260	\$2,972,493	\$1,791,122	\$7,330,408

In Fiscal 2013, revenue totaled \$7,330,408, a decrease of \$900,016, or 10.9%, from Fiscal 2012. The overall sales decline in Fiscal 2013 resulted from a \$1,082,892, or 14.7%, year-over-year reduction in direct-to-consumer sales, to \$6,303,955, from \$7,386,847 in Fiscal 2012, which more than offset the 24.9% increase in retail sales. The decrease principally reflects the lower sales in the fiscal third quarter caused in part by a labor strike in the ports of Los Angeles and Long Beach which delayed the delivery of container loads of AeroGardens in the critical pre-Christmas time period along with an overall decline in sales of seed kits and accessory items. During the Fiscal 2013, direct-to-consumer sales per dollar of advertising expense totaled \$5.97 as compared to \$9.83 in the prior year period, with much of the decline reflecting increases in advertising expense incurred during the fiscal third quarter, but prior to the commencement of the port labor strike that adversely impacted revenue. In addition, we increased the utilization of catalog mailings and other marketing methods to prospect for new customers, which tend to generate lower immediate returns on marketing investment relative to marketing efforts focused on existing customers. Finally, on a comparative year-to-date basis, our advertising spending in the prior year was constrained by liquidity issues for much of the time period.

Sales to retailer customers for Fiscal 2013 totaled \$887,417, up \$176,946, or 24.9%, from the same period a year earlier, principally reflecting sales to newly acquired retail accounts, particularly Amazon.com, during the latter half of Fiscal 2013.

International sales for Fiscal 2013 totaled \$139,036, up \$5,930 from Fiscal 2012. This increase reflects the timing of reorders from existing international distributors, as we were not attempting to develop our international markets in Fiscal 2013. As of March 31, 2013, our products were being sold in seven countries outside the United States and Canada, principally in Europe, Asia and in Australia.

The following table presents our quarterly sales by product category, in U.S. Dollars and as a percent of total net revenue, for Fiscal 2013 and Fiscal 2012.

	Quarters ended				Year ended
	30-Jun-11	30-Sep-11	31-Dec-11	31-Mar-12	31-Mar-12
Product Revenue					
AeroGardens	\$547,564	\$475,184	\$1,694,529	\$979,905	\$3,697,182
Seed kits and accessories	932,339	1,022,335	1,331,416	1,247,152	4,533,242
Total	\$1,479,903	\$1,497,519	\$3,025,945	\$2,227,057	\$8,230,424
% of Revenue					
AeroGardens	37.0	% 31.7	% 56.0	% 44.0	% 44.9
Seed kits and accessories	63.0	% 68.3	% 44.0	% 56.0	% 55.1
Total	100.0	% 100.0	% 100.0	% 100.0	% 100.0

	Quarters ended				Year ended
	30-Jun-12	30-Sep-12	31-Dec-12	31-Mar-13	31-Mar-13
Product Revenue					
AeroGardens	\$519,189	\$411,302	\$1,846,612	\$747,508	\$3,524,611
Seed kits and accessories	897,344	732,958	1,125,881	1,049,614	3,805,797

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Total	\$1,416,533		\$1,144,260		\$2,972,493		\$1,797,122		\$7,330,408	
% of Revenue										
AeroGardens	36.7	%	35.9	%	62.1	%	41.6	%	48.1	%
Seed kits and accessories	63.3	%	64.1	%	37.9	%	58.4	%	51.9	%
Total	100.0	%	100.0	%	100.0	%	100.0	%	100.0	%

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AeroGarden sales totaled \$3,524,611 in Fiscal 2013, down \$172,571 or 4.7%, from the year earlier. The minimal decrease is garden sales compared to the overall sales decrease, reflects the increase in sales to retailers in the fiscal third quarter, the increase in direct-to-consumer prospecting activity which tends to generate a higher mix of AeroGarden sales, and the launch of the new AeroGarden ULTRA model. Sales of seed kits and accessories declined, by \$727,445, or 16.0%, principally reflecting the overall decline in direct-to-consumer sales and the shift in marketing mix to new customer acquisition activity. On a cumulative basis, we have sold approximately 2.6 million after-market seed kits to-date. In Fiscal 2013, sales of seed kits and accessories represented 51.9% of our total net revenue, down from 55.1% in the prior fiscal year.

Cost of Revenue

Cost of revenue for Fiscal 2013 totaled \$4,000,126, a 4.0% decrease from the prior fiscal year. Cost of revenue includes product costs for purchased and manufactured products, freight costs for inbound freight from manufacturers and outbound freight to customers, costs related to warehousing, and duties and customs fees applicable to products imported. The dollar amount of cost of revenue decreased because of the decrease in total sales, as well as cost reductions in our seed kit assembly, fulfillment, and distribution operations. As a percent of total revenue, cost of revenue totaled 54.6% in Fiscal 2013, as compared to 50.6% in the year earlier period. The increase in costs as a percent of revenue reflected a greater mix of lower-margin retail and AeroGarden sales, and the amortization of access overhead in inventory,

Gross Margin

Our gross margin varies based upon the factors affecting net revenue and cost of revenue as discussed above, as well as the mix of our revenue that comes from the retail, direct-to-consumer, and international channels. In a direct-to-consumer sale, we recognize as revenue the full consumer purchase price for the product; in retail and international sales, by comparison, we recognize as revenue the wholesale price for the product which we charge to the retailer or international distributor. Media costs associated with direct sales are included in sales and marketing costs. For international sales, margins are based on the distributor purchasing products by letter of credit or cash-in-advance terms with the distributors bearing all of the marketing and distribution costs within their territories. As a result, international sales generally have lower margins than domestic retail sales. Overall, the gross margin for Fiscal 2013 was 45.4% as compared to 49.4% in the prior year.

Sales and Marketing

Sales and marketing costs for Fiscal 2013 totaled \$2,325,475, an increase of \$294,432, or 14.5%, from the prior fiscal year. Sales and marketing costs include all costs associated with the marketing, sales, operations, customer support, and sales order processing for our products. The following table breaks down the components of our sales and marketing costs for Fiscal 2013 and Fiscal 2012:

	Fiscal Years Ended March 31,	
	2013	2012
Advertising	\$ 1,055,619	\$ 751,456
Salaries and related expenses	1,004,194	998,963
Sales commissions	41,843	9,003
Trade shows	9,165	--
Other	214,654	271,621
	\$ 2,325,475	\$ 2,031,043

Advertising is principally composed of the costs of developing and airing our infomercials, the costs of development, production, printing, and postage for our catalogues, and mailing and web media costs for search and affiliate web marketing programs. Each of these can be key components of our integrated marketing strategy because they generate direct-to-consumer sales and help build awareness of, and consumer demand for, our products in all our channels of

distribution. Advertising expense totaled \$1,055,619 for Fiscal 2013, a year-over-year increase of 40.5%, or \$304,163, reflecting more catalogues mailed during the current year period, and increases in all areas of advertising activity because liquidity issues severely constrained advertising spending during the prior year period.

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Sales and marketing personnel costs include salaries, payroll taxes, employee benefits and other payroll costs for our sales, operations, customer service, graphics and marketing departments. Personnel costs for sales and marketing in Fiscal 2013 were \$1,004,194, up 0.5% from Fiscal 2012.

Sales commissions, generally 5% of cash collections from our retailer customers, are paid to third-party sales representatives that assist us in developing and maintaining relationships with retailers. Sales commission expense totaled \$41,483 for the fiscal year ended March 31, 2013, up 364.8% from the prior fiscal year. The year-over-year increase in sales commission expense resulted from the increase in retail sales.

Other marketing expenses decreased year-over-year because of reductions in travel expense, inventory storage fees, order processing costs, and generally reduced spending in a variety of categories.

General and Administrative

General and administrative expense for the fiscal year ended March 31, 2013 totaled \$1,818,094, down \$460,397, or 20.2% from the prior fiscal year. The decrease reflected a reduction in depreciation and amortization expense, as well as spending reductions in all areas, including legal expenses, administration, and facility and office-related expenses.

Research and Development

Research and development costs totaled \$295,882 for Fiscal 2013, an increase of \$247,213, or 507.9%, from the prior fiscal year.

Research and development costs are comprised of payroll and other costs associated with (i) development of new AeroGarden models and technologies; (ii) our plant laboratories that research new plant varieties; and (iii) new technologies, such as improved lighting and nutrient formulation and delivery to enhance the performance of our products. The increase principally reflected expenses related to design and consulting service expenses we incurred to support new product development activities related to the launch of the AeroGarden ULTRA.

Operating Loss

The loss from operations totaled \$1,109,169 in Fiscal 2013, an increase of \$816,714, or 279.3%, over the prior year, primarily as a result of increased spending on business development activities including marketing and product development costs designed to grow the business long term, combined with lower sales.

As a non-U.S. GAAP measure of our operating performance, we track earnings before interest, taxes, depreciation and amortization ("EBITDA") as an indicator of our ability to generate cash, which we define as Operating Profit or Loss excluding the non-cash depreciation, amortization and stock based compensation expense incurred during the period. As calculated in the table below, our EBITDA loss for Fiscal 2013 totaled \$757,791, \$1,056,289 less favorable than the \$298,498 EBITDA recognized during the prior year.

	Fiscal Years Ended March 31,	
	2013	2012
Operating loss	\$ (1,109,169)	\$ (292,455)
Add Back Non-Cash Items:		
Depreciation	160,613	235,972
Amortization	13,915	96,089
Stock based compensation	176,850	258,892
Total Non-Cash Items	351,378	590,953
EBITDA	\$ (757,791)	\$ 298,498

The GAAP measure most directly comparable to EBITDA is net earnings. The non-GAAP financial measure of EBITDA should not be considered as an alternative to net earnings. EBITDA is not a presentation made in accordance with GAAP and has important limitations as an analytical tool. EBITDA should not be considered in isolation or as a substitute for analysis of our results as reported under GAAP. Because EBITDA excludes some, but not all, items that affect net earnings and is defined differently by different companies, our definition of EBITDA may not be comparable to similarly titled measures of other companies.

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Other Income and Expense

Other expense for Fiscal 2013 totaled \$7,149,425, as compared to \$3,258,579 in the prior year. The net other expense in Fiscal 2013 included \$6,648,267 in non-recurring, non-cash debt conversion costs, \$80,389 in non-recurring gains relating to adjustments in estimates of certain accounts payable accounts, and \$130,992 in non-cash amortization expense related to short-term promissory notes issued in September 2012. Net other expense for Fiscal 2012 included \$398,373 in gains related to accounts payable balance concessions we negotiated with certain of our vendors and \$2,182,842 in non-cash amortization expense related to the 2010 issuance of convertible promissory notes were fully converted into common equity in April 2012.

Net Loss

The net loss for Fiscal 2013 was \$8,258,594, \$4,707,560 higher than in Fiscal 2012, primarily due to the increase in net other expense related to the non-recurring, non-cash charges resulting from the conversion of our convertible debt into common equity in April 2012, as well as the increased operating loss during the year.

Liquidity and Capital Resources

After adjusting the net loss for non-cash items and changes in assets and liabilities, the net cash used by operating activities totaled \$342,152 in Fiscal 2013 as compared to net cash provided by operating activities of \$369,460 in the prior fiscal year.

Non-cash items, comprising depreciation, amortization, loss on disposal of fixed assets, bad debt allowances, issuances of common stock and options, and interest expense from warrants issued with convertible debentures, totaled \$7,257,270 of non-cash expense Fiscal 2013, as compared to of \$3,114,529 in the prior fiscal year.

Changes in current assets contributed cash of \$469,651 during Fiscal 2013, principally from reductions in inventory and other current assets. In Fiscal 2012, changes in these assets contributed \$937,743 reflecting decreases in accounts receivable and inventory. As of March 31, 2013, the inventory balance was \$1,229,397, representing approximately 112 days of sales activity during Fiscal 2013. Net accounts receivable totaled \$173,096 as of March 31, 2013, representing approximately 71 days of net retail sales activity at the average daily rate of sales recognized during Fiscal 2013. The days of sales in receivables and inventory calculations can fluctuate, and are greatly impacted, by our seasonality, and by the timing of sales and receipts of inventory during the period.

Current operating liabilities increased \$189,521 during Fiscal 2013, principally because of reductions in accounts payable totaling \$228,598 which were offset by a \$323,464 increase in accrued interest and customer deposits and \$67,590 in accrued expenses. In the prior year period, current operating liabilities decreased \$131,778 during the twelve months ended March 31, 2012, principally because of reductions in accounts payable and accrued expenses totaling \$667,398 which were partially offset by a \$568,602 increase in accrued interest. Accounts payable as of March 31, 2013 totaled \$379,242, representing approximately 16 days of daily expense activity at both the average daily rate of expenses incurred during Fiscal 2013.

Net investment activity used \$302,719 of cash totaling, principally because of the purchase of tooling for the AeroGrow ULTRA, as compared to cash provided of \$369,460 in the prior year. Net financing activity, including the issuance of short-term working capital debt and the net reduction in total debt obligations, provided cash of \$667,785 during Fiscal 2013, as compared to a use of cash of \$311,606 in the prior year.

As of March 31, 2013, we had a cash balance of \$566,785, of which \$42,924 was restricted as collateral for our various corporate obligations. This compares to a cash balance of \$544,333 as of March 31, 2012, of which \$42,756 was restricted.

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As of March 31, 2013 and March 31, 2012, the outstanding balance of our note payable and debt, including accrued interest, is as follows:

	March 31, 2013	March 31, 2012
Main Power Promissory Note	\$ 1,703,764	\$ 1,999,297
First Western Trust Term Loan	322,832	578,445
Subordinated Secured Convertible Notes	--	5,032,188
Notes Payable –Credit Card		
Receipts-Backed Notes	640,373	941,815
Pawnee Promissory Note	41,514	74,422
Total Debt	2,708,483	8,626,167
Less current portion	1,539,722	2,030,869
Long Term Debt	\$ 1,168,761	\$ 6,595,298

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We use, or have used, a variety of debt funding sources to meet our liquidity requirements, including the following:

Main Power Promissory Note

On June 30, 2009, we entered into a Letter Agreement (“Letter Agreement”) with Main Power Electrical Factory, Ltd. (“Main Power”) and executed a Promissory Note. Pursuant to the terms of the Letter Agreement, Main Power agreed to release AeroGrow from \$1,386,041 of existing obligations owed to Main Power in return for the execution of the Promissory Note for the same amount. In addition, the Letter Agreement included other provisions relating to the terms and conditions under which we purchase AeroGarden products from Main Power.

Effective as of December 31, 2010, AeroGrow and Main Power entered into an agreement to amend various obligations owed by AeroGrow to Main Power. As part of the amendments, AeroGrow issued a new promissory note (the “Revised Main Power Note”) in the amount of \$2,162,046. The Revised Main Power Note retired and replaced the original Promissory Note, and also retired and replaced certain obligations totaling \$661,446 relating to raw material and finished goods inventory purchased and/or manufactured by Main Power on behalf of AeroGrow. The Revised Main Power Note had a final maturity of May 31, 2013, and carried an interest rate of 8% per annum.

The parties executed an amendment to the Revised Main Power Note that, effective as of December 31, 2011, restructured the amortization schedule for the Revised Main Power Note and extended the final maturity to December 15, 2015. In addition, Main Power agreed to waive any existing defaults under the Revised Main Power Note. The agreed revisions to the amortization schedule provide for monthly interest payments through the final maturity and principal payments totaling \$159,000 during Fiscal 2013, \$555,000 during the fiscal year ending March 31, 2014, \$725,000 during the fiscal year ending March 31, 2015, and \$664,724 during the period April 2015 through December 2015. In addition, any utilization by AeroGrow of consignment inventory held as collateral by Main Power further reduces the amount outstanding under the Revised Main Power Note. As of March 31, 2013, the outstanding balance under the Revised Main Power Note, including accrued interest, totaled \$1,703,764 and we were current and in compliance with all terms and conditions.

On April 23, 2013, the MainPower Promissory Note outstanding, including all accrued interest, was paid in full for \$950,000. For further information in the termination of the Main Power Promissory Note, please see Note 8 “Subsequent Events” to our financial statements.

First Western Trust Term Loan

On May 21, 2010, the Company, First Western Trust Bank (“FWTB”) and Jack J. Walker, our Chairman, as guarantor, executed a business loan agreement and related promissory note (the “FWTB Term Loan”) for a four-year loan in an initial principal amount of \$1 million. The FWTB Term Loan is secured by a lien on our assets. The FWTB Term Loan bears interest at a fixed rate of 7.25% per annum. We make equal monthly payments of principal and interest over the four-year term of the FWTB Term Loan, which has a final maturity date of May 21, 2014. The terms and conditions of the FWTB Term Loan include limitations on the Company incurring additional debt and paying dividends on our stock without the consent of FWTB. In the event of a default under the FWTB Term Loan, FWTB has the option to declare the loan immediately due and payable. As of March 31, 2013, \$322,832 was outstanding under the FWTB Term Loan, including accrued interest and we were current and in compliance with all terms and conditions.

Subordinated Secured Convertible Notes

Between May and September 2010, we completed a private offering of \$7,020,000 in Subordinated Secured Convertible Notes (the “Subordinated Secured Convertible Notes”) and warrants to purchase 70,200 shares of our

common stock (the “Warrants”). We used the proceeds from the private offering to invest in advertising and marketing programs to support our direct-to-consumer business, provide general working capital, pay commissions and expenses related to the private offering, and repay certain outstanding obligations.

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On April 11, 2012, Subordinated Secured Convertible Notes totaling \$7,444,380, inclusive of accrued interest of \$647,985, were converted into 2,977,815 shares of our common stock, reflecting a conversion price of \$2.50 per share of common stock. Subsequent to the conversions, there were no remaining Subordinated Secured Convertible Notes or accrued interest outstanding. The Subordinated Secured Convertible Notes holders agreed to convert the Subordinated Secured Convertible Notes into common stock in exchange for our agreement to reduce the conversion price from \$10.00 per share of common stock to \$2.50 per share of common stock. As a result of the conversion of the Subordinated Secured Convertible Notes into common equity, we recognized a total of \$6,648,267 in non-cash expense comprising \$3,461,637 of debt conversion costs on the exchange and \$3,186,630 on the accelerated recognition of the debt discount and deferred debt issuance costs during Fiscal 2013.

As of March 31, 2013, there were no Subordinated Secured Convertible Notes or accrued interest outstanding.

Notes Payable – 2010 Credit Card Receipts-Backed Notes

On October 28, 2010 and November 5, 2010, we closed on the private sale of \$1.5 million in 15% secured convertible promissory notes, including \$450,000 in 15% related party secured convertible promissory notes, backed by a portion of our prospective credit card receipts, (the “2010 Credit Card Notes”) and 50,000 warrants to purchase our common stock (the “Credit Card Warrants”) (collectively, the “2010 Credit Card Offering”). Consideration for the 2010 Credit Card Offering comprised \$1.5 million in cash. Net cash proceeds to AeroGrow after deducting placement agent sales commissions totaled \$1,474,500. We used the proceeds from the 2010 Credit Card Offering to invest in advertising and marketing programs to support our direct-to-consumer business, provide general working capital, pay commissions and expenses related to the private offering, and repay certain outstanding obligations.

For the twelve months ended March 31, 2013 and March 31, 2012, the total amortized deferred debt issuance costs relating to the 2010 Credit Card Offering were zero and \$23,401, respectively.

As of October 3, 2011, the 2010 Credit Card Notes were repaid in full.

Notes Payable – 2011 Credit Card Receipts-Backed Notes

During the three months ended December 31, 2011, we closed on the private sale of \$1,633,776 in 17% secured promissory notes backed by a portion of our prospective credit card receipts, (the “2011 Credit Card Notes”) and a 1% share of our prospective monthly sales into the network marketing channel for a period of three years following our first sale into the network marketing channel (the “MLM Revenue Share”) (collectively, the “2011 Credit Card Offering”). Consideration for the 2011 Credit Card Offering comprised \$1,477,300 in cash and the conversion of \$156,476 in other obligations of the Company, including \$61,476 of deferred compensation owed to executive officers of AeroGrow. After deducting \$46,565 of placement agent sales commissions and expenses, net cash proceeds to AeroGrow totaled \$1,430,735. In addition, we are obligated to pay a deferred sales commission to the placement agent equal to 10% of the MLM Revenue Share paid to investors in the 2011 Credit Card Offering (with the deferred sales commission reduced to 6% for payments to company-referred investors and 0% on payments to officers and directors), concurrently with the payment of the MLM Revenue Share. We used the proceeds from the 2011 Credit Card Offering to invest in advertising and marketing programs to support our direct-to-consumer business, purchase inventory, provide other general working capital, and pay commissions and expenses related to the private offering.

As of September 13, 2012, the remaining balance and accrued interest on the 2011 Credit Card Notes were repaid in full.

Notes Payable – 2012 Credit Card Receipts-Backed Notes

On September 14, 2012, we closed on the private sale of \$1,285,722 in Series 2012CC 15% secured promissory notes backed by a portion of our prospective credit card receipts, (the “2012 Credit Card Notes”) and 128,573 shares of common stock (collectively, the “2012 Credit Card Offering”). Consideration for the 2012 Credit Card Offering comprised \$1,285,722 in cash. After deducting \$46,129 of placement agent sales commissions (5% on third-party investors, 3% on company-referred investors and 0% on investments by our officers and directors) and expenses, net cash proceeds to AeroGrow totaled \$1,239,594. In addition, we issued 12,858 shares of common stock to the placement agent as additional sales compensation, representing one share of common stock for every 10 shares issued to investors in the 2012 Credit Card Offering.

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We used the proceeds from the 2012 Credit Card Offering to invest in advertising and marketing programs to support its direct-to-consumer business, purchase inventory, provide other general working capital, repay \$198,406 of the 2011 Credit Card Notes (including accrued interest) and pay commissions and expenses related to the private offering. The issuance of the 2012 Credit Card Offering was conducted in reliance upon exemptions from registration requirements under the Securities Act of 1933 (the “Securities Act”), including, without limitation, those under Rule 506 of Regulation D (as promulgated under the Securities Act). The 2012 Credit Card Offering was offered and sold only to investors who are, or we reasonably believed to be, “accredited investors,” as defined in Rule 501(a) of Regulation D under the Securities Act. Because the 2012 Credit Card Offering has not been registered under the Securities Act, the securities sold in the 2012 Credit Card Offering are “restricted securities” within the meaning of Rule 144 under the Securities Act, and investors will not be able to sell the securities in the United States absent an effective registration statement or an applicable exemption from registration.

Our directors and officers invested \$245,000 in the 2012 Credit Card Offering and were issued 2012 Credit Card Notes with a face amount of \$245,000 and 24,500 shares of common stock. Investors having a beneficial ownership in AeroGrow of more than 5% who are not also directors or officers invested \$350,000 in the 2012 Credit Card Offering and were issued 2012 Credit Card Notes with a face amount of \$350,000 and 35,000 shares of common stock. The investments by the directors, officers, and investors having a beneficial ownership in AeroGrow of more than 5% were on the same terms and conditions as all other investors in the 2012 Credit Card Offering.

The 2012 Credit Card Notes bear interest at 15% per annum and have a final maturity of November 1, 2013. Of our daily credit card receipts, 20% will be held in escrow with First Western Trust Bank under an Escrow and Account Control Agreement to fund bi-weekly payments of principal and interest to the investors in the 2012 Credit Card Offering.

As of March 31, 2013, \$640,373 was outstanding under the 2012 Credit Card Notes, including accrued interest and we were current and in compliance with all terms and conditions.

Pawnee Lease Promissory Note

On November 30, 2011, we executed a promissory note (the “Lease Promissory Note”) in the principal amount of \$116,401 in favor of Pawnee Properties, LLC (“Pawnee”). The Lease Promissory Note details the terms and conditions pursuant to which we will pay to Pawnee past due rent and building operating expenses related to our headquarters lease. The Lease Promissory Note carries an interest rate of 6% per annum for the first twelve months, and 8% per annum thereafter. Payments of principal and interest are due on the first day of each month during the periods: (i) October 2011 through April 2012 (aggregate payments for the period of \$63,320); (ii) May 2012 through April 2013 (aggregate payments for the period of \$110,764); and (iii) May 2013 through April 2014 (aggregate payments for the period of \$114,641), and (iv) May 2014 through September 2014 (aggregate payments for the period of \$48,450). The Lease Promissory Note can be prepaid at any time, at our option, without penalty. In the event of a default in payment, the interest rate would be increased to 15% per annum and Pawnee would have the option to (i) declare the Lease Promissory Note to be immediately payable, or (ii) add the accrued interest to the principal balance. As of March 31, 2013, the outstanding balance of the Lease Promissory Note, including accrued interest, was \$41,514 and we were current and in compliance with all terms and conditions.

Cash Requirements

We generally require cash to:

- fund our operations and working capital requirements,
- develop and execute our product development and market introduction plans,

- execute our sales and marketing plans,
- fund research and development efforts, and
- pay for debt obligations as they come due.

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At this time, we do not expect to enter into additional capital leases to finance major purchases. In addition, we do not currently have any binding commitments with third parties to obtain any material amount of equity or debt financing other than the financing arrangements described in this report.

Assessment of Future Liquidity and Results of Operations

Liquidity

To assess our ability to fund ongoing operating requirements, we developed assumptions regarding operating cash flow. Critical sources of funding, and key assumptions and areas of uncertainty include:

- our cash of \$566,785 (\$42,294 of which is restricted as collateral for our various corporate obligations) as of March 31, 2013;
- the increase in our cash balance as of June 15, 2013 to \$3,414,966 (\$15,014 of which is restricted as collateral for our various corporate obligations), primarily resulting from the sale of convertible preferred stock and intellectual property to Scotts Miracle-Gro on April 22, 2013 (as discussed below and in Note 8 “Subsequent Events” to our financial statements);
 - continued support of, and extensions of credit by, our suppliers and lenders;
- our historical pattern of increased sales between September and March, and lower sales volume from April through August;
 - the level of spending necessary to support our planned initiatives; and
- our sales to consumers, retailers, and international distributors, and the resulting cash flow from operations, which will depend in great measure on the success of the planned direct-to-consumer sales initiatives.

During Fiscal 2012 and Fiscal 2013 we took a number of actions to address our liquidity issues. Specifically, we re-focused our efforts on building our direct-to-consumer business, which we believe carries higher margin opportunities than our retailer business. We also reduced the number of retailers that carry our products in order to focus on those retailers that have proven to be the best and most profitable business partners.

In Fiscal 2012, we restructured the amounts and payment timing of certain of our accounts payable, issued \$1.6 million in 2011 Credit Card Notes (as described above), restructured the payment schedule for the Revised Main Power Note, and received approval from our shareholders and affected creditors to convert our Series A Preferred Stock and Subordinated Secured Convertible Notes into common stock.

In Fiscal 2013, we offered our warrant holders the opportunity to exercise their warrants at a reduced price, and raised \$1.59 million in common equity capital.

On April 23, 2013, during the first fiscal quarter of the year ended December 31, 2014, the Company entered into a Securities Purchase Agreement with a wholly owned subsidiary of Scotts Miracle-Gro. Pursuant to the Securities Purchase Agreement, Scotts Miracle-Gro acquired the following securities for an aggregate purchase price of \$4,000,000; (i) 2,649,007 shares of our Series B Convertible Preferred Stock, par value \$0.001 per share, and (ii) a warrant to purchase shares of our common stock. After deducting offering expenses, including commissions and expenses paid to the Company’s advisor, net cash proceeds to the Company totaled to \$3,830,000. In addition, we also agreed to sell all intellectual property associated with our Hydroponic IP, other than the AeroGrow and AeroGarden trademarks, to Scotts Miracle-Gro for \$500,000. Please see Note 8 “Subsequent Events” to our financial statements. Finally, we repaid the outstanding balance on the MainPower Promissory Note, which outstanding, including all accrued interest, which totaled to \$1,703,764 as of March 31, 2013, was paid in full for \$950,000.

Based on these facts and assumptions, we believe our existing cash and cash equivalents, along with the cash generated by our anticipated results from operations, will be sufficient to meet our needs for the next twelve months.

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Results of Operations

There are several factors that could affect our future results of operations. These factors include, but are not limited to, the following:

- the effectiveness of our consumer marketing efforts in generating both direct-to-consumer sales, and sales to consumers by our retailer customer,
 - uncertainty regarding the impact of macroeconomic conditions on consumer spending,
- uncertainty regarding the capital markets and our access to sufficient capital to support our current and projected scale of operations,
- the seasonality of our business, in which we have historically experienced higher sales volume during the fall and winter months (September through March),
 - a continued, uninterrupted supply of product from our third-party manufacturing suppliers in China, and
 - the success of the Scotts Miracle-Gro relationship.

Off-Balance Sheet Arrangements

We do not have current commitments under capital leases and have not entered into any contracts for financial derivative such as futures, swaps, and options.

Obligations and Commitments

As part of our ongoing operations, we enter into arrangements that obligate us to make future payments under contracts, such as leases and the timing and effect that such commitments are expected to have on our liquidity and cash flow in future periods. The following is a summary of these obligations as of March 31, 2013.

	Less than 1 year	1 -3 years	More than 3 years	Total
Operating leases	\$ 234,312	\$ 68,140	\$ -	\$ 302,452
Notes payable and long-term debt	1,539,771	1,226,772	-	2,708,483
Totals:	\$ 1,774,083	\$ 1,294,912	\$ -	\$ 3,010,935

See Note 2 and Note 6 to our financial statements for additional information related to our notes payable and long term debt and operating leases, respectively.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Risk

Our interest income is most sensitive to fluctuations in the general level of U.S. interest rates. As such, changes in U.S. interest rates affect the interest earned on our cash, cash equivalents, and short-term investments, and the value of those investments. Due to the short-term nature of our cash equivalents and investments, we have concluded that a change in interest rates does not pose a material market risk to us with respect to our interest income. Our debt carries fixed interest rates and therefore changes in the general level of market interest rates will not impact our interest expense during the terms of our existing debt arrangements.

Foreign Currency Exchange Risk

We transact business in primarily in U.S. currency. Although we purchase our products in U.S. dollars, the prices charged by our China factories are predicated upon their cost for components, labor and overhead. Therefore, changes in the valuation of the U.S. dollar in relation to the Chinese currency may cause our manufacturers to raise prices of our products which could reduce our profit margins.

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In future periods, it is possible that we could be exposed to fluctuations in foreign currency exchange rates on accounts receivable from sales and net monetary assets denominated in foreign currencies and liabilities. To date, however, virtually all of our transactions have been denominated in U.S. dollars.

ITEM 8. FINANCIAL STATEMENTS

Our financial statements appear in a separate section at the end of this Annual Report. Such information is incorporated herein by reference.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

On November 17, 2011, Eide Bailly LLP (“Eide Bailly”) resigned as the independent registered public accounting firm of the Company. Eide Bailly had been the independent registered public accounting firm of the Company since November 1, 2008. Gordon, Hughes & Banks, LLP, whose operations were acquired by Eide Bailly on November 1, 2008, had served as the independent registered public accounting firm of the Company from our inception through November 1, 2008.

The audit report of Eide Bailly on the financial statements of the Company as of and for the years ended March 31, 2011 did not contain an adverse opinion or disclaimer of opinion, nor were they qualified or modified as to uncertainty, audit scope or accounting principles, except as follows noted below.

Eide Bailly’s report on the financial statements of the Company as of and for the year ended March 31, 2011 contained a separate paragraph stating:

“The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1, the Company does not currently have sufficient liquidity to meet its anticipated working capital, debt service and other liquidity needs in the near term. These conditions raise substantial doubt about our ability to continue as a going concern. Management’s plans in regard to these matters are also described in Note 1 to the financial statements. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.”

In connection with the audit of the years ended March 31, 2011, and through to November 17, 2011, there were no disagreements between the Company and Eide Bailly on any matter of accounting principles or practices, financial statement disclosure or auditing scope or procedure, which disagreements, if not resolved to the satisfaction of Eide Bailly, would have caused Eide Bailly to make reference to the subject matter of the disagreement in connection with its report on our financial statements.

During the audit of the years ended March 31, 2011 and through to November 17, 2011, there were no “reportable events” with respect to the Company as that term is defined in item 304(a)(1)(v) of Regulation S-K under the Securities Exchange Act of 1934, as amended (“Regulation S-K”).

We provided a copy of the foregoing disclosures to Eide Bailly and requested that Eide Bailly furnish it with a letter addressed to the Securities and Exchange Commission stating whether or not it agrees with the above statements. A copy of that letter furnished in response to that request was filed as Exhibit 16.1 to our Form 8-K filed with the SEC on November 23, 2011.

On November 22, 2011, we executed an engagement letter with EKS&H LLLP (“EKS&H”) to assume the role of our independent registered public accounting firm.

During audit of the years ended March 31, 2011 and the subsequent interim period prior to the engagement of EKS&H, neither we nor anyone on our behalf consulted EKS&H regarding: (i) the application of accounting principles to any specified transaction, either completed or proposed; (ii) the type of audit opinion that might be rendered on our financial statements; or (iii) any matter that was the subject of a disagreement or reportable event as defined in Regulation S-K, Item 304(a)(1)(iv) and Item 304(a)(1)(v), respectively.

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The decision to appoint EKS&H as our independent registered public accounting firm was approved by the Audit Committee of the Board of Directors and ratified by the full Board of Directors on November 21, 2011.

ITEM 9A. CONTROLS AND PROCEDURES

We conducted an evaluation under the supervision and with the participation of our management, including our Chief Executive Officer and Vice President, Accounting, of the effectiveness of the design and operation of our disclosure controls and procedures. The term “disclosure controls and procedures,” as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by the company in the reports it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission’s rules and forms. Disclosure controls and procedures also include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company’s management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. Based on our assessment, management has concluded that, as of March 31, 2013, our disclosure controls and procedures were effective.

Management’s Report on Internal Control Over Financial Reporting

Management assessed the effectiveness of our internal control over financial reporting as of March 31, 2013. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations (“COSO”) of the Treadway Commission’s Internal Control-Integrated Framework.

Based on our assessment, management has concluded that, as of March 31, 2013, our internal control over financial reporting was effective based on those criteria.

Management is responsible for establishing and maintaining adequate internal controls over financial reporting. Internal control over financial reporting is defined in Rule 13a-15(f) and 15d-15(f), promulgated under the Securities Exchange Act of 1934, as a process designed by, or under the supervision of, our principal executive and principal financial officers and effected by our board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

- Pertain to the maintenance of records that in reasonable detail accurately and fairly reflect transactions and dispositions of the assets;
- Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures are being made only in accordance with authorizations of our management and directors; and
 - Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Internal control over financial reporting cannot provide absolute assurance of achieving financial reporting objectives because of its inherent limitations. Internal control over financial reporting is a process that involves human diligence and compliance and is subject to lapses in judgment and breakdowns resulting from human failure. Internal control over financial reporting can also be circumvented by collusion or improper management override. Because of such limitations, there is a risk that material misstatements may not be prevented or detected on a timely basis by internal control over financial reporting. However, these inherent limitations are known features of the financial reporting process. Therefore, it is possible to design into the process safeguards to reduce, though not eliminate, this risk.

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Attestation Report of the Independent Registered Public Accounting Firm

This Annual Report does not include an attestation report of our independent registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by our independent registered public accounting firm pursuant to rules of the SEC that permit us to provide only management's report in this Annual Report.

Changes in Internal Control over Financial Reporting

There have been no changes in our internal control over financial reporting during the fourth quarter of fiscal year ended March 31, 2013 that have or are reasonably likely to materially affect our internal control over financial reporting identified in connection with the previously mentioned evaluation.

ITEM 9B. OTHER INFORMATION

None.

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PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Executive Officers

The following sets forth certain information with respect to our executive officers and significant employees, as of the filing date of this report. All of our officers and employees serve at the pleasure of the Board or until their successors are elected and qualified.

Name	Age	Position with AeroGrow
J. Michael Wolfe	54	President, Chief Executive Officer and Director
Grey H. Gibbs	46	Vice President - Accounting
John K. Thompson	52	SVP, Sales & Marketing and Secretary

J. Michael Wolfe, age 54, has been a director since February 2011. Mr. Wolfe became our Chief Operating Officer in January 2010, our President on February 9, 2011, and our Chief Executive Officer on March 31, 2011. He previously served as Vice President of Operations since April 2006. Prior to joining AeroGrow, Mr. Wolfe was an independent consultant. From 1992 to 2002, he was President and Chief Operating Officer of Concepts Direct and was its Chief Executive Officer from 2000 to 2001. At Concepts Direct, Mr. Wolfe oversaw the development, launch and operations of seven independent catalogs. From 1987 to 1992, Mr. Wolfe served as Vice President of database management company Wiland Services, Inc, where he oversaw the redesign of the company's product line, its sales and investor relations. Mr. Wolfe's leadership experience, combined with his extensive direct response marketing background, his executive experience at a variety of direct response companies, and his knowledge of AeroGrow's history and business, led the Board to conclude that he should serve as a director.

Grey H. Gibbs, age 46, has been with AeroGrow since November of 2007. He was named Vice President – Accounting in February 2011. From 2006 to 2011, Mr. Gibbs was Director of Sarbanes-Oxley Compliance, and from 2004 to 2006, Assistant Corporate Controller, of Swift & Company, an animal protein processor. From 2003 to 2004, Mr. Gibbs was the Chief Financial Officer of JCIT International, a educational and consulting firm in lean manufacturing. From 1994 to 2002, Mr. Gibbs served in a range of strategic and financial roles for Agilent Technologies and Hewlett Packard, including New Product Introduction Program Manager, Outsourcing Program Manager, Site Finance Manager, Planning and Reporting Analyst and Senior Internal Auditor. Mr. Gibbs was also an Audit Supervising Senior for KPMG LLP from 1991 to 1994.

John K. Thompson, age 52, became Senior Vice President of Sales and Marketing on January 14, 2010. Mr. Thompson joined AeroGrow in 2002 and has served in a variety of senior management positions at AeroGrow, including his most recent position as Vice President of Marketing, which he assumed in October 2009. Mr. Thompson also served as the Company's International Division General Manager and Vice President of Investor Relations, and was instrumental in the research activities leading up to the development and launch of the Company's AeroGarden product line. Prior to joining AeroGrow, Mr. Thompson was Director of Marketing for Productivity Point International, a direct marketing and direct sales company, and Sales and Marketing Manager for CareerTrack, a direct marketing company that sold personal and professional growth products to the consumer and commercial markets.

Board of Directors

Our Board of Directors oversees the management of AeroGrow on your behalf. Among other things, the Board reviews our long-term strategic plans and exercises direct decision-making authority on key issues, including the appointment of our executive officers and setting the scope of their authority in managing AeroGrow's day-to-day operations. Our Board is currently comprised of Jack J. Walker (Chairman), Michael S. Barish, Wayne E. Harding III, and J. Michael Wolfe. Biographical information about Messrs. Clarke and Wolfe is contained above under the caption heading "Executive Officers." Biographical information for Messrs. Barish, Harding and Walker is presented below.

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Jack J. Walker, age 78, has been a director since February 2006, and became Chairman of the Board in July 2008. Mr. Walker served as President from January 2010 until February 9, 2011 and as our Chief Executive Officer from January 2010 until March 31, 2011. Mr. Walker has been the Managing Member of Walker Enterprises LLLP, and its predecessors, a real estate investment and development company, since 1980. During that time he has developed in excess of \$500 million of commercial real estate in California, Colorado, Arizona and Texas. He serves on the Board of Pathogen Systems, Inc. and is an advisor to several start-up companies. Mr. Walker is an English Solicitor and began his career in 1956 in London, England. In 1968, Mr. Walker founded English & Continental Property Company, and served as Joint Managing Director of this commercial property development company, which operated in Europe with over 200 staff, until its sale to the Post Office Pension Fund in 1973. From 1973, Mr. Walker controlled several English listed companies, including Charles Spreckly Industries, Town & Commercial Properties and Associated Development Holdings, with worldwide interests and over 3,500 employees. Mr. Walker served as a director of supermarket group Megafoods Stores, Inc. from 1987 to 1993, and was Chief Financial Officer for part of that time. Mr. Walker serves as a director of and advisor to various civic and charitable organizations. Mr. Walker's extensive executive leadership experience, combined with his international and entrepreneurial business background and broad range of knowledge of AeroGrow's history and business, among other factors, led the Board to conclude that he should serve as a Director and Chairman of the Board.

Michael S. Barish, age 73, has been a director since July 2009. Mr. Barish co-founded Lazarus Investment Partners LLLP, a private investment partnership focused on microcap stocks, in 2003, and served as the fund's Chief Investment Officer until his retirement in June 2009. In 1973, Mr. Barish founded Cambiar Investors and grew the firm's assets from less than \$1 million in 1973 to over \$2.3 billion upon his retirement in 2001. Mr. Barish's experience as a chief investment officer, particularly his specialized focus on microcap stocks, led the Board to conclude that he should serve as a director.

Chris J. Hagedorn, age 28, has been a director since April 2013. Mr. Hagedorn was appointed the Director of Indoor Gardening at Scotts Miracle-Gro in May of 2013. From 2011 to 2013, Mr. Hagedorn served as a Marketing Manager for the North Region at Scotts Miracle-Gro. Between 2007 and 2010, Mr. Hagedorn served as a Copywriter at ML Rogers Agency after graduation with a bachelor's degree from Bowdoin College. Mr. Hagedorn was appointed to the Board by Scotts Miracle-Gro pursuant to a condition to the Securities Purchase Agreement between AeroGrow and Scotts Miracle-Gro which allows Scotts Miracle-Gro, as holder of the Series B Preferred Convertible Stock, to appoint one member to the Board of Directors for so long as the Warrant remains outstanding. For more details regarding the Securities Purchase Agreement, the Series B Preferred Stock, the Warrant, and related agreements, refer to Note 8. "Subsequent Events" to our financial statements. Mr. Hagedorn's business experience and ties to Scotts Miracle-Gro, particularly in light of AeroGrow's strategic alliance with Scotts Miracle-Gro, led the Board to conclude that he should serve as a director. Mr. Hagedorn is the son of James Hagedorn, the Chief Executive Officer and Chairman of the Board of The Scotts Miracle-Gro Company (NYSE: "SMG").

Wayne E. Harding III, age 58, has been the Chief Financial Officer of Two Rivers Water & Farming Company ("Two Rivers"), a publicly traded company (OTC QB: TURV) that acquires and develops high yield irrigated farmland and the associated water rights in the western United States, since September 2009, and previously served as the controller of Two Rivers, beginning in July 2008. Prior to joining Two Rivers, Mr. Harding served as vice president business development of Rivet Software since December 2004. Mr. Harding was the principal of Wayne Harding & Company P.C., a financial consulting organization, from August 2002 to December 2004. Mr. Harding was owner and President of Wayne Harding & Company CPAs, and from 2000 until August 2002, he was director-business development of CPA2Biz. Mr. Harding also served on the Board, and was chair of the Governance, Compensation and Nominating Committee and the Audit Committee, for AeroGrow from 2005 – 2007. Mr. Harding holds an active CPA license in Colorado and a CGMA (Charter Global Management Accountant) designation. He received his BS and MBA degrees from the University of Denver. He previously served on the American Institute of CPAs (AICPA) Council, is a past-President of the Colorado Society of CPAs, and was the recipient of the prestigious AICPA Special Recognition

Award for his early involvement in developing the AICPA XBRL project. Mr. Harding also teaches accounting in the University of Denver MBA program. Mr. Harding's experience as a Chief Financial Officer of a public company, as a CPA, and as a former Board member of AeroGrow led the Board to conclude that he should serve as a director.

Board Committees and Meetings

We have established two standing committees so that certain matters can be addressed in more depth than may be possible in a full Board meeting: an Audit Committee and a Governance, Compensation and Nominating Committee. The two committees each operate under a written charter.

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Audit Committee. The current members of our Audit Committee are Mr. Harding (chairman), Mr. Barish, and Mr. Walker. The members were elected to the committee, and the chairman was appointed, by the Board. The Board has determined that Messrs. Harding and Barish are considered “audit committee financial experts,” as defined by Item 407(d)(5)(ii) of Regulation S-K, due to their extensive financial background and experience (as summarized in the biographical information for Messrs. Harding and Barish disclosed above). The Board has affirmatively determined that Mr. Harding is an independent director as defined by applicable securities law and NASDAQ corporate governance guidelines. Due to their positions as significant stockholders of AeroGrow, Mr. Walker and Mr. Barish are not independent directors. The Audit Committee’s charter provides that the committee shall:

- oversee the accounting and financial reporting processes and audits of the financial statements;
- assist the Board with oversight of the integrity of our financial statements, our compliance with legal and regulatory requirements, our independent auditors’ qualifications and independence, and the performance of the independent auditors; and
- provide the Board with the results of its monitoring.

Governance, Compensation and Nominating Committee. The current members of the Governance, Compensation and Nominating Committee are Mr. Walker (chairman) and Mr. Barish. The members were elected to the committee, and the chairman was appointed, by the Board. The Governance, Compensation and Nominating Committee’s charter provides that the committee shall:

- recommend to the Board the corporate governance guidelines to be followed;
- review and recommend the nomination of Board members;
- set the compensation for the chief executive officer and other officers; and
- administer the equity-based performance compensation plans of AeroGrow.

The Governance, Compensation and Nominating Committee does not have a formal policy concerning stockholder recommendations to the Board of Directors and we did not receive any recommendations from stockholders requesting that the Board consider a candidate for inclusion as a nominee. The Committee has determined that it is appropriate to not have such a policy given the infrequency of such recommendations. The absence of such a policy does not mean, however, that a recommendation would not have been considered had one been received. The Committee would consider any candidate proposed in good faith by a stockholder on the same basis as a candidate proposed directly by the Board. To do so, a stockholder should send the candidate’s name, credentials, contact information, and his or her consent to be considered as a candidate to the Governance, Compensation and Nominating Committee, c/o Corporate Secretary, AeroGrow International, Inc., 6075 Longbow Drive, Boulder, Colorado, 80301. The proposal should be received by the due date for a stockholder proposal, as set forth below under the caption heading “Submission of Stockholder Proposals,” in order to be considered timely for consideration at the Annual Meeting of Stockholders or, in lieu of an annual meeting, for an action by written consent of the stockholders. The proposing stockholder should also include his or her contact information and a statement of his or her share ownership (how many shares owned and for how long).

In evaluating director nominees, the Governance, Compensation and Nominating Committee considers the appropriate skills and personal characteristics needed in light of the makeup of the current Board, including considerations of character, background, professional experience, education, skill, qualifications for committee membership, independence, race, gender, national origin, differences in viewpoint, and other individual qualities and attributes.

Other than the foregoing, there are no stated minimum criteria for director nominees, although the Committee may also consider such other factors as it may deem are in the best interests of the AeroGrow and its stockholders. The Committee does, however, believe it is appropriate for a member or members of AeroGrow's management to participate as members of the Board.

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The Governance, Compensation and Nominating Committee identifies nominees by first evaluating the current members of the Board willing to continue in service. Current members of the Board with skills and experience that are relevant to our business and who are willing to continue in service are considered for re-nomination. If any member of the Board does not wish to continue in service or if the Board decides not to re-nominate a member for re-election, the Committee then identifies the desired skills and experience of a new nominee in light of the criteria above. Current members of the Board would be polled for suggestions as to individuals meeting the criteria described above. The Committee may also engage in research to identify qualified individuals. To date, we have not engaged third parties to identify or evaluate or assist in identifying potential nominees, although we reserve the right in the future to retain a third-party search firm, if appropriate.

Meetings. During the fiscal year ended March 31, 2013 the Board held nine meetings. Each director attended all of the meetings held by the Board during the period that he served as a director of AeroGrow. Also during the fiscal year ended March 31, 2013, the Audit Committee held four meetings and the Governance, Compensation and Nominating Committee held two meetings. Each committee member attended all of the committee meetings held during the period that he served as a committee member.

The Company encourages all incumbent directors, as well as all nominees for election as director, to attend the annual stockholder meetings, but they are not required to do so. We did not hold an annual meeting last year.

Code of Ethics

The Board of Directors has adopted a Code of Ethics to provide guidance to all of our directors, officers and employees, including our principal executive officer, principal financial and accounting officers, and persons performing similar functions. The Code of Ethics is posted on our website at www.aerogrow.com, and may be found by linking to “Investors” and then “Code of Ethics.” We intend to satisfy the disclosure requirement under Item 5.05 of Form 8-K regarding an amendment to, or waiver from, a provision of this code of ethics by posting such information on our Website.

Board Structure and Risk Oversight

Jack J. Walker serves as the Chairman of the Board and J. Michael Wolfe serves as President and Chief Executive Officer. Mr. Walker is one of the largest investors in AeroGrow and his financial support has been instrumental in allowing AeroGrow to persevere through a very difficult economic period. He is involved in helping set the strategic direction for the Company. Mr. Wolfe has responsibility for our day-to-day operations, as well as for helping set our strategic directions.

Our Board has overall responsibility for risk oversight. Throughout the year, the Board dedicates a portion of their meetings to review and discuss specific risk topics in greater detail. Strategic and operational risks are presented and discussed in the context of the President’s report on operations to the board of directors at regularly scheduled board meetings and at presentations to the board of directors by our other employees and consultants. The Boards’ risk oversight process builds upon management’s risk assessment and mitigation processes. The small size of AeroGrow allows our board of directors to develop in-depth knowledge of different facets of the business. This in-depth knowledge, coupled with exposure to and frequent communication with our management, assists the board of directors in performing its oversight responsibilities, including risk management, in an effective manner.

Communications with the Board of Directors

Stockholders and other interested parties may communicate with the Board or any individual director, by writing to:

AeroGrow International, Inc.
Attention: Board of Directors
c/o Corporate Secretary
6075 Longbow Drive, Suite 200
Boulder, Colorado 80301

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If the letter is from a stockholder, the letter should state that the sender is a stockholder. Under a process approved by the Board, depending on the subject matter, management will:

- forward the letter to the director or directors to whom it is addressed; or
- attempt to handle the matter directly (as where information about our business or our stock is requested); or
- not forward the letter if it is primarily commercial in nature or relates to an improper or irrelevant topic.

A summary of all relevant communications that are received after the last meeting of the full Board and which are not forwarded will be presented at each Board meeting along with any specific communication requested by a director.

All communications will be handled in a confidential manner, to the degree the law allows. Communications may be made on an anonymous basis; however, in these cases the reporting individual must provide sufficient details for the matter to be reviewed and resolved. The Company will not tolerate any retaliation against an employee who makes a good faith report.

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act of 1934 (the “Exchange Act”) requires our executive officers and directors, and persons who own more than 10% of our common stock (herein collectively, our “Section 16 insiders”) to file with the SEC certain forms reporting their ownership and changes in beneficial ownership of our common stock and other equity with the SEC, and to furnish us with copies of these filings.