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PSC INC
Form 8-K
February 07, 2003

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SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 8-K

CURRENT REPORT

Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Date of Report (Date of earliest event reported): January 17, 2003

PSC INC.

(Exact Name of Registrant as Specified in its Charter)

NEW YORK ----- (State or other jurisdiction of incorporation)	0-9919 ----- (Commission File Number)	16-0969362 ----- (I.R.S. Employer Identification No.)
111 S.W. FIFTH AVENUE, SUITE 4100, PORTLAND, OREGON ----- (Address of principal executive offices)		97204 ----- (Zip Code)

(503) 553-3920

(Registrant's telephone number, including area code)

Not applicable

(Former name or former address; if changed since last report.)

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Item 5. Other Events

As previously reported, on November 22, 2002, PSC Inc. (the "Company") filed a voluntary bankruptcy petition for relief under Chapter 11 of the United States Bankruptcy Code in the United States Bankruptcy Court for the Southern District of New York. Since the November 22, 2002 petition date, the Company has operated as a debtor in possession and is in compliance with all bankruptcy reporting requirements.

As a result of the Chapter 11 proceeding, each month the Company is required to file with the Bankruptcy court a schedule of monthly income and

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expenses, along with selected balance sheet data (the "Monthly Operating Statement"). On January 17, 2003, the Registrant filed a Monthly Operating Statement with the Bankruptcy Court covering the period of November 22, 2002 to December 31, 2002. This Monthly Operating Statement is filed as Exhibit 99.1 to this Current Report.

The financial data included in the Monthly Operating Statement is not audited. The Monthly Operating Statement is in a format prescribed by applicable bankruptcy laws. There can be no assurance that, from the perspective of an investor or potential investor in the Company's securities, the Monthly Operating Statement is complete. The Monthly Operating Statement also contains information for periods different from those required in the Company's reports pursuant to the Securities Exchange Act of 1934, as amended ("the Exchange Act"). This information might not be indicative of the Company's financial condition or operating results for the period that would be reflected in the Company's financial statements or in its reports pursuant to the Exchange Act. Results set forth in any Monthly Operating Statement should not be viewed as indicative of future results.

Item 7. Financial Statements and Exhibits.

(c) EXHIBITS.

EXHIBIT NO.	DESCRIPTION
99.1	PSC Inc. Monthly Operating statement for the period from November 22, 2002 to December 31, 2002

FORWARD LOOKING STATEMENTS

Certain statements in this Form 8-K are forward-looking statements that involve risk and uncertainties, which may cause actual results to differ materially from the statements made including market potential, regulatory clearances, business growth and other risks listed from time to time in the Company's Securities and Exchange Commission filings. These forward-looking statements represent the Company's judgment, as of the date of this release, and the Company disclaims any intent or obligation to update these forward-looking statements.

SIGNATURES

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 hereunto duly authorized.

PSC INC.

By: /s/EDWARD J. BOREY

Name: Edward J. Borey

Title: President, Chief Executive Officer and Director

Dated: February 5, 2003

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Paul M. Brown

 Printed Name of Authorized Individual

Vice President and Chief
 Financial Officer

 Title of Authorized Individual

Indicated if this is an amended statement
 by checking here: AMENDED STATEMENT: -----

PSC INC.
 CASE #: 02-15876 (SMB)
 REPORTING PERIOD: DECEMBER 31, 2002
 \$ AMOUNTS IN THOUSANDS

		----- UNAUDITED -----
		December 31, 2002 (b)
CONSOLIDATED STATEMENT OF OPERATIONS (MOR-1)	(a)	-----
Sales to third parties		\$ 15,529
Cost of Sales		11,261

GROSS PROFIT		4,268

Operating Expenses		
Sales & Marketing		3,526
Engineering, R&D		1,089
General & Administrative		1,304
Severance & Other Costs		(202)
Debt Restructuring Fees		450
Foreign Curr. (Gain) Loss		(212)
Amortization of Intangibles		-

Total Operating Expenses		5,955

OPERATING PROFIT (LOSS)		(1,687)

Other (Income) Expense		
Other (Income) Expense		(1,788)
Interest Expense		77

Other (Income) Expense		(1,711)

INCOME (LOSS) BEFORE TAXES		\$ 24

Tax Provision (Benefit)		338

NET INCOME (LOSS)		\$ (314)
		=====

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Notes:

- (a) This Statement of Operations is for the PSC Inc., on a consolidated basis. All foreign subsidiaries included in this statement are excluded from the Chapter 11 filing of the debtors.
- (b) Reporting period for December, 2002 is actually from November 22, 2002 (the petition filing date) to December 31, 2002.

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SCHEDULE: MOR-1

PSC INC.
CASE #: 02-15876 (SMB)
REPORTING PERIOD: DECEMBER 31, 2002
\$ AMOUNTS IN THOUSANDS

	UNAUDITED	UNAUDITED
	11/22/02 (Petition Date)	12/31/02 (a)
CONSOLIDATED BALANCE SHEET (MOR-2)		
ASSETS		

CURRENT ASSETS		
Cash and cash equivalents	2,328	3,308
Accounts Receivable - net	29,643	29,012
Inventories - net	22,891	20,121
Prepaid Expenses and Other	2,832	3,960
	-----	-----
Total current assets	57,694	56,401
	-----	-----
PROPERTY, PLANT AND EQUIPMENT		
Land	-	-
Buildings & Improvements	29	54
Office Furniture	13,966	14,117
Production Equipment	17,629	17,719
Leasehold Improvements	921	926
	-----	-----
Total property, plant and equipment	32,545	32,816
Less: Accumulated Depreciation	(23,961)	(24,337)
	-----	-----
NET PROPERTY, PLANT AND EQUIPMENT	8,584	8,479
	-----	-----
OTHER ASSETS		
Intangibles from Acquisitions	102	50
Other Intangibles	14,751	15,119
Other Assets	(358)	86
Less: Accumulated amortization	(5,593)	(5,742)
	-----	-----
Total other assets	8,902	9,513
	-----	-----

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TOTAL ASSETS 75,180 74,393
=====

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SCHEDULE: MOR-2

PSC INC.
CASE #: 02-15876 (SMB)
REPORTING PERIOD: DECEMBER 31, 2002
\$ AMOUNTS IN THOUSANDS

	UNAUDITED	UNAUDITED
CONSOLIDATED BALANCE SHEET (MOR-2)	11/22/02 (Petition Date)	12/31/02 (a)
LIABILITIES & SHAREHOLDERS' EQUITY		
LIABILITIES (POST-PETITION)		
CURRENT LIABILITIES		
DIP Financing Arrangement	-	4,000
Accounts Payable	-	4,945
Note Payable	-	-
Accrued Expenses	-	151
Accrued Interest	-	11
Deferred Revenue	-	131
Accrued Warranty	-	138
Accrued Taxes/VAT	-	19
Accrued Royalties	-	535
Accrued Payroll and Commissions	-	947
Accr. Acq. Related Restructuring Costs	-	550
Intercompany payable (receivable)	-	170
TOTAL CURRENT LIABILITIES	-	11,597
LONG-TERM LIABILITIES		
Deferred Revenue	-	-
LT Warranty Accrual	-	110
Other LT Liabilities (includes warrants)	-	-
TOTAL LONG-TERM LIABILITIES	-	110
TOTAL LIABILITIES (POST-PETITION)	-	11,707
LIABILITIES (PRE-PETITION)		
CURRENT LIABILITIES		

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Secured debt	93,462	93,462
Priority debt	29,268	29,268
Note Payable	1,651	1,651
Accounts Payable	17,226	8,463
Accrued Expenses	8,543	6,956
Accrued Interest	14,128	13,927
Deferred Revenue	884	560
Accrued Warranty	1,519	1,387
Accrued Taxes/VAT	(457)	-
Accrued Royalties	1,637	716
Accrued Payroll and Commissions	2,983	1,639
Accr. Acq. Related Restructuring Costs	-	-
Intercompany payable (receivable)	-	-
	-----	-----
TOTAL CURRENT LIABILITIES	170,844	158,029
	-----	-----
LONG-TERM LIABILITIES		
Deferred Revenue	550	555
LT Warranty Accrual	1,557	1,497
Other LT Liabilities (includes warrants)	489	495
	-----	-----
TOTAL LONG-TERM LIABILITIES	2,596	2,547
	-----	-----
TOTAL LIABILITIES (PRE-PETITION)	173,440	160,576
	-----	-----
TOTAL LIABILITIES	173,440	172,283
	-----	-----
SHAREHOLDERS' EQUITY		
Common Shares	130	130
Additional Paid-in Capital	73,078	73,078
Cumulative Translation Adjustment	(3,277)	(2,593)
Retained earnings - prepetition	(166,834)	(166,834)
Retained earnings - postpetition	-	(314)
Less: Treasury Shares	(1,357)	(1,357)
	-----	-----
TOTAL SHAREHOLDERS' EQUITY	(98,260)	(97,890)
	-----	-----
TOTAL LIABILITIES AND SHAREHOLDERS, EQUITY	75,180	74,393
	=====	=====

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SCHEDULE: MOR-2

PSC INC.
CASE #: 02-15876 (SMB)
REPORTING PERIOD: DECEMBER 31, 2002
\$ AMOUNTS IN THOUSANDS

UNAUDITED

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CONSOLIDATED STATEMENT OF CASHFLOWS (MOR-3)	(b)	12/31/02	(a)

CASH FLOWS FROM OPERATING ACTIVITIES			

Net income/(loss)			(314)
Adjustments to reconcile net income to net cash:			
Depreciation			348
Amortization			95
(Gain)/Loss on disposition of assets			-
Change in fair value of warrants			-
Changes to Debt Discount			-
(INCREASE) DECREASE IN ASSETS:			
Accounts receivable			631
Inventories			2,770
Prepaid expenses and other			(1,124)
INCREASE (DECREASE) IN LIABILITIES:			
Accounts payable			(6,450)
Accrued expenses			1,771
Accrued payroll & commissions			(351)
Other Long-term liabilities			(132)

Net Cash Provided by/(Used in) Operating Activities			(2,756)

CASH FLOWS FROM INVESTING ACTIVITIES			
Capital expenditures, net			(243)
Proceeds from sale of assets			-
Write-off of goodwill			-
Addition to intangible assets & other long-term assets, net			(706)

Net Cash Provided by/(Used in) Investing Activities			(949)

CASH FLOWS FROM FINANCING ACTIVITIES			
Additions to Debtor-In-Possession Financing Arrangement			4,000
Additions (Payments) of long-term debt			1
Net proceeds from exercise of options and sale of stocks			-
Tax benefit from exercise or early disposition of stock options			-

Net Cash Provided by/(Used in) Financing Activities			4,001

Effect of Exchange Rate Changes on Cash & Cash Equivalents			684

Net Increase (Decrease) in Cash & Cash Equivalents			980
CASH AND CASH EQUIVALENTS, beginning of period			2,328

CASH AND CASH EQUIVALENTS, end of period			3,308
			=====

Notes:

- (a) This Statement of Cashflows is for the PSC Inc., on a consolidated basis. All foreign subsidiaries included in this statement are excluded from the Chapter 11 filing of the debtors.
- (b) Reporting period for December, 2002 is actually from November 22, 2002 (the petition filing date) to December 31, 2002.

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SCHEDULE: MOR-3

PSC INC.
CASE #: 02-15876 (SMB)
REPORTING PERIOD: DECEMBER 31, 2002
\$ AMOUNTS IN THOUSANDS

	UNAUDITED
	12/31/02
SCHEDULE OF CASH RECEIPTS & DISBURSEMENTS (MOR-4)	(a), (b)
Cash Receipts	
Accounts Receivable Collections	10,394
Cash Repatriations From International Subsidiaries	3,681
Additions to Post-Petition Debt	4,000
Other Cash Receipts	-
Total Cash Receipts	18,075
OPERATING DISBURSEMENTS (c)	
Payroll and Payroll Taxes	2,638
Accounts Payable And Accrued Liabilities	11,774
Consulting and Professionals In The Normal Course	201
Royalty Payments	921
Director & Officer Liability Insurance Payments	307
Rents	221
Capital Expenditures	468
TOTAL OPERATING DISBURSEMENTS	16,530
BANKRUPTCY-RELATED FEES AND EXPENSES	
Payments To Professionals	-
US Trustee Fees	-
Court Costs	-
Other Costs	-
TOTAL BANKRUPTCY-RELATED FEES AND EXPENSES	-
TOTAL CASH DISBURSEMENTS	16,530
Net Change In Cash	1,545
Beginning Cash Balance, US Bank Accounts	(282)
ENDING CASH BALANCE, US BANK ACCOUNTS	1,263
RECONCILIATION TO BALANCE SHEET:	
Cash - US Bank Accounts	1,263
Cash - International Bank Accounts (Not In Chapter 11)	2,045
TOTAL CASH PER BALANCE SHEET	3,308

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(a) This schedule of Cash Receipts And Disbursements is related to US-only disbursements that are treated in accordance with the Chapter 11 provisions. International revenues and expenses are excluded. Note that Cash Repatriations From International Subsidiaries is the net cash swept from foreign cash collections, after local disbursements.

(b) Reporting period for December, 2002 is actually from November 22, 2002 (the petition filing date) to December 31, 2002.

(c) Includes payment of Court-approved Pre-Petition items.

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SCHEDULE: MOR-4

PSC, INC.
PSC INC.
Case #: 02-15876 (SMB)
Reporting Period: December 31, 2002
\$ Amounts in thousands

UNAUDITED

SCHEDULE OF ACCOUNTS PAYABLE (MOR-5)

12/31/02

Trade Accounts Payable	
US Pre-Petition Accounts Payable	7,870
US Post-Petition Accounts Payable	4,945
Foreign Subsidiary Accounts Payable	593

TOTAL CONSOLIDATED ACCOUNTS PAYABLE	13,408
	=====

Payable
(Receivable)

INTERCOMPANY TRADE ACCOUNTS (a)

PSC Inc. (debtor)	9,715
PSC Scanning, Inc (debtor)	(19,765)
PSC UK	(233)
PSC France	686
PSC Italy	2,551
PSC Germany	3,559
PSC Australia	10
PSC Japan	268
Consolidation Eliminations	3,209

TOTAL INTERCOMPANY TRADE ACCOUNTS	-
	=====

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Note:

(a) All cash flows within subsidiaries flow from the foreign subsidiaries to the domestic debtors. There are no cash disbursements from the debtors to non-debtor subsidiaries.

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SCHEDULE: MOR-5

PSC INC.

CASE #: 02-15876 (SMB)

REPORTING PERIOD: DECEMBER 31, 2002

SCHEDULE OF SALES AND USE TAXES (MOR-6)

Jurisdiction	GROSS TAXABLE SALES		SALES & USE TAX LIABILITY		
	DECEMBER 31, 2002	(a)	11/22/02 BALANCE	TOTAL COLLECTIONS	PAYMENTS
Canada	(11,771)		731	787	
Arkansas	(88)		202	6	
Arizona	(2,283)		(7,533)	148	
California	(8,543)		(2,319)	667	
Colorado	(5,930)		327	201	(3)
Florida	(20,712)		3,898	1,382	(3,8)
Georgia	(15,663)		3,122	995	(3,0)
Hawaii/adj to be made			(22)	-	
Illinois	(26,986)		696	1,666	(6)
Indiana	(2,785)		(9,324)	163	
Louisiana/adj to be made			(6)	-	
Massachusetts	(4,241)		(873)	208	
Maryland	(628)		95	31	
Michigan			708	820	(7)
Minnesota	(6,317)		3,456	410	
Minnesota/adj to be made			1,305	-	
North Carolina	(164,528)		1,005	11,372	(1,0)
New Jersey	43,745		(4,113)	(2,580)	
New York	(15,156)		629	1,116	(4)
Ohio	(17,908)		613	(1,327)	(6)
Oklahoma			(46)	-	
Pennsylvania	(18,283)		389	1,139	(3)
Tennessee	(21,175)		(2,825)	1,948	
Texas	(38,394)		3,133	3,104	(3,1)
Virginia	(28,717)		278	1,268	(2)
Washington	6,939		266	(616)	(2)
Posting errors to be adj			76	-	
			-	-	
Total	(359,423)		(6,132)	22,909	(14,8)

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(a) Reporting period for December 2002 is actually from November 22, 2002 (the petition filing date) to December 31, 2002.

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PSC INC.
CASE #: 02-15876 (SMB)
REPORTING PERIOD: DECEMBER 31, 2002

SCHEDULE OF PAYROLL & PAYROLL TAXES (MOR-7) (a)

Jurisdiction	GROSS SALARY/WAGES PAID					EMPLOYEE PAYROLL TAXES		
	Pre 11/22/02	Post 11/22/02	12/20/02	12/24/02	Total	Pre 11/22/02	Post 11/22/02	12/20/02
	109,855	1,139,482	1,298,464	247,068	2,794,869			
Federal						9,183	83,483	164,320
EIC						(4)	(33)	(4)
Social Security						3,338	30,350	51,530
Medicare						1,078	9,797	18,360
FUTA								
California						91	824	1,460
Colorado						10	93	470
Florida								
Georgia						87	794	2,200
Indiana						6	50	70
Massachusetts						10	89	150
Maryland						67	608	210
North Carolina						10	90	180
New Jersey						5	41	300
Nevada								
New York						70	636	810
Ohio						20	1,543	3,360
Oregon						3,664	33,310	60,060
Pennsylvania						34	313	630
Texas								
Utah						10	90	130
Washington								
Canada	528	5,113	6,714		12,355	216	1,430	2,110
Total	110,383	1,144,595	1,305,178	247,068	2,807,224	17,894	163,508	306,360

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Jurisdiction	Location	Asset Description	Expensed	Liability
Boulder County	Boulder, CO	Tooling (scrapped in 2001)		
Orange County	Santa Ana, CA	Tooling		
Miami Dade County	Miami, CA	office furniture/equip		
Citicorp Vendor Finance	Philadelphia, PA	2 photo copiers		
GE Capital	Pasadena, CA	14 Sharp photo copiers		
Siemens Financial	Chicago, IL	Manufacturing Equip.	3,943	
Siemens Financial	Chicago, IL	Manufacturing Equip.	1,451	
Siemens Financial	Chicago, IL	Manufacturing Equip.	2,386	
Clark County	Vancouver, WA	Tooling	34,233	
Lane County	Eugene, OR	various asset classes		24,249
Multnomah County	Portland, OR	office furniture/equip		
TOTAL			42,013	24,249

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PSC INC.
CASE #: 02-15876 (SMB)
REPORTING PERIOD: DECEMBER 31, 2002

SCHEDULE OF INCOME TAXES (MOR-9)

	11/22/2002 TAX LIABILITY	TAX REFUNDS	TAX DUE	TAX WITHHELD	T PAY
Federal Income Tax	-	-	-		
State Income Tax	-	-	-		
Pennsalvania Refund	-	(10,619.00)	-		
NY State Refund	-	(6,488.00)	-		
Foreign Income Tax	-	-	-	31,500.00	(31,500.00)
TOTAL	-	(17,107.00)	-	31,500.00	(31,500.00)

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PSC INC.
CASE #: 02-15876 (SMB)
REPORTING PERIOD: DECEMBER 31, 2002
\$ AMOUNTS IN THOUSANDS

SCHEDULE OF ACCOUNTS RECEIVABLE (MOR-9)

	----- UNAUDITED ----- December 31, 2002 -----
US	15,000
Europe	12,744
Asia	1,889
Total Accounts Receivable	29,633

Allowance For Doubtful Accounts	(621)

Net Accounts Receivable	29,012
	=====

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SCHEDULE: MOR-9

PSC INC.
Case #: 02-15876 (SMB)
Reporting Period: December 31, 2002

DEBTOR QUESTIONNAIRE (MOR-10)

	----- December 31, 2002 -----	
----- Must be completed each month -----	Yes	No
1. Have any assets been sold or transferred outside the normal course of business this period? If yes, provide an explanation below.		X
2. Have any funds been disbursed for any account other than a debtor in possession account this reporting period? If yes, provide an explanation below.		X
3. Have all postpetition tax returns been timely filed? If no, provide an explanation below.	X	
4. Are workers compensation and general liability and other necessary insurance coverages in effect? If no, provide an explanation below.	X	
5. All insurance policies are fully paid for the current period.	X	
6. All amounts relating to workers compensation and disability insurance have been paid for the current period.	X	

PSC INC.
CASE#: 02-15876 (SMB)
REPORTING PERIOD: DECEMBER 31, 2002

NOTES TO FINANCIALS

1. THE COMPANY

The accompanying financial statements are comprised of the accounts of PSC Inc. (a New York corporation) (the Company) and its wholly-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation. Certain schedules have been provided to provide direct cash receipts and disbursement information that relates solely to the debtors.

On November 22, 2002, PSC Inc. and PSC Scanning, Inc. (both US corporations) (the debtors) filed for protection from creditors under Chapter 11, of the US Bankruptcy Code. The Company filed a Plan of Reorganization outlining its anticipated treatment of various creditor classes on the same date. At the time of the filing, the debtors had negotiated a Debtor-In-Possession financing arrangement (DIP financing) to provide up to \$20 million in working capital for the period of reorganization, subject to certain performance covenants. This DIP financing was subsequently approved by the Bankruptcy Court. As of December 31, 2002, the Company was in compliance with all performance covenants.

2. SUMMARY OF SIGNIFIGANT ACCOUNTING POLICIES

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to revenue recognition, bad debts, inventories, warranty obligations, and income taxes. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. We believe the following critical accounting policies and the related judgments and estimates affect the preparation of our consolidated financial statements.

REVENUE RECOGNITION. Our policy is to recognize revenue upon delivery of our products to our customers and the fulfillment of all contractual terms and conditions, pursuant to the guidance provided by Staff Accounting Bulletin No. 101, Revenue Recognition in Financial Statements (SAB 101), issued by the Securities and Exchange Commission.

Revenue related to the sales of the Company's scanning products is generally recognized when products are shipped or services are rendered, the risk of loss has passed to the customer, the sales price is fixed or determinable, and collectibility is reasonably assured. Some distributors and dealer agreements allow for return of product and/or price protection under certain conditions

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within limited time periods. The Company maintains a reserve for sales returns and price adjustments based on historical experience and other qualitative

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factors. Estimated sales returns and price protection amounts are reserved for against revenue in the month in which it is recognized. These estimates have not differed materially from actual results. Service and maintenance sales are recognized over the contract term.

ALLOWANCE FOR DOUBTFUL ACCOUNTS. Our policy is to maintain allowances for estimated losses resulting from the inability of our customers to make required payments. Credit limits are established through a process of reviewing the financial history and stability of each customer. Where appropriate, we obtain credit rating reports and financial statements of the customer when determining or modifying their credit limits. We regularly evaluate the collectibility of our trade receivable balances based on a combination of factors. When a customer's account balance becomes past due, we initiate dialogue with the customer to determine the cause. If it is determined that the customer will be unable to meet its financial obligation to us, such as in the case of a bankruptcy filing, deterioration in the customer's operating results or financial position or other material events impacting their business, we record a specific allowance to reduce the related receivable to the amount we expect to recover given all information presently available.

We also record an allowance for all other customers based on certain other factors including the length of time the receivables are past due and historical collection experience with individual customers. If the financial conditions of those customers were to deteriorate, however, resulting in their inability to make payments, we may need to record additional allowances, which would result in additional selling, general and administrative expenses being recorded for the period in which such determination was made.

INVENTORY RESERVES. As a designer and manufacturer of bar code verification products, we are exposed to a number of economic and industry factors that could result in portions of our inventory becoming either obsolete or in excess of anticipated usage. These factors include, but are not limited to, technological changes in our markets, our ability to meet changing customer requirements, competitive pressures in products and prices, and the availability of key components from our suppliers. Our policy is to establish inventory reserves when conditions exist that suggest that our inventory may be in excess of anticipated demand, or is obsolete based upon our assumptions about future demand for our products and market conditions. We regularly evaluate the ability to realize the value of our inventory based on a combination of factors including the following: historical usage rates, forecasted sales or usage, product end of life dates, estimated current and future market values and new product introductions. Purchasing requirements and alternative usage avenues are explored within these processes to mitigate inventory exposure. When recorded, our reserves are intended to reduce the carrying value of our inventory to its net realizable value.

PRODUCT WARRANTIES. Our products are sold with warranty provisions that require us to remedy deficiencies in quality or performance of our products over a specified period of time at no cost to our customers. Our policy is to establish warranty reserves at levels that represent our estimate of the costs that will be incurred to fulfill those warranty requirements at the time that revenue is recognized. We believe that our recorded liability at December 31, 2002, is adequate to cover our future cost of materials, labor and overhead for the

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servicing of our products sold through that date. If actual product failures, or material or service delivery costs differ from our estimates, our warranty liability would need to be revised accordingly.

INCOME TAXES. The Company has recorded a valuation allowance to reduce our deferred tax assets to the amount that is more likely than not to be realized.

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The Company has assessed the valuation allowance based upon our estimate of future taxable income covering a relatively short time horizon given the volatility in the markets we serve and our historic operating results. External market data is considered in this evaluation. The availability of tax planning strategies to utilize our recorded deferred tax assets is also considered.

DEBT. Prepetition senior secured and subordinated unsecured debt was acquired from the Company's prior lenders by affiliates of Littlejohn & Co., LLC (Littlejohn), a private investment firm based in Greenwich, Connecticut. Littlejohn makes control equity investments in mid-sized companies that can benefit from operational or financial restructuring. Immediately following the debt purchase, and agreement with the terms of an arrangement between Littlejohn and the Company, the debtors filed a petition from protection from creditors under Chapter 11 of the US Bankruptcy Code. Simultaneously with the filing of the bankruptcy petition, the debtors also filed a Plan of Reorganization (the Plan) which, among other provisions, contemplates that all pre-petition debt will be converted to equity upon confirmation of the Plan

As an integral part of the arrangement between Littlejohn and the Company, a DIP financing arrangement was agreed upon, to provide working capital financing during the period of reorganization, for amounts up to \$20 million. The DIP financing arrangement provides that the Company maintain certain financial and non-financial performance covenants, including minimum revenue, cash receipts and cash disbursements results and well as cash flow and EBITDA performance measurements. In addition, there are certain non-financial performance measures related to progressing efficiently through the reorganization process. The DIP financing arrangement expires on March 31, 2003.

GOODWILL. In November 2002, in conjunction with the filing of the Chapter 11 reorganization, all goodwill was determined to be impaired. The write-off resulted in a charge of \$63 million recorded in November 2002.

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