

Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

WORKFLOW MANAGEMENT INC  
Form 10-Q  
December 15, 2003

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

Form 10-Q

(Mark One)

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

For the quarterly period ended October 31, 2003

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_.

Commission File Number 0-24383

WORKFLOW MANAGEMENT, INC.

(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization.)

06-1507104  
(I.R.S. Employer  
Identification No.)

240 Royal Palm Way  
Palm Beach, FL  
(Address of principal executive offices)

33480  
(Zip Code)

(561) 659-6551  
(Registrant's telephone number, including area code)

N/A  
(Former name, former address and former fiscal year, if changed since  
last report)

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 X No .

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes No X

--- ---

As of December 12, 2003, there were 13,414,125 shares of common stock outstanding.

WORKFLOW MANAGEMENT, INC.

# Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

## INDEX

### PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

Consolidated Balance Sheet.....	
October 31, 2003 (unaudited) and April 30, 2003	
Consolidated Statement of Operations (unaudited).....	
For the three and six months ended October 31, 2003 and October 31, 2002	
Consolidated Statement of Cash Flows (unaudited).....	
For the six months ended October 31, 2003 and October 31, 2002	
Notes to Consolidated Financial Statements (unaudited).....	

Item 2. Management's Discussion and Analysis of Financial Condition  
and Results of Operations.....

Item 3. Quantitative and Qualitative Disclosure About Market Risk.....

Item 4. Controls and Procedures.....

### PART II - OTHER INFORMATION

Item 6. Exhibits and Reports on Form 8-K.....

Signatures.....

### PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

WORKFLOW MANAGEMENT, INC.  
CONSOLIDATED BALANCE SHEET  
(In thousands, except share amounts)

	October 31, 2003
ASSETS	-----
	(Unaudited)
Current assets:	
Cash and cash equivalents	\$ 2,427
Accounts receivable, less allowance for doubtful accounts of \$3,818 and \$3,455, respectively	86,783
Inventories	44,743
Assets of businesses held for sale	
Short-term deferred income taxes	7,760
Prepaid expenses and other current assets	10,206
	-----
Total current assets	151,919

Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

Property and equipment, net	36,691
Goodwill	113,531
Other intangible assets, net	1,294
Long-term deferred income taxes	9,239
Other assets	4,643
	-----
Total assets	\$ 317,317
	=====

LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities:	
Short-term debt	\$ 154,091
Accounts payable	38,562
Accrued compensation	10,460
Accrued additional purchase consideration	4,839
Accrued restructuring costs	2,108
Liabilities of businesses held for sale	
Short-term swap liability	2,508
Other accrued liabilities	19,577
	-----
Total current liabilities	232,145

Long-term credit facility	
Other long-term debt	1,147
Deferred income taxes	5,573
Other long-term liabilities	8,517
	-----
Total liabilities	247,382
	-----

Stockholders' equity:	
Preferred stock, \$.001 par value, 1,000,000 shares authorized, none outstanding	
Common stock, \$.001 par value, 150,000,000 shares authorized, 13,414,125 and 13,359,164 shares, respectively, issued and outstanding	13
Additional paid-in capital	53,491
Notes receivable from officers	(40)
Accumulated other comprehensive income (loss)	533
Retained earnings	15,938
	-----
Total stockholders' equity	69,935
	-----
Total liabilities and stockholders' equity	\$ 317,317
	=====

See accompanying notes to consolidated financial statements.

WORKFLOW MANAGEMENT, INC.  
CONSOLIDATED STATEMENT OF OPERATIONS  
(In thousands, except per share amounts)  
(Unaudited)

	Three Months Ended	Six Mon
	-----	-----
	October 31,	October 31,
		October 31,

Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

	2003 -----	2002 -----	2003 -----
Revenues	\$ 148,194	\$ 159,201	\$ 291,097
Cost of revenues	106,701	114,399	211,476
Gross profit	41,493	44,802	79,621
Selling, general and administrative expenses	33,733	35,868	67,231
Restructuring costs			1,021
Severance and other employment costs			(2,239)
Operating income	7,760	8,934	13,608
Interest expense	4,440	5,860	8,754
Interest income	(29)	(123)	(67)
Loss on ineffective interest rate hedge	105	1,106	124
Financing fees and other bank related costs	661	810	661
Abandoned debt offering costs		174	
Other expense (income)	58	(3)	(25)
Income (loss) from continuing operations before provision (benefit) for income taxes	2,525	1,110	4,161
Provision (benefit) for income taxes	1,439	457	2,378
Income (loss) from continuing operations	1,086	653	1,783
Discontinued operations:			
(Loss) income from discontinued operations		(235)	(2,171)
(Benefit) provision for income taxes		(99)	(912)
(Loss) income from discontinued operations		(136)	(1,259)
Net income (loss)	\$ 1,086	\$ 517	\$ 524
Net income (loss) per share:			
Basic:			
Income (loss) from continuing operations	\$ 0.08	\$ 0.05	\$ 0.13
(Loss) income from discontinued operations		(0.01)	(0.09)
Net income (loss)	\$ 0.08	\$ 0.04	\$ 0.04
Diluted:			
Income (loss) from continuing operations	\$ 0.08	\$ 0.05	\$ 0.13
(Loss) income from discontinued operations		(0.01)	(0.09)
Net income (loss)	\$ 0.08	\$ 0.04	\$ 0.04
Weighted average common shares outstanding:			
Basic	13,396	13,194	13,382
Diluted	13,534	13,224	13,474

See accompanying notes to consolidated financial statements.

WORKFLOW MANAGEMENT, INC.  
CONSOLIDATED STATEMENT OF CASH FLOWS  
(In thousands)  
(Unaudited)

	Six Months E 2003
	-----
Cash flows from operating activities:	
Net income (loss)	\$ 524
Adjustments to reconcile net income to net cash provided by operating activities:	
Depreciation and amortization expense	4,606
Restructuring costs, net of cash paid	(351)
Amortization of deferred financing costs	1,624
Loss on ineffective swap	124
Loss on abandoned debt offering	
Loss from discontinued operations	2,171
Change in assets and liabilities held for sale, net	651
Changes in assets and liabilities:	
Accounts receivable	4,830
Inventories	5,769
Prepaid expenses and other assets	(1,716)
Accounts payable	2,444
Accrued liabilities	(5,877)
	-----
Net cash provided by operating activities	14,799
	-----
Cash flows from investing activities:	
Cash paid in acquisitions	(48)
Cash paid for additional purchase consideration	(6,286)
Cash proceeds from the sale of discontinued operations	5,000
Additions to property and equipment	(1,948)
Other	40
	-----
Net cash used in investing activities	(3,242)
	-----
Cash flows from financing activities:	
Proceeds from credit facility borrowings	48,139
Payments of credit facility borrowings	(59,713)
Payments of other debt	(314)
Payment of abandoned debt offering costs	
Payment on cash settlement of interest rate swap	(1,879)
Payments of deferred financing costs	(742)
Other	170
	-----
Net cash (used in) provided by financing activities	(14,339)
	-----
Effect of exchange rates on cash and cash equivalents	217
	-----
Net (decrease) increase in cash and cash equivalents	(2,565)
Cash and cash equivalents at beginning of period	4,992
	-----

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

Cash and cash equivalents at end of period	\$	2,427
=====		
Supplemental disclosures of cash flow information:		
Interest paid	\$	6,077
Income taxes paid	\$	1,779

### Non-cash transactions:

- o During the six months ended October 31, 2003 and October 31, 2002, the Company accrued \$3,656 and \$3,940 for additional purchase consideration for earn-outs, respectively.
- o During the six months ended October 31, 2003, the Company recorded additional paid-in capital of \$2 relating to the tax benefit of stock options exercised.

See accompanying notes to consolidated financial statements.

5

WORKFLOW MANAGEMENT, INC.  
CONSOLIDATED STATEMENT OF CASH FLOWS  
(In thousands)  
(Unaudited)

### NOTE 1 - NATURE OF BUSINESS

-----

Workflow Management, Inc. (the "Company" or "Workflow Management") is one of the largest distributors of printed business products in North America and is also a leading provider of end-to-end business management outsourcing solutions, which include vendor-neutral custom print sourcing, consulting and integrated storage and distribution services, that allow its customers to control all of their print-related costs. The Company produces and distributes a full range of printed business products and provides related management services to approximately 31,000 customers in North America ranging in size from small businesses to Fortune 100 companies. Workflow Management provides customers with an integrated set of services and information tools that reduce the costs of procuring, storing, distributing and using printed business products and produces custom business documents, envelopes, direct mail and commercial printing. The Company employs approximately 2,700 persons and has 87 facilities located throughout North America.

### NOTE 2 - LIQUIDITY

-----

Effective on August 1, 2003, the Company amended its credit facility (the "Amended Restructured Credit Facility"). Under the terms of the amendment, the Company deferred repayment of the \$50,000 term loan portion of the Amended Restructured Credit Facility until May 1, 2004. In addition, the repayment terms for another term loan and the asset based revolving facility of the Amended Restructured Credit Facility have been accelerated to August 1, 2004. The Company is currently pursuing various strategic and refinancing alternatives that would allow it to repay its obligations under the Amended Restructured Credit Facility by their respective due dates. However, the Company does not have any firm commitments with respect to any potential refinancing or similar

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

transactions, nor does the Company anticipate generating operating cash flows that would allow it to repay these obligations directly. There can be no assurance that the Company will be able to repay its obligations by their respective due dates. In the event that the Company is unable to do so, it will be in default with its lenders under the Amended Restructured Credit Facility. Any such default likely would have a material adverse effect on the Company's business, financial condition and results of operations and the lenders' remedies upon such default would include the right to foreclose on the Company's assets.

### NOTE 3 - BASIS OF PRESENTATION

-----

The accompanying consolidated financial statements and related notes to consolidated financial statements include the accounts of Workflow Management and all of its wholly-owned subsidiaries. All significant intracompany accounts and transactions have been eliminated.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates include allowance for doubtful account and inventory reserves, impairment of property and equipment, impairment of goodwill and realization of deferred tax assets.

6

WORKFLOW MANAGEMENT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In thousands, except per share amounts)  
(Unaudited)

In the opinion of management, the information contained herein reflects all adjustments necessary to make the results of operations for the interim periods a fair presentation of such operations. All such adjustments are of a normal recurring nature. Operating results for interim periods are not necessarily indicative of results that may be expected for the year as a whole. The consolidated financial statements included in this Form 10-Q should be read in conjunction with the Company's audited consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended April 30, 2003.

As used in the Notes to Consolidated Financial Statements, "Fiscal 2003", "Fiscal 2002", "Fiscal 2001" and "Fiscal 1999" refer to the Company's fiscal years ended April 30, 2003, 2002 and 2001 and April 24, 1999, respectively.

### NOTE 4 - INVENTORIES

-----

Inventories consist of the following:

October 31,  
2003

Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

Raw materials.....	\$ 9,17
Work-in-process.....	8,58
Finished goods.....	26,98
	-----
Total inventories	\$ 44,74
	=====

NOTE 5 - PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

	October 31
	2003
	-----
Buildings.....	\$
Furniture and fixtures.....	28,3
Computer equipment and software.....	24,8
Warehouse equipment.....	34,1
Equipment under capital leases.....	1,2
Leasehold improvements.....	12,5
	-----
Less: Accumulated depreciation.....	101,0
	(64,3
	-----
Net property and equipment.....	\$ 36,6
	=====

Depreciation expense for the three months ended October 31, 2003 and October 31, 2002 was \$2,321 and \$2,436, respectively, and for the six months ended October 31, 2003 and October 31, 2002 was \$4,569 and \$4,858, respectively.

7

WORKFLOW MANAGEMENT, INC.  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
 (In thousands, except per share amounts)  
 (Unaudited)

NOTE 6 - DEBT

Revolving Credit Facility

On August 1, 2003, the Company entered into the Amended Restructured Credit Facility with its senior lenders. Under the terms of the Amended Restructured Credit Facility, Term Loan B matures on May 1, 2004 while the asset based facility ("Revolver") and Term Loan A both mature on August 1, 2004.

The Amended Restructured Credit Facility contains a number of affirmative covenants. These covenants include, but are not limited to, the requirement that the Company meet certain leverage ratio, interest coverage ratio, fixed charge ratio and minimum EBITDA thresholds on an ongoing basis. The Revolver contains advance rates of 85% of the Company's eligible accounts receivable, 60% of the Company's eligible inventories (until February 1, 2004 at which time it reduces to 50%) and \$10,000 against the Company's fixed assets. Under the Amended



## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

Restructured Credit Facility, the Company's senior lenders hold warrants for 2,400 shares which would represent approximately 15.2% of the Company's outstanding common stock if the warrants were exercised. Under the terms of the warrant, the first warrant tranche, for 400 shares, would become exercisable on December 31, 2003 unless, by November 30, 2003, the Company had delivered to its senior lenders a plan acceptable to its lenders to repay, in total, all of the outstanding obligations under the Amended Restructured Credit Facility by March 31, 2004. On November 26, 2003, the Company met the plan delivery requirement with its lenders. The lenders have until December 31, 2003 to accept the plan. Additional warrant tranches of 400 shares each become exercisable each month for a period of five months beginning no later than March 31, 2004 but only in the event there remains outstanding indebtedness under the Amended Restructured Credit Facility on the date the tranche becomes exercisable. Each warrant tranche would have an exercise price equal to the fair market value of the Company's common stock on the date the tranche becomes exercisable.

The outstanding balances on the Amended Restructured Credit Facility at October 31, 2003 were as follows:

	Maximum Availability	Amount Outstanding	Applicable Interest Rate
	-----	-----	-----
Revolver	\$ 100,000	\$ 87,220	LIBOR + 5%
Term Loan A	16,313	16,313	LIBOR + 8%
Term Loan B	50,000	50,000	11%, 12%, 13% & 14%
			calendar quarter of
	-----	-----	
	\$ 166,313	\$ 153,533	
	=====	=====	

At October 31, 2003, the Company had \$153,533 outstanding on the Amended Restructured Credit Facility and, in addition, \$3,094 in outstanding letters of credit. The Company's availability under the Restructured Credit Facility at October 31, 2003 was \$9,686 after inclusion of letters of credit.

8

WORKFLOW MANAGEMENT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In thousands, except per share amounts)  
(Unaudited)

### Letters of Credit

The Company has outstanding letters of credit of approximately \$3,094 related to performance and payment guarantees. Based upon the Company's experience with these arrangements, the Company does not believe that any obligations that may arise will be significant.

### Interest Rate Swap

The Company does not hold or issue derivative financial instruments for trading purposes. On May 3, 2001, the Company entered into an interest rate swap agreement (the "Swap") with various lending institutions at no initial cost to the Company with an effective date of August 1, 2001 and an expiration date of

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

March 10, 2004. The Company exchanged its variable interest rate on \$100,000 in credit facility debt for a fixed LIBOR of approximately 5.10% plus the Company's interest rate spread under its prior credit facility. The Swap was entered into to manage interest rate risk on the variable rate borrowings under the Company's revolving credit portion of its debt. This interest rate swap has the effect of locking in, for a specified period, the base interest rate the Company will pay on the \$100,000 notional principal amount established in the Swap. As a result, while this hedging arrangement is structured to reduce the Company's exposure to increases in interest rates, it also limits the benefit the Company might otherwise have received from any decreases in interest rates.

The Company accounted for the Swap under the guidelines of SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." Effective May 1, 2001, the Company implemented SFAS No. 133 as amended. This standard requires companies to record all derivative instruments as assets or liabilities on the balance sheet, measured at fair value. The recognition of gains or losses resulting from changes in the values of those derivative instruments is based on the use of each derivative instrument and whether it qualifies for hedge accounting. The key criterion for hedge accounting is that the hedging relationship must be highly effective in achieving offsetting changes in fair value or cash flows. Under the guidelines of SFAS No. 133, the Company originally classified the Swap as a cash flow hedge. However, on October 16, 2002, the Company's prior credit facility was amended so that borrowings under the credit facility bore a non-LIBOR based fixed interest rate. Thus, under SFAS No. 133 as amended, the Swap underlying this debt became ineffective and could no longer be designated as a cash flow hedge of variable rate debt. This ineffective Swap is cash settled quarterly dependent upon the movement of 3-month LIBOR rates. In measuring the fair value of the Swap at October 31, 2003, the Company recorded a short-term liability of \$2,508. During the six months ended October 31, 2003, the Company paid \$1,879 representing quarterly cash settlement payments. The Company recorded a net loss of \$124 on the ineffective interest rate hedge for the six months ended October 31, 2003.

9

WORKFLOW MANAGEMENT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In thousands, except per share amounts)  
(Unaudited)

NOTE 7 - STOCKHOLDERS' EQUITY  
-----

Changes in stockholders' equity during the six months ended October 31, 2003 were as follows:

Stockholders' equity balance at April 30, 2003	\$	67,866
Issuance of common stock in conjunction with:		
Exercise of stock options, including tax benefits		21
Employee stock purchase program		111
Fees paid to outside members of the Company's Board of Directors		25
Change in balance of notes receivable from directors and officers		13
Value of contingent common stock warrants		142
Comprehensive income		1,757
		-----

Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

Stockholders' equity balance at October 31, 2003 \$ 69,935  
=====

Comprehensive Income

The components of comprehensive income are as follows:

	Three Months Ended		Si
	October 31, 2003	October 31, 2002	October 2003
Net income (loss)	\$ 1,086	\$ 517	\$
Other comprehensive income (loss):			
Unfunded benefit plan obligation, net of tax	(2,935)		(2
Changes in fair market value of financial instruments designated as hedges of interest rate exposure, net of taxes			
Write-off of fair market value of ineffective interest rate hedge, net of tax			
Foreign currency translation adjustment	2,868	197	4
Comprehensive income	\$ 1,019 =====	\$ 714 =====	\$ 1 =====

Notes Receivable from Officers

During Fiscal 2001 and Fiscal 1999, the Company extended unsecured loans to certain members of management and the Board of Directors (the "Director and Officer Notes") for the purchase, in the open market, of the Company's common stock by those individuals. The Director and Officer Notes were full recourse promissory notes bearing interest at 6.75% and 8.0% per annum, respectively, with principal and interest payable at maturity on January 2, 2003 and February 3, 2003. During the year ended April 30, 2003, the Company collected \$4,502 in principal and \$769 in interest as payments on the Director and Officer Notes and charged off \$681 for uncollectible notes. At October 31, 2003, \$40 (net of a \$270 reserve established for uncollectible notes) was outstanding on the Director and Officer notes.

WORKFLOW MANAGEMENT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In thousands, except per share amounts)  
(Unaudited)

NOTE 8 - EARNINGS PER SHARE ("EPS")  
-----

Basic EPS excludes dilution and is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. The following information presents the Company's computations

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

of basic and diluted EPS for the periods presented in the consolidated statement of income:

	Three Months Ended October 31, October 31,		Six Mo October
	2003	2002	2003
Earnings per share:			
Net income (loss) from continuing operations	\$ 1,086	\$ 653	\$ 1,783
Net (loss) income from discontinued operations		(136)	(1,259)
Net income (loss)	\$ 1,086	\$ 517	\$ 524
Weighted average number of			
Common shares outstanding	13,396	13,194	13,382
Potentially dilutive shares*	138	30	92
Total	13,534	13,224	13,474
Basic income (loss) earnings per share:			
Net income (loss) from continuing operations	\$ 0.08	\$ 0.05	\$ 0.13
Net (loss) income from discontinued operations		(0.01)	(0.09)
Net income (loss)	\$ 0.08	\$ 0.04	\$ 0.04
Diluted income (loss) earnings per share:			
Net income (loss) from continuing operations	\$ 0.08	\$ 0.05	\$ 0.13
Net (loss) income from discontinued operations		(0.01)	(0.09)
Net income (loss)	\$ 0.08	\$ 0.04	\$ 0.04

\* The Company had additional employee stock options outstanding during the periods presented that were not included in the computation of diluted earnings per share because they were anti-dilutive. Options to purchase 2,532 and 4,549 shares of common stock were anti-dilutive and outstanding during the six months ended October 31, 2003 and October 31, 2002, respectively.

11

WORKFLOW MANAGEMENT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In thousands, except per share amounts)  
(Unaudited)

NOTE 9 - BUSINESS COMBINATIONS  
-----

During the six months ended October 31, 2003 and Fiscal 2003, the Company did not complete any business combinations.

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

During Fiscal 2002 and Fiscal 2001, the Company made two and eight acquisitions, respectively, accounted for under the purchase method (the "Purchased Companies"). These acquisitions were made in order to expand the Company's presence in the marketplace in which it serves. The results of these acquisitions have been included in the Company's results from their respective dates of acquisition. Initial cash consideration and subsequent acquisition costs paid associated with the acquisition of the Purchased Companies totaled \$6,334, \$8,537, \$17,494 and \$29,989 during the six months ended October 31, 2003, Fiscal 2003, Fiscal 2002 and Fiscal 2001, respectively. The total assets acquired and earn-outs paid in connection with the Purchased Companies during the six months ended October 31, 2003, Fiscal 2003, Fiscal 2002 and Fiscal 2001, were \$6,334, \$8,537, \$18,078 and \$39,431, respectively, including intangible assets of \$6,334, \$8,537, \$16,464 and \$20,282, respectively.

The majority of the Purchased Companies have earn-out provisions that could result in additional purchase consideration payable in subsequent periods, ranging from three to five years, dependent upon the future earnings of these acquired companies. During the six months ended October 31, 2003, Fiscal 2003, Fiscal 2002 and Fiscal 2001, \$6,286, \$7,659, \$9,451 and \$6,614, respectively, of additional purchase consideration was paid by the Company in connection with earn-out provisions and another \$4,839 has been accrued for these earn-out provisions at October 31, 2003. The additional consideration, whether paid or accrued, has been reflected in the accompanying balance sheet as goodwill at October 31, 2003.

### NOTE 10 - RESTRUCTURING COSTS

-----

The Company historically has grown significantly through acquisitions. However, the Company began to implement a new strategic business plan in Fiscal 2003. Under its new strategic plan, the Company has focused on (i) integrating its existing core operations to improve profitability and (ii) divesting non-core operations to pay down debt. The Company did not consummate any acquisitions during the six months ended October 31, 2003 or in Fiscal 2003 and does not anticipate pursuing or consummating acquisitions in the near future.

During the six months ended October 31, 2003, the Company recorded a restructuring charge of \$1,021 in connection with its consolidation of envelope printing facilities in the New York area. The costs mainly were comprised of future rental payments for a facility the Company vacated in May 2003.

During the six months ended October 31, 2002, the Company reversed into income a \$1,242 restructuring charge taken in the three months ended April 30, 2001 that was no longer required since the Company settled the underlying contract dispute and expensed \$1,463 in strategic restructuring costs associated with the exploration of other financial, restructuring and strategic alternatives.

WORKFLOW MANAGEMENT, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(In thousands, except per share amounts)  
(Unaudited)

Under the restructuring plan implemented during Fiscal 2003, the Company terminated and provided severance benefits to 37 employees. However, certain severed employees have delayed severance payments. The majority of the workforce reductions were within the production area and administration.

Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

The following table sets forth the Company's accrued restructuring costs for the six months ended October 31, 2003.

	Facility Closure and Consolidation	Severance and Terminations
	-----	-----
Balance at April 30, 2003.....	\$ 206	\$ 1,845
Additions.....	1,021	
Utilizations.....	(658)	(703)
	-----	-----
Balance at October 31, 2003.....	\$ 569	\$ 1,142
	=====	=====

NOTE 11 - GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill consists of the following:

Balance at April 30, 2003 .....	\$ 109,515
Additions.....	4,080
Disposals.....	(64)
	-----
Balance at October 31, 2003.....	\$ 113,531
	=====

Intangible assets subject to amortization consist of the following:

	October 31, 2003	April 30, 2003
	-----	-----
Customer lists.....	\$ 1,327	\$ 1,302
Non-compete agreements.....	398	398
Other .....	664	664
	-----	-----
	2,389	2,364
Less: Accumulated amortization.....	(1,095)	(1,057)
	-----	-----
Net intangible assets.....	\$ 1,294	\$ 1,307
	=====	=====

NOTE 12 - SEGMENT REPORTING

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

The Company transacts business in the United States, Canada and Puerto Rico. The Company does not allocate corporate overhead by segment in assessing performance. Corporate expenses and overhead included within the operating income of the Company's United States operations totaled \$1,364 and \$1,371 for the three months ended October 31, 2003 and October 31, 2002, respectively, and \$545 and \$3,774 for the six months ended October 31, 2003 and October 31, 2002, respectively.

The following table sets forth information as to the Company's operations in its different geographic segments:

	Three Months Ended		Six Mon
	October 31, 2003	October 31, 2002	October 31, 2003
<b>Revenues:</b>			
<hr style="border-top: 1px dashed black;"/>			
United States.....	\$ 106,902	\$ 122,978	\$ 209,438
Canada.....	38,765	33,612	76,500
Puerto Rico.....	2,527	2,611	5,159
	<hr style="border-top: 1px dashed black;"/>	<hr style="border-top: 1px dashed black;"/>	<hr style="border-top: 1px dashed black;"/>
Total.....	\$ 148,194	\$ 159,201	\$ 291,097
	<hr style="border-top: 3px double black;"/>	<hr style="border-top: 3px double black;"/>	<hr style="border-top: 3px double black;"/>
	Three Months Ended		Six Mon
	October 31, 2003	October 31, 2002	October 31, 2003
<b>Operating Income:</b>			
<hr style="border-top: 1px dashed black;"/>			
United States.....	\$ 3,961	\$ 5,851	\$ 6,713
Canada.....	3,722	2,968	6,605
Puerto Rico.....	77	115	290
	<hr style="border-top: 1px dashed black;"/>	<hr style="border-top: 1px dashed black;"/>	<hr style="border-top: 1px dashed black;"/>
Total.....	\$ 7,760	\$ 8,934	\$ 13,608
	<hr style="border-top: 3px double black;"/>	<hr style="border-top: 3px double black;"/>	<hr style="border-top: 3px double black;"/>
<b>Identifiable assets (at quarter-end):</b>			
<hr style="border-top: 1px dashed black;"/>			
			October 31, 2003
United States.....			\$ 248,567
Canada.....			66,236
Puerto Rico.....			2,514
			<hr style="border-top: 1px dashed black;"/>
Total.....			\$ 317,317
			<hr style="border-top: 3px double black;"/>

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

(In thousands, except per share amounts)  
(Unaudited)

### NOTE 13 - SALE OF DISCONTINUED OPERATIONS

-----

Effective July 31, 2003, the Company completed the divestiture of certain non-core print manufacturing operations. The assets and liabilities of the divested businesses, which had been excluded from the Company's historical operating results and classified as discontinued operations at April 30, 2003 pursuant to SFAS No. 144, were sold to a financial buyer for \$5,000 in gross proceeds. After payment of expenses, the transaction generated net cash proceeds of approximately \$4,900. The Company used these net proceeds to make certain earn-out payments that were due in May 2003 under purchase agreements for prior acquisitions and to reduce outstanding indebtedness with its senior lenders. With the divestiture, the Company exited the print manufacturing of various types of specialty packaging, folding boxes and vinyl, flexographic and silkscreen labels and signs.

Summarized below are the results of discontinued operations for the six months ended October 31, 2003 and October 31, 2002:

	Six Months Ended October 31,	
	2003	2002
Revenues	\$ 5,677	\$ 13,119
(Loss) income from discontinued operations	(2,171)	135

The major classes of assets and liabilities sold included in the consolidated balance sheet at April 30, 2003 under the captions "Assets of Businesses Held for Sale" and "Liabilities of Businesses Held for Sale" are as follows:

Assets Held for Sale:	April 30, 2003 -----
Accounts receivable, net	\$ 3,880
Inventories	3,662
Prepaid expenses and other current assets	61
Property, plant and equipment, net	616
	\$ 8,219
	=====
Liabilities Held for Sale:	April 30, 2003 -----
Accounts payable	\$ 838
Accrued compensation	903
Accrued additional purchase consideration	970
Other accrued liabilities	508
	\$ 3,219
	=====



Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

This Quarterly Report on Form 10-Q contains forward-looking statements that involve risks and uncertainties. When used in this Report, the words "anticipate," "believe," "estimate," "intend," "may," "will," "expect" and similar expressions as they relate to Workflow Management, Inc. (the "Company," "Workflow Management," "we," "us," and "our") or its management are intended to identify such forward-looking statements. The Company's actual results, performance or achievements could differ materially from the results expressed in, or implied by, these forward-looking statements, which are made only as of the date hereof.

#### Introduction

We are one of the largest distributors of printed business products in North America and we are also a leading provider of end-to-end business management outsourcing solutions, which include vendor-neutral custom print sourcing, consulting and integrated storage and distribution services, that allow our customers to control all of their print-related costs. We produce and distribute a full range of printed business products and provide related management services to approximately 31,000 customers in North America ranging in size from small businesses to Fortune 100 companies. We provide customers with an integrated set of services and information tools that reduce the costs of procuring, storing, distributing and using printed business products and produce custom business documents, envelopes, direct mail and commercial printing. We employ approximately 2,700 persons and have 87 facilities throughout North America.

As used in this Management's Discussion and Analysis of Financial Condition and Results of Operations, "Fiscal 2004", "Fiscal 2003" and "Fiscal 2002" refer to our fiscal years ending April 30, 2004 and ended April 30, 2003 and 2002, respectively.

The following discussion should be read in conjunction with the consolidated historical financial statements, including the related notes thereto, appearing elsewhere in this Quarterly Report on Form 10-Q, as well as our audited consolidated financial statements, and notes thereto, included in our Annual Report on Form 10-K for the fiscal year ended April 30, 2003.

#### Consolidated Results of Operations

Three Months Ended October 31, 2003 Compared to Three Months Ended October 31, 2002

Revenues. Consolidated revenues decreased 6.9%, from \$159.2 million for the three months ended October 31, 2002, to \$148.2 million for the three months ended October 31, 2003. The decrease in consolidated revenues was primarily within our distribution, envelope printing and direct mail project management operations as we continue to experience strong competition and the impact of our customers re-evaluating their purchasing programs for direct mail advertising, commercial printing and other related products due to general economic conditions. We also continue to evaluate customer relationships and renegotiate or eliminate unprofitable accounts. In addition, revenues for the three months

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

ended October 31, 2002 benefited from bi-annual political mailings.

International revenues increased 14.0%, from \$36.2 million, or 22.8% of consolidated revenues, for the three months ended October 31, 2002, to \$41.3 million, or 27.9% of consolidated revenues, for the three months ended October 31, 2003. The increase in international revenues was primarily due to the relative strengthening of the Canadian dollar. In local currency, Canadian dollar revenues increased 0.2% for the three months ended October 31, 2003 versus the three months ended October 31, 2002. International revenues consist exclusively of revenues generated in Canada and Puerto Rico.

Gross Profit. Gross profit decreased 7.4%, from \$44.8 million, or 28.1% of revenues, for the three months ended October 31, 2002, to \$41.5 million, or 28.0% of revenues, for the three months ended October 31, 2003. The decrease in gross profit was primarily in our envelope, direct mail and commercial printing units due to: (i) pricing pressures from competition, and (ii) an overall decrease in manufacturing volumes, described above, resulting in under absorption of fixed factory overhead.

Selling, General and Administrative Expenses. Selling, general and administrative expenses decreased 6.0%, from \$35.9 million, or 22.5% of revenues, for the three months ended October 31, 2002, to \$33.7 million, or 22.8% of revenues, for the three months ended October 31, 2003. The decrease in selling, general and administrative expenses was primarily due to the cost savings realized associated with our restructuring plan and aggressive cost cutting and integration efforts.

Interest Expense, net. Interest expense, net of interest income, decreased 23.1%, from \$5.7 million for the three months ended October 31, 2002, to \$4.4 million for the three months ended October 31, 2003. This decrease in net interest expense during the three months ended October 31, 2003 was due to a decrease in our interest rates under our restructured credit facility and a decrease in the level of debt outstanding during the period. See "Note 6 to the Company's Consolidated Financial Statements" of this Form 10-Q and "Liquidity and Capital Resources" below.

Loss on Ineffective Interest Rate Hedge. On October 16, 2002, our credit facility was amended so that borrowings under the credit facility bore a non-LIBOR based fixed interest rate. Thus, under SFAS No. 133 as amended the Swap became ineffective and could no longer be designated as a cash flow hedge of variable rate debt. During the three months ended October 31, 2003 and the three months ended October 31, 2002, we recorded \$105,000 and \$1.1 million for the subsequent change in the value of the Swap as a component of income.

Financing Fees and Other Banking Related Costs. On August 1, 2003, we entered into an amended restructured senior secured credit facility with our lenders (the "Amended Restructured Credit Facility"). During the three months ended October 31, 2003, we expensed \$0.7 million of unamortized deferred financing costs per the guidelines of Emerging Issues Task Force ("EITF") 98-14, "Debtor's Accounting for Changes in Line-of-Credit or Revolving Debt Arrangements." On January 15, 2003, we entered into a restructured senior secured credit facility with our lenders (the "Restructured Credit Facility"). During the three months ended October 31, 2002, we expensed \$0.8 million in connection with consultants and other professional fees incurred in the negotiation and consummation of the Restructured Credit Facility.

Abandoned Debt Offering Costs. During the three months ended October 31, 2002 we incurred \$174,000 in transaction costs paid in connection with a

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

proposed private placement of senior secured notes (the "Offering"). Due to unfavorable market conditions at the timing of the Offering, we decided not to actively pursue the placement of the senior secured notes. The transaction costs incurred in connection with the Offering were expensed during the three months ended October 31, 2002.

Other Expense (Income). Other income, net of other expense decreased \$61,000 from net other income of \$3,000 for the three months ended October 31, 2002, to net other expense of \$58,000 for the three months ended October 31, 2003. Other income primarily represents the net of gains and/or losses on sales of equipment and miscellaneous other income and expense items.

Income Taxes. Income taxes from continuing operations increased \$982,000 from \$0.5 million for the three months ended October 31, 2002, to \$1.4 million for the three months ended October 31, 2003, reflecting effective income tax rates of 41.2% and 57.0%, respectively. During the three months ended October 31, 2003, the effective income tax rate was greater than the statutory rate due to treating earnings of our Canadian subsidiary as taxable income in the U.S. without the ability to use offsetting foreign tax credits. This treatment resulted from the pledge of our Canadian subsidiary's assets as part of our January 2003 debt restructuring. During both periods, the effective income tax rates reflect the recording of tax provisions at the federal statutory rate of 35.0%, plus appropriate state and local taxes.

Discontinued Operations. During Fiscal 2003, we committed to a plan to dispose of certain non-core businesses. We completed the sale of these non-core businesses effective July 31, 2003 under our long-term business plan and strategic objectives. The net loss from discontinued operations during the three months ended October 31, 2002 includes a loss from operations of \$136,000.

Six Months Ended October 31, 2003 Compared to Six Months Ended October 31, 2002

Revenues. Consolidated revenues decreased 5.9%, from \$309.3 million for the six months ended October 31, 2002, to \$291.1 million for the six months ended October 31, 2003. The decrease in consolidated revenues was primarily within our distribution, envelope printing and direct mail project management operations as we continue to experience strong competition and the impact of our customers re-evaluating their purchasing programs for direct mail advertising, commercial printing and other related products due to general economic conditions. We also continue to evaluate customer relationships and renegotiate or eliminate unprofitable accounts. In addition, revenues for the three months ended October 31, 2002 benefited from bi-annual political mailings. We believe that our inability to make certain earn-out payments due to financial covenants with our lenders adversely impacted the morale and productivity of some of our most important employees which in turn also negatively impacted revenues during the three months ended July 31, 2003.

International revenues increased 13.9%, from \$71.7 million, or 23.2% of consolidated revenues, for the six months ended October 31, 2002, to \$81.7 million, or 28.1% of consolidated revenues, for the six months ended October 31, 2003. The increase in international revenues was primarily due to the relative strengthening of the Canadian dollar. In local currency, Canadian dollar revenues increased 0.9% for the six months ended October 31, 2003 versus the six months ended October 31, 2002. International revenues consist exclusively of revenues generated in Canada and Puerto Rico

Gross Profit. Gross profit decreased 8.3%, from \$86.8 million, or 28.1% of revenues, for the six months ended October 31, 2002, to \$79.6 million, or 27.4% of revenues, for the six months ended October 31, 2003. The decrease in gross profit was primarily a result of lower margins due to pricing pressures from competition and a decrease in volumes within our commercial printing, direct

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

mail and envelope operations due to the sluggish economy and political uncertainty.

**Selling, General and Administrative Expenses.** Selling, general and administrative expenses decreased 5.6%, from \$71.2 million, or 23.0% of revenues, for the six months ended October 31, 2002, to \$67.2 million, or 23.1% of revenues, for the six months ended October 31, 2003. The decrease in selling, general and administrative expenses was due to the realized cost savings and additional cost initiatives implemented during Fiscal 2002 and Fiscal 2003.

18

**Restructuring Costs.** During the six months ended October 31, 2003, the Company incurred \$1.0 million in restructuring costs for the consolidation of certain envelope manufacturing facilities in the New York area. The costs are mainly comprised of future rental payments for the vacated facility. During the six months ended October 31, 2002, net restructuring costs totaled \$221,000 as we reversed into income a \$1.2 million restructuring charge taken in the three months ended April 30, 2001 that was no longer required since we settled the underlying contract dispute and we expensed \$1.4 million in strategic restructuring costs associated with the exploration of other financial, restructuring and strategic alternatives.

**Severance and Other Employment Costs.** During the six months ended October 31, 2003, Thomas B. D'Agostino, Sr., the Chairman of the Board of Directors, resigned from the Board and as Chairman, and released us from any obligation to pay severance or other amounts under his employment agreement with us. As a result, during the six months ended October 31, 2003, we reversed into income approximately \$2.2 million, which was previously recorded as an obligation to Mr. D'Agostino.

**Interest Expense, net.** Interest expense, net of interest income, decreased 10.8%, from \$9.7 million for the six months ended October 31, 2002, to \$8.7 million for the six months ended October 31, 2003. This decrease in net interest expense during the six months ended October 31, 2003 was due to a decrease in our interest rates under our Restructured Credit Facility and a decrease in the level of debt outstanding during the period. See "Note 6 to the Company's Consolidated Financial Statements" of this Form 10-Q and "Liquidity and Capital Resources" below.

**Loss on Ineffective Interest Rate Hedge.** On October 16, 2002, our former credit facility was amended so that borrowings under the credit facility bore a non-LIBOR based fixed interest rate. Thus, under SFAS No. 133 as amended, the Swap has become ineffective and can no longer be designated as a cash flow hedge of variable rate debt. As such, we wrote off \$4.3 million for the fair market value of the ineffective hedge and recorded \$1.1 million for the subsequent changes in the value of the Swap as a component of income. During the six months ended October 31, 2003, we paid \$1.9 million representing cash settlement payments on the Swap and have \$2.5 million accrued at October 31, 2003. Prior to the Swap becoming ineffective, we recorded \$1.7 million as interest expense during the six months ended October 31, 2002.

**Financing Fees and Other Banking Related Costs.** During the six months ended October 31, 2003, we expensed \$0.7 million of unamortized deferred financing costs pertaining to the Amended Restructured Credit Facility as per the guidelines of Emerging Issues Task Force ("EITF") 98-14, "Debtor's Accounting for Changes in Line-of-Credit or Revolving Debt Arrangements." During the six months ended October 31, 2002, we expensed \$0.8 million in connection with consultants and other professional fees incurred in the negotiation and consummation of the Restructured Credit Facility.

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

Abandoned Debt Offering Costs. During the six months ended October 31, 2002 we incurred \$1.9 million in transaction costs paid in connection with a proposed private placement of senior secured notes (the "Offering"). Due to unfavorable market conditions at the timing of the Offering, we decided not to actively pursue the placement of the senior secured notes. The transaction costs incurred in connection with the Offering were expensed during the three months ended October 31, 2002.

Other Expense. Other expense, net of other income, decreased \$35,000 from other expense of \$10,000 during the six months ended October 31, 2002 to other income of \$25,000 during the six months ended October 31, 2003. Other expense primarily represents the net of gains and/or losses on sales of equipment and miscellaneous other income and expense items.

Income Taxes. Provision for income taxes increased 516.5% from a \$0.6 million tax benefit for the six months ended October 31, 2002, to a tax provision of \$2.4 million for the six months ended October 31, 2003, reflecting effective income benefit and tax rates of 22.6% and 57.1% respectively. During the six months ended October 31, 2002, the effective income tax rate was lower due to the tax benefit associated with the restructuring costs, abandoned software costs, uncollectible notes receivable, severance, and other employment costs, loss on ineffective interest rate hedge and financing fees and other banking related costs. During the six

19

months ended October 31, 2003, the effective income tax rate was greater than the statutory rate due to treating earnings of our Canadian subsidiary as taxable income in the U.S. without the ability to use offsetting foreign tax credits. This treatment resulted from the pledge of our Canadian subsidiary's assets as part of our January 2003 debt restructuring. At October 31, 2003, we have both short-term and long-term deferred tax assets totaling \$17.0 million. We evaluate recoverability of deferred tax assets based on estimated future taxable income. To the extent that recovery is deemed not likely, a valuation allowance is recorded. We believe that as of October 31, 2003 realization of its deferred tax assets is more likely than not, and thus no valuation allowance is recorded. During both periods, the effective income tax rates reflect the recording of tax provisions at the federal statutory rate of 35.0%, plus appropriate state and local taxes.

Discontinued Operations. During Fiscal 2003, we committed to a plan to dispose of certain non-core businesses. We completed the sale of these non-core businesses effective July 31, 2003 under our long-term business plan and strategic objectives. The net loss from discontinued operations during the six months ended October 31, 2003 of \$1.3 million which includes a write-down in assets of \$1.0 million and a loss from operations of \$0.3 million compared to income from discontinued operations of \$79,000 during the six months ended October 31, 2002. The reason for the decrease in net income during the six months ended October 31, 2003 related to softness in general economic conditions in the print industry and further deterioration of these non-core businesses.

### Liquidity and Capital Resources

At October 31, 2003, we had a working capital deficit of \$80.2 million, which includes \$153.5 million in debt under our existing credit facility, which has been classified as short-term debt. Our capitalization, defined as the sum of long-term debt and stockholders' equity, at October 31, 2003 was approximately \$71.1 million.

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

We use a centralized approach to cash management and the financing of our operations. As a result, minimal amounts of cash and cash equivalents are typically on hand as any excess cash would be used to pay down our revolving credit facility. Cash at October 31, 2003, primarily represented customer collections and in-transit cash sweeps from our subsidiaries at the end of the quarter and cash in Canada that has not been repatriated.

Our anticipated capital expenditures budget for the next twelve months is approximately \$6.0 million. We anticipate that these capital expenditures primarily will be equipment purchases, leasehold improvements and related costs we expect to incur in connection with the integration of certain operations.

During the six months ended October 31, 2003, net cash provided by operating activities was \$14.8 million. Net cash used in investing activities was \$3.2 million, which was mainly comprised of \$6.3 million used for additional purchase consideration and \$1.9 million used for capital expenditures which was partially offset by \$5.0 million in proceeds from the sale of discontinued operations. Net cash used by financing activities was \$14.3 million, which was mainly comprised of \$11.6 million in net pay-downs on our revolving credit facility, \$1.9 million in settlement payments for the interest rate swap, \$0.7 million in payments of deferred financing costs and \$0.3 million in payments of other long-term debt.

During the six months ended October 31, 2002, net cash provided by operating activities was \$4.7 million. Net cash used in investing activities was \$10.6 million, including \$8.5 million used for acquisitions and additional purchase consideration and \$2.5 million used for capital expenditures. Net cash provided by financing activities was \$6.9 million, which was mainly comprised of \$11.6 million in net borrowings on our revolving credit facility which was partially offset by \$1.9 million in payments of abandoned debt offering costs, \$1.6 million for the cash settlement of the interest rate hedge, \$1.2 million in payments of deferred financing costs and \$0.4 million in payments of other long-term debt.

We have significant operations in Canada. Net sales from our Canadian operations accounted for approximately 26.3% of our total revenues for the six months ended October 31, 2003. As a result, we are subject to certain risks inherent in conducting business internationally, including fluctuations in currency

20

exchange rates. Changes in exchange rates may have a significant effect on our business, financial condition and results of operations.

Effective August 1, 2003 we entered into the Amended Restructured Credit Facility with our senior lenders. The following discussion reflects the terms of this amendment.

At April 30, 2003, we had exceeded certain debt covenants with our lenders that limited capital expenditures and the incurrence of restructuring costs. As part of the Amended Restructured Credit Facility, our senior lenders waived these defaults. The Amended Restructured Credit Facility also modified the calculation of EBITDA for credit facility covenant purposes to exclude the impact of goodwill impairment and the results of discontinued operations and amended certain financial covenants for future periods in a manner consistent with our current business plan and forecasts.

The tranches of debt under the Amended Restructured Credit Facility consist

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

of: (i) an approximately \$100.0 million in availability asset-based revolving credit facility (the "Revolver") which provides access to working capital advanced on a borrowing base formula; (ii) an approximately \$16.2 million senior term loan (the "Term Loan A"); and (iii) a \$50.0 million senior term loan (the "Term Loan B"). The Revolver and Term Loan A mature on August 1, 2004. Term Loan B matures on May 1, 2004. The Revolver contains advance rates of 85% of our eligible accounts receivable, 60% of our eligible inventories (until February 1, 2004 at which time it reduces to 50%) and \$10.0 million against our fixed assets. Under the Amended Restructured Credit Facility, we have granted our senior lenders warrants to acquire up to 2.4 million shares of our common stock. Under the terms of the warrant, the first warrant tranche, for 400,000 shares, would become exercisable on December 31, 2003 unless by November 30, 2003 we had delivered a plan acceptable to our lenders to repay all of our obligations under the Amended Restructured Credit Facility by March 31, 2004. On November 26, 2003, we met the plan delivery requirement with our lenders. Our lenders have until December 31, 2003 to accept the plan. Additional warrant tranches of 400,000 shares each become exercisable each month for a period of five months beginning no later than March 31, 2004 but only in the event there remains outstanding indebtedness under the credit facility on the date the tranche becomes exercisable. Each 400,000 share warrant tranche would have an exercise price equal to the fair market value of our common stock on the date the tranche becomes exercisable.

The outstanding balances (in millions) on the Amended Restructured Credit Facility at December 12, 2003 were as follows:

	Maximum Availability	Amount Outstanding	Applicable Interest Rate
	-----	-----	-----
Revolver	\$ 100.0	\$ 91.2	LIBOR + 5%
Term Loan A	16.2	16.2	LIBOR + 8%
Term Loan B	50.0	50.0	11%, 12%, 13% & 14% for each calendar quarter of 2003
	-----	-----	
	\$ 166.2	\$ 157.4	
	=====	=====	

At December 12, 2003, we had \$157.4 million outstanding on the Amended Restructured Credit Facility and, in addition, \$3.1 million in outstanding letters of credit. Our availability under the Amended Restructured Credit Facility at December 12, 2003 was \$5.7 million after inclusion of letters of credit.

As noted above, the \$50.0 million Term Loan B portion of the Amended Restructured Credit Facility matures on May 1, 2004 and Term Loan A and the Revolver mature on August 1, 2004. We are currently pursuing various strategic and refinancing alternatives that would allow us to repay the components of our credit facility debt by their respective due dates. However, we do not have any firm commitments with respect to any potential refinancing or similar transactions, nor do we anticipate generating operating cash flows that would allow us to repay these obligations directly. There can be no assurance that we will be able to repay the Amended Restructured Credit Facility by its due date. In the event we are not able to do so, we will be in default with our lenders under the Amended Restructured Credit Facility. Any such default could have a material adverse effect on our business, financial condition and results of operations.

In addition, the Amended Restructured Credit Facility contains a number of

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

other affirmative covenants related to our business with which we must comply. These covenants include, but are not limited to, the requirements that (i) we meet certain liquidity tests before making any earn-out payments as a result of our prior acquisitions and (ii) we meet certain leverage ratio, interest coverage ratio, fixed charge ratio, and minimum EBITDA thresholds on an ongoing basis. There can be no assurance that we will be able to satisfy all or any of these covenants. Any failure to satisfy these covenants (or any other covenants) would constitute a default under the Amended Restructured Credit Facility. Any such default likely would have a material adverse effect on our business, financial condition and results of operations.

In May 2001, we entered into an interest rate swap agreement to manage interest rate risk on the variable rate borrowings under our then existing credit facility. As of October 31, 2003, the swap was recorded at \$2.5 million, which represents the amount which we would have paid to settle the swap at that date. If we repay the amounts outstanding under the Amended Restructured Credit Facility with proceeds from any alternate financing, we will be required to settle the swap at the fair value as of that date. We anticipate using a portion of the proceeds from any such financing to make this payment.

We historically have grown significantly through acquisitions. However, we began to implement a new strategic business plan in Fiscal 2003. Under our new strategic plan, we have focused on (i) integrating our existing core operations to improve profitability, (ii) divesting non-core operations to pay down debt and (iii) greater focus on profitable accounts even at the expense of lower overall revenue. We did not consummate any acquisitions in Fiscal 2003 and we do not anticipate pursuing or consummating acquisitions in the near future.

### Fluctuations in Quarterly Results of Operations

Our envelope and commercial print businesses are subject to seasonal influences resulting from the lower demand for consumable printed business products during the summer months which coincides with our fiscal quarters ending in October. Quarterly results also may be materially affected by variations in the prices by us for the products we sell, the mix of products sold and general economic conditions. Therefore, results for any quarter are not necessarily indicative of results that may be achieved for any subsequent fiscal quarter or full fiscal year.

### Inflation

We do not believe that inflation has had a material impact on our results of operations during the six months ended October 31, 2003 and 2002.

### Critical Accounting Policies and Judgments

Use of Estimates. In preparing our financial statements in conformity with generally accepted accounting principles, we are required to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. We evaluate our estimates and judgments on an ongoing basis, including those related to allowance for doubtful accounts, inventory reserves, impairment of property and equipment, impairment of goodwill and intangible assets and realization of deferred tax assets. We base our estimates and judgments on historical experience and on various other factors that we believe to be reasonable under the circumstances. Actual results may differ from these estimates.

Revenue Recognition. We recognize revenue for the majority of our products



## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

upon shipment to the customer, upon the transfer of title and at the time risk of loss passes to the buyer. Under agreements with certain customers, we may store custom forms for future delivery. In these situations, we typically receive a warehousing fee for the services we provide. In these cases, delivery and billing schedules are agreed upon with the customer and revenue is recognized when manufacturing is complete, title transfers to the customer, the order is invoiced and there is reasonable assurance as to collectibility. Since the majority of products are

22

customized, product returns are not significant. We recognize revenues for warehousing customers' inventory as storage services are provided. We do not charge separate fees for on-line access and ordering of inventory as these services are offered to customers as a convenience. Delivery costs billed to customers are recognized in revenues.

Allowance for Doubtful Accounts. We maintain an allowance for doubtful accounts, which is reviewed at least quarterly for estimated losses resulting from the inability of our customers to make required payments. Additional allowances may be necessary in the future if the ability of our customers to pay deteriorates.

Inventory Reserves. We maintain a reserve for slow moving or obsolete inventory, which is reviewed at least quarterly, based upon usage and inventory age to determine its adequacy. Physical inventories are taken throughout each fiscal year.

Impairment of Property and Equipment. Property and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. An estimate of undiscounted future cash flows produced by the asset, or the appropriate grouping of assets, is compared with the carrying value to determine whether an impairment exists, pursuant to the provisions of Statement of Financial Accounting Standards No. 144 "Accounting for the Impairment or Disposal of Long-Lived Assets" beginning in fiscal year 2003.

Impairment of Goodwill and Intangible Assets. During Fiscal 2002, Statement of Financial Accounting Standards ("SFAS") No. 142, "Goodwill and Other Intangible Assets", was issued. We adopted this new standard and as a result, we ceased to amortize goodwill effective May 1, 2001. In lieu of amortization we performed an initial impairment review of our goodwill and indefinite-lived intangible assets as of the implementation date, following which we concluded that there was no impairment at May 1, 2001. An impairment is recorded when the fair value of a reporting unit is less than the carrying value of the reporting unit's net assets. Fair value of a reporting unit is derived from a combination of discounted future cash flow and comparison to comparable publicly traded companies. We are required to perform an annual impairment review upon the completion of each fiscal year. The results of these annual impairment reviews are highly dependent on management's projection of future results for our reporting units and there can be no assurance that at the time such reviews are completed a material impairment charge will not be recorded. An impairment test was performed at April 30, 2003 at which time an \$18.0 million charge was recorded as a component of operating income.

Realization of Deferred Tax Assets. A valuation allowance is recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized. The primary factors we consider are our historical results, earnings potential determined through use of internal projections and the nature of income that can be used to realize the deferred tax asset. Based

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

on our consideration of these factors, we believe it is more likely than not all of our deferred tax assets will be realized. If future results of operations are less than expected future assessments may result in a determination that some or all of the net deferred tax assets are not realizable.

### New Accounting Pronouncements

Extinguishment of Debt and Accounting for Leases. In April 2002, the FASB issued SFAS No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections," that supercedes previous guidance for the reporting of gains and losses from extinguishment of debt and accounting for leases, among other things.

SFAS No. 145 requires that only gains and losses from the extinguishment of debt that meet the requirements for classification as "Extraordinary Items," as prescribed in APB No. 30, should be disclosed as such in the financial statements. Previous guidance required all gains and losses from the extinguishment of debt to be classified as "Extraordinary Items." This portion of SFAS No. 145 is effective for fiscal years beginning after May 15, 2002, with restatement of prior periods required. Implementation of this portion of the standard will result in the reclassification of certain losses on extinguishment of debt previously treated as

23

extraordinary items by Workflow.

In addition, SFAS No. 145 amends SFAS No. 13, "Accounting for Leases," as it relates to accounting by a lessee for certain lease modifications. Under SFAS No. 13, if a capital lease is modified in such a way that the change gives rise to a new agreement classified as an operating lease, the assets and obligation are removed, a gain or loss is recognized and the new lease is accounted for as an operating lease. Under SFAS No. 145, capital leases that are modified so the resulting lease agreement is classified as an operating lease are to be accounted for under the sale-leaseback provisions of SFAS No. 98, "Accounting for Leases." These provisions of SFAS No. 145 are effective for transactions occurring after May 15, 2002.

SFAS No. 145 will be applied as required. Adoption of SFAS No. 145 is not expected to have a material impact on the Company's results of operations, financial position or cash flows.

Accounting for Exit and Disposal Activities. In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" which addresses the recognition, measurement, and reporting of costs associated with exit and disposal activities, including restructuring activities. This statement requires that liabilities for costs associated with an exit or disposal activity not be recognized until the liability is incurred and the fair value can be estimated, except for certain one-time termination benefits. SFAS No. 146 nullifies Emerging Issues Task Force (EITF) 94-3 which permitted recognition of a liability for such costs at the date of a company's commitment to an exit plan. The provisions of SFAS No. 146 are effective, and we have adopted its provisions, for exit and disposal activities initiated after December 31, 2002. The provisions of EITF 94-3 will continue to apply for liabilities previously recorded.

Accounting for Consideration Received from a Vendor. In January 2003, the Emerging Issues Task Force issued EITF 02-16, "Accounting by a Customer (Including a Reseller) for Certain Consideration Received from a Vendor," which

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

states that cash consideration received from a vendor is presumed to be a reduction of the prices of the vendor's products or services and should, therefore, be characterized as a reduction of cost of goods sold when recognized in the statement of operations. That presumption is overcome when the consideration is either a reimbursement of specific, incremental, identifiable costs incurred to sell the vendor's products, or a payment for assets or services delivered to the vendor. EITF 02-16 is effective, and we have adopted its provisions, for arrangements entered into after December 31, 2002.

Guarantor's Accounting for Guarantees. In December 2002, the FASB issued Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others," which provides for additional disclosures to be made by a guarantor in its interim and annual financial statements about its obligations and requires, under certain circumstances, a guarantor to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. We have adopted the disclosure requirements for Fiscal 2003 and do not expect the recognition and measurement provisions of Interpretation No. 45 to have an effect on our consolidated financial statements.

### Factors Affecting the Company's Business

The terms of our amended credit facility require us to repay at least \$50.0 million of debt by May 1, 2004 and to repay our remaining credit facility obligations by August 1, 2004. There can be no assurance that we will be able to satisfy these obligations.

Under the terms of an amendment to our credit facility that we entered into with our senior lenders effective as of August 1, 2003, the due date for the \$50.0 million term loan was extended from December 31, 2003 until May 1, 2004 and the due dates for another term loan and the revolving portion of the facility were accelerated to August 1, 2004. We are currently pursuing various strategic and refinancing alternatives that would allow us to repay our credit facility obligations by their respective due dates. However, we do not have any firm commitments with respect to any potential refinancing or similar transactions, nor do we anticipate generating operating cash flows that would allow us to repay these obligations directly. There can be no

24

assurance that we will be able to repay our credit facility obligations by their respective due dates. In the event we are unable to do so, our lenders would have the right to declare our entire approximately \$170.0 million credit facility in default and foreclose on our assets unless we obtained a waiver or amendment to the credit facility. As a result, the inability to repay our credit facility obligations would have a material adverse effect on our business, financial condition and results of operations.

Under the terms of our amended credit facility, we have granted our lenders warrants to acquire up to 2.4 million shares of our common stock. These warrants could have a dilutive effect on our existing stockholders.

Under the terms of our amended credit facility, we have granted our senior lenders warrants to acquire up to 2.4 million shares of our common stock, which would represent approximately 15.2% of our outstanding common stock if the warrants were exercised. Under the terms of the warrant, the first warrant tranche, for 400,000 shares, would become exercisable on December 31, 2003 unless, by November 30, 2003, we had delivered a plan acceptable to our lenders to repay all of our obligations under our credit facility by March 31, 2004. On

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

November 26, 2003, we met the plan delivery requirement with our lenders. Our lenders have until December 31, 2003 to accept the plan. Additional warrant tranches of 400,000 shares each become exercisable each month for a period of five months beginning no later than March 31, 2004, but only in the event there remains outstanding indebtedness under the credit facility on the date the tranche becomes exercisable. Each warrant tranche would have an exercise price equal to the fair market value of our common stock on the date the tranche becomes exercisable.

To the extent we are unable to refinance or otherwise repay our credit facility obligations by the dates on which the various warrant tranches become exercisable, our lenders will have the right to acquire shares of our common stock up to a maximum of 2.4 million shares. These warrants would have a dilutive impact on our existing stockholders to the extent that our lenders ever exercise the warrants at exercise prices that are less than the fair market value of our common stock on the date of exercise. Any dilutive impact, or potentially dilutive impact, of the warrants could adversely affect the market price of our common stock.

In order to remain in compliance with our credit facility, we have breached our obligations to pay earn-outs under numerous purchase agreements for prior acquisitions. These breaches have had, and may continue to have, an adverse impact on our business.

The terms of most of our purchase agreements for prior acquisitions require us to pay earn-outs to the former owners of the acquired businesses. In many cases, the earn-out recipients are employed by us and are critical to maintaining good relationships with some of our best customers. Under the terms of an amendment to our credit facility that we entered into with our senior lenders in January 2003, we were required to defer or otherwise not pay at least \$4.0 million of earn-outs due in May 2003.

Recipients of approximately \$1.0 million of earn-out payments voluntarily agreed to accept subordinated notes due in 2005 in lieu of receiving a cash earn-out payment in May. However, many earn-out recipients were not willing to accept these notes. As a result, to remain in compliance with our credit facility, we were required to breach our earn-out obligations, or in one case deliver a short-term promissory note, with respect to individuals entitled to approximately \$3.0 million in earn-out payments. Under the terms of the amendment to the credit facility that we entered into with our senior lenders on August 1, 2003, we were allowed to make these earn-out payments that were previously required to be deferred. However, we believe that the earn-out breaches have had an adverse effect on the morale and productivity of some of our most important employees and this adverse effect may impact our operations on a long-term basis.

We have previously announced that we are pursuing various strategic and refinancing alternatives, including a potential sale of the Company. Pursuing the sale of the Company or other strategic alternatives could have a disruptive effect on our employees and our relationships with our customers and suppliers, regardless of whether any transaction is consummated.

As previously announced in two public press releases, our Board of Directors is pursuing various strategic and refinancing alternatives to address our credit facility obligations, including a potential sale of the

Company. The inherent uncertainties surrounding our pursuit of strategic and refinancing alternatives, and in particular the uncertainties associated with

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

the potential sale of the Company, could have disruptive effects on our employees and our relationships with our customers and suppliers. These disruptive effects could adversely impact our business, financial condition and results of operations.

Depending on the strategic or refinancing alternatives we ultimately pursue to address our credit facility obligations, we may have to issue a significant amount of our equity to lenders and/or investors. Any such issuance of equity could have a significant dilutive impact on our existing stockholders.

In order to address our credit facility obligations, we may be required to refinance all or a portion of our debt with equity and/or debt investments by third parties. Any such transactions could require that we issue lenders and/or investors a significant amount of our common stock or potentially shares of a newly created class of preferred stock. Any such issuance of common or preferred stock could have a significant dilutive impact on our existing stockholders and could adversely impact the market price of our common stock.

Our credit facility subjects us to a number of financial covenants. If our financial results in future periods are not what we anticipate, we likely will breach one or more of these covenants. Any such breaches could have a material adverse impact on our business and financial condition.

The terms of our credit facility require us to comply with certain financial covenants, including minimum liquidity and minimum EBITDA covenants. Based on our current business plans and prospects, we believe that we will be able to satisfy these covenants on an ongoing basis. However, in the event that our financial results in future periods are not what we anticipate, then we likely will breach one or more of these covenants. In the event of any such breaches, our lenders would have the right to declare our credit facility in default and foreclose on our assets unless we obtain waivers for the breaches. There can be no assurance that our lenders will provide waivers in the event we breach any covenants in future periods.

Economic events and outside influences from world events have adversely affected us and could affect our business adversely in future periods.

The U.S. economy has had an adverse effect on our sales and subsequent profit in recent periods and a continued lack of economic growth could affect our business adversely in future periods. Changes in economic conditions that affect customer buying patterns have an impact on our business. Additionally, world events such as the recent war in the Middle East, anthrax in the U.S. and SARS and Mad Cow disease in Canada have adversely impacted many of our operating units. There can be no assurances that events such as these will not impact our business negatively in the future.

Thomas B. D'Agostino, Sr., a founder of the Company and former Chairman and Chief Executive Officer, and Thomas B. D'Agostino, Jr., former President of our Solutions Division, are no longer directors of, or employed by, the Company. Each of these individuals has the ability to compete against the Company if he desires. Any such competition could adversely impact our business.

In March 2003, we terminated the employment of Thomas B. D'Agostino, Jr., the President of our Solutions Division, and he subsequently resigned as a director. In October 2003, Thomas B. D'Agostino, Sr. resigned as a director, officer and employee. Under the terms of their respective employment separations, each of these individuals is entitled to compete against the Company if he so desires. We believe that Mr. D'Agostino, Jr. has already begun some competitive activities within our industry and solicited some of our employees. However, the majority of our key managers and performers have employment contracts containing non-compete provisions which we believe would preclude them from joining Mr. D'Agostino, Jr.

## Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

Both of these individuals have longstanding relationships with many of our key employees and key customers. In the event that either or both of these individuals choose to actively compete against the Company, there can be no assurance that any such competitive efforts will not adversely impact our business.

For additional risk factors, refer to our Annual Report on Form 10-K for the fiscal year ended April 30, 2003.

26

### Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Our financial instruments include cash, accounts receivable, accounts payable, long-term debt and an interest rate swap. Market risks relating to the Company's operations result primarily from changes in interest rates. Our borrowings under our credit facility are primarily dependent upon LIBOR rates. The estimated fair value of long-term debt approximates its carrying value at October 31, 2003.

We do not hold or issue derivative financial instruments for trading purposes. On May 3, 2001, we entered into an interest rate swap agreement (the "Swap") with various lending institutions at no cost to us. The Swap's effective date is August 1, 2001 with a termination date of March 10, 2004. We exchanged our variable interest rate on \$100.0 million in credit facility debt for a fixed 3-month LIBOR of approximately 5.10% plus our interest rate spread under our credit facility. The Swap was entered into to manage interest rate risk on the variable rate borrowings under our revolving credit portion of our debt. This interest rate swap has the effect of locking in, for a specified period, the base interest rate we will pay on the \$100.0 million notional principal amount established in the Swap. As a result, while this hedging arrangement is structured to reduce our exposure to interest rate increases, it also limits the benefit we might otherwise have received from any interest rate decreases. The Swap is cash settled quarterly, with the Swap's carrying value adjusted for amounts paid or received. If 3-month LIBOR were to increase or decrease by 1.0%, the impact to us would be a cash savings of \$1.0 million in annual interest expense or additional annual cash interest expense of \$1.0 million over the interest charged on \$100.0 million in debt under the variable 3-month LIBOR. Any such change in interest rates would have a related impact on the Swap in that a 1% increase or decrease would have an impact on the fair value of the swap of approximately \$1.0 million.

### Item 4. Controls and Procedures

- (a) Within the 90-day period prior to the date of this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Rule 13a-15(e) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Based upon the evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective in timely alerting them to material information relating to the Company (including its consolidated subsidiaries) required to be included in the Company's Exchange Act filings.
- (b) There have been no significant changes in the Company's internal controls or in other factors which could significantly affect its

Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

internal controls subsequent to the date the Company carried out its evaluation.

27

PART II - OTHER INFORMATION

Item 6. Exhibits and Reports on Form 8-K.

(a) Exhibits

- \*\* 10.90 Indemnification Agreement dated October 28, 2003 by and between Workflow Management, Inc. and Michael L. Schmickle.
- \*\* 10.91 Indemnification Agreement dated October 28, 2003 by and between Workflow Management, Inc. and Gary W. Ampulski.
- \*\* 10.92 Indemnification Agreement dated October 28, 2003 by and between Workflow Management, Inc. and James J. Maiwurn.
- \*\* 10.93 Indemnification Agreement dated October 28, 2003 by and between Workflow Management, Inc. and Roger J. Pearson.
- \*\* 10.94 Indemnification Agreement dated October 28, 2003 by and between Workflow Management, Inc. and Peter Redding.
- \*\* 10.95 Indemnification Agreement dated October 28, 2003 by and between Workflow Management, Inc. and Gerald F. Mahoney.
- \*\* 10.96 Indemnification Agreement dated October 28, 2003 by and between Workflow Management, Inc. and Thomas A. Brown, Sr.
- \*\* 31.1 Section 302 - Chief Executive Officer
- \*\* 31.2 Section 302 - Chief Financial Officer
- \*\* 32.1 Section 906 - Chief Executive Officer
- \*\* 32.2 Section 906 - Chief Financial Officer

-----  
\*\* Filed herewith.

(b) Reports on Form 8-K

1. The Company filed a Form 8-K on August 8, 2003, under Item 9. The Form 8-K contains a press release regarding an amendment to the Company's credit facility and a sale by the Company of its discontinued operations.
2. The Company filed a Form 8-K on September 16, 2003, under Item 9. The Form 8-K contains a press release regarding the Company's financial and operating results for the fiscal quarter ended July 31, 2003.

28

SIGNATURES

Edgar Filing: WORKFLOW MANAGEMENT INC - Form 10-Q

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

WORKFLOW MANAGEMENT, INC.

December 15, 2003

-----

Date

By: /s/ Gary W. Ampulski

-----

Gary W. Ampulski  
President and Chief Executive Officer  
(Principal Executive Officer)

December 15, 2003

-----

Date

By: /s/ Michael L. Schmickle

-----

Michael L. Schmickle  
Executive Vice President, Chief Financial  
Officer, Secretary and Treasurer (Principal  
Financial Officer and Principal Accounting  
Officer)