

# ARC DOCUMENT SOLUTIONS, INC.

## FORM 10-Q (Quarterly Report)

Filed 11/14/05 for the Period Ending 09/30/05

Address	1981 N. BROADWAY, SUITE 385 WALNUT CREEK, CA 94596
Telephone	925 949-5100
CIK	0001305168
Symbol	ARC
SIC Code	7330 - Mailing, Reproduction, Commercial Art And
Industry	Business Services
Sector	Services
Fiscal Year	12/31

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

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**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 September 30, 2005

or

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

Commission File Number: 001-32407

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**AMERICAN REPROGRAPHICS COMPANY**

(Exact name of Registrant as specified in its Charter)

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

**20-1700361**  
(I.R.S. Employer  
Identification No.)

**700 North Central Avenue, Suite 550  
Glendale, California 91203  
(818) 500-0225**

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

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

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

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

As of September 30, 2005, there were 44,314,812 shares of the Registrant's common stock outstanding.

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AMERICAN REPROGRAPHICS COMPANY  
Quarterly Report on Form 10-Q  
For the Quarter Ended September 30, 2005

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**PART I. FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**AMERICAN REPROGRAPHICS COMPANY  
CONSOLIDATED BALANCE SHEETS**

	<u>December 31, 2004</u>	<u>September 30, 2005</u> (Unaudited)
	(Dollars in thousands)	
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 13,826	\$ 12,828
Accounts receivable, net	61,679	72,761
Inventories, net	6,012	7,017
Deferred taxes	1,364	2,897
Prepaid expenses and other current assets	<u>7,855</u>	<u>5,085</u>
Total current assets	90,736	100,588
Property and equipment, net	35,023	37,375
Goodwill	231,357	241,703
Other intangible assets, net	12,095	19,474
Deferred financing costs, net	6,619	4,596
Deferred taxes	—	17,815
Other assets	<u>1,504</u>	<u>1,461</u>
Total assets	<u>\$ 377,334</u>	<u>\$ 423,012</u>
<b>Liabilities and Stockholders' Equity</b>		
Current liabilities:		
Accounts payable	\$ 21,170	\$ 22,266
Accrued payroll and payroll-related expenses	11,683	11,544
Accrued expenses	24,834	23,233
Current portion of long-term debt and capital leases	<u>10,276</u>	<u>12,426</u>
Total current liabilities	67,963	69,469
Long-term debt and capital leases, net of debt discount	310,557	245,875
Mandatorily redeemable preferred membership units	27,814	—
Deferred taxes	5,634	—
Other long-term liabilities	<u>375</u>	<u>376</u>
Total liabilities	<u>412,343</u>	<u>315,720</u>
Commitments and contingencies (Note 6)		
Stockholders' equity (deficit):		
Members' deficit	(32,688)	—
Preferred stock, \$.001 par value, 25,000,000 shares authorized; zero and zero shares issued and outstanding	—	—
Common stock, \$.001 par value, 150,000,000 shares authorized; zero and 44,314,812 shares issued and outstanding	—	44
Additional paid-in capital	—	53,722
Deferred stock-based compensation	(2,527)	(2,078)
Retained earnings	—	55,550
Accumulated other comprehensive income	<u>206</u>	<u>54</u>
Total stockholders' equity (deficit)	<u>(35,009)</u>	<u>107,292</u>
Total liabilities and stockholders' equity (deficit)	<u>\$ 377,334</u>	<u>\$ 423,012</u>

The accompanying notes are an integral part of these consolidated financial statements.

**AMERICAN REPROGRAPHICS COMPANY  
CONSOLIDATED STATEMENTS OF OPERATIONS**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2005	2004	2005
	(Unaudited)			
	(Dollars in thousands, except per share data)			
Reprographics services	\$ 82,476	94,730	\$ 253,367	\$ 277,133
Facilities management	18,480	21,577	53,736	61,825
Equipment and supplies sales	9,209	11,180	29,195	30,555
Total net sales	110,165	127,487	336,298	369,513
Cost of sales	65,878	74,965	196,668	215,012
Gross profit	44,287	52,522	139,630	154,501
Selling, general and administrative expenses	26,170	28,315	81,434	83,336
Amortization of intangible assets	415	603	1,267	1,418
Income from operations	17,702	23,604	56,929	69,747
Other income	(7)	(63)	(574)	(287)
Interest expense, net	8,559	6,131	25,089	20,649
Income before income tax provision (benefit)	9,150	17,536	32,414	49,385
Income tax provision (benefit)	1,959	7,018	6,940	(8,079)
Net income	\$ 7,191	\$ 10,518	\$ 25,474	\$ 57,464
Earnings per share:				
Basic	\$ 0.20	\$ 0.24	\$ 0.72	\$ 1.37
Diluted	\$ 0.19	\$ 0.23	\$ 0.68	\$ 1.33
Weighted average common shares outstanding:				
Basic	35,487,511	44,170,226	35,487,511	42,080,404
Diluted	37,473,657	45,014,364	37,473,657	43,058,179

The accompanying notes are an integral part of these consolidated financial statements.

**AMERICAN REPROGRAPHICS COMPANY**  
**CONDENSED CONSOLIDATED STATEMENT OF**  
**CHANGES IN STOCKHOLDERS' EQUITY**

	Members' Deficit	Common Stock		Additional Paid-In Capital	Deferred Compensation (Unaudited)	Retained Earnings	Accumulated Other Comprehensive Income	Total Stockholders' Equity	
		Shares	Par Value						
Balance at December 31, 2004	\$(32,688)	—	\$ —	\$ —	—	\$ (2,527)	\$ —	206	\$ (35,009)
Amortization of deferred stock-based compensation for the period from January 1 to February 9, 2005	—	—	—	—	61	—	—	—	61
Comprehensive income for the period from January 1 to February 9, 2005:									
Net income	1,914	—	—	—	—	—	—	—	1,914
Fair value adjustment of derivatives	—	—	—	—	—	—	—	195	195
Comprehensive income									2,109
Distributions to members	(8,244)	—	—	—	—	—	—	—	(8,244)
Reorganization from LLC to "C" Corporation	39,018	35,510,011	35	(39,053)	—	—	—	—	—
Issuance of common stock in initial public offering, net of underwriting discounts	—	7,666,667	8	92,682	—	—	—	—	92,690
Issuance of common stock in exchange for warrants exercised upon initial public offering	—	754,476	1	—	—	—	—	—	1
Direct costs of initial public offering	—	—	—	(3,899)	—	—	—	—	(3,899)
Amortization of deferred stock-based compensation for the period from February 10 to September 30, 2005	—	—	—	—	388	—	—	—	388
Issuance of common stock under Employee Stock Purchase Plan	—	177,058	—	1,956	—	—	—	—	1,956
Stock options exercised	—	206,600	—	1,036	—	—	—	—	1,036
Tax benefit from exercise of stock options	—	—	—	1,000	—	—	—	—	1,000
Comprehensive income for the period from February 10 to September 30, 2005:									
Net income	—	—	—	—	—	55,550	—	—	55,550
Fair value adjustment of derivatives, net of tax effects	—	—	—	—	—	—	—	(347)	(347)
Comprehensive income									55,203
Balance at September 30, 2005	\$ —	44,314,812	\$ 44	\$ 53,722	\$ (2,078)	\$55,550	\$ 54	\$ 107,292	

The accompanying notes are an integral part of these consolidated financial statements.

**AMERICAN REPROGRAPHICS COMPANY**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

	Nine Months Ended September 30,	
	2004	2005
	(Unaudited)	
	(Dollars in thousands)	
<b>Operating activities</b>		
Net income	\$ 25,474	\$ 57,464
Adjustments to reconcile net income to net cash provided by operating activities:		
Accretion of yield on redeemable preferred member units	1,494	449
Allowance for doubtful accounts	1,110	1,052
Reserve for inventory obsolescence	68	76
Depreciation	12,739	12,489
Amortization of intangible assets	1,267	1,418
Amortization of deferred financing costs	1,855	1,212
Deferred income taxes	689	(24,982)
Write-off of deferred financing costs	—	1,683
Amortization of deferred stock-based compensation	332	449
Changes in operating assets and liabilities, net of effect of business acquisitions:		
Accounts receivable, net	(10,287)	(7,150)
Inventory	29	211
Prepaid expenses and other assets	(572)	1,676
Accounts payable and accrued expenses	8,221	(3,460)
Net cash provided by operating activities	42,419	42,587
<b>Investing activities</b>		
Capital expenditures	(4,772)	(3,376)
Payments for businesses acquired, net of cash acquired and including other cash payments associated with acquisitions	(2,893)	(16,299)
Other	54	(35)
Net cash used in investing activities	(7,611)	(19,710)
<b>Financing activities</b>		
Proceeds from initial public offering, net of underwriting discounts	—	92,690
Direct costs of initial public offering	—	(1,487)
Proceeds from stock option exercises	—	1,036
Proceeds from issuance of common stock under Employee Stock Purchase Plan	—	1,956
Redemption of preferred member units	—	(28,263)
Proceeds from borrowings under debt agreements	1,000	13,000
Payments on long-term debt under debt agreements	(36,191)	(94,204)
Payment of loan fees	(355)	(359)
Member distributions	(4,569)	(8,244)
Net cash used in financing activities	(40,115)	(23,875)
Net decrease in cash and cash equivalents	(5,307)	(998)
Cash and cash equivalents at beginning of period	17,315	13,826
Cash and cash equivalents at end of period	\$ 12,008	\$ 12,828
<b>Supplemental disclosure of cash flow information Noncash investing and financing activities</b>		
Noncash transactions include the following:		
Capital lease obligations incurred	\$ 6,274	\$ 9,191
Issuance of subordinated notes in connection with the acquisition of businesses	\$ 250	\$ 8,230
Change in fair value of derivatives	\$ 479	\$ (152)

The accompanying notes are an integral part of these consolidated financial statements.

**AMERICAN REPROGRAPHICS COMPANY**  
**Notes to Consolidated Financial Statements (Unaudited)**

**1. Description of Business and Basis of Presentation**

American Reprographics Company (ARC or the Company) is the leading reprographics company in the United States providing business-to-business document management services to the architectural, engineering and construction industry, or AEC industry. ARC also provides these services to companies in non-AEC industries, such as technology, financial services, retail, entertainment, and food and hospitality, that also require sophisticated document management services. The Company conducts its operations through its wholly-owned operating subsidiary, American Reprographics Company, L.L.C., a California limited liability company (Opco), and its subsidiaries.

***Reorganization and Initial Public Offering***

Prior to the consummation of the Company's initial public offering on February 9, 2005, the Company was reorganized (the Reorganization) from a California limited liability company (American Reprographics Holdings, L.L.C. or Holdings) to a Delaware corporation (American Reprographics Company). In connection with the Reorganization, the members of Holdings exchanged their common member units for common stock of ARC. Each option issued to purchase Holdings' common member units under Holding's equity option plan was exchanged for an option exercisable for shares of ARC's common stock with the same exercise prices and vesting terms as the original grants. In addition, all outstanding warrants to purchase common units of Holdings were exchanged for shares of ARC's common stock.

On February 9, 2005, the Company closed an initial public offering (IPO) of its common stock at \$13.00 per share, consisting of 7,666,667 newly issued shares sold by the company and 5,683,333 outstanding shares sold by the selling stockholders. The Company used net proceeds from its IPO to prepay \$50.7 million of its \$225 million senior second priority secured term loan facility and \$9 million of its \$100 million senior first priority secured term loan facility. As required by the operating agreement of Holdings, the Company also repurchased all of the preferred equity of Holdings upon the closing of the Company's initial public offering with \$28.3 million of the net proceeds from the IPO. Please see our Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 and our 2004 Annual Report on Form 10-K for additional information concerning our IPO.

Due to their tax attributes, certain members of Holdings have in the past elected to receive less than their proportionate share of distributions for income taxes as a result of a difference in the tax basis of their equity interest in Holdings. In accordance with the terms of the operating agreement of Holdings, the Company made a cash distribution of \$8.2 million to such members on February 9, 2005 in connection with the consummation of its IPO to bring their proportionate share of tax distributions equal to the rest of the members of Holdings. These distributions have been reclassified into additional paid-in capital in the Company's consolidated balance sheet as of September 30, 2005 in connection with the Reorganization in February 2005. See the accompanying consolidated statement of changes in stockholders' equity for the nine months ended September 30, 2005 for additional details regarding the changes in the Company's capital accounts resulting from the Reorganization.

***Basis of Presentation***

The accompanying consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and in conformity with the requirements of the Securities and Exchange Commission. As permitted under those rules, certain footnotes or other financial information required by GAAP for complete financial statements have been condensed or omitted. In management's opinion, the interim consolidated financial statements presented herein reflect all adjustments of a normal and recurring nature that are necessary to fairly present the interim consolidated financial statements. All material intercompany accounts and transactions have been eliminated in consolidation. The operating results for the three and nine months ended September 30, 2005 are not necessarily indicative of the results that may be expected for the year ending December 31, 2005.

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The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. We evaluate our estimates and assumptions on an ongoing basis and rely on historical experience and various other factors that we believe to be reasonable under the circumstances to determine such estimates. Actual results could differ from those estimates and such differences may be material to the consolidated financial statements.

These interim consolidated financial statements and notes should be read in conjunction with the consolidated financial statements and notes included in the Company's 2004 Annual Report on Form 10-K. The accounting policies used in preparing these interim consolidated financial statements are the same as those described in our 2004 Annual Report on Form 10-K.

### 2. Accounting for Equity-Based Compensation

The Company accounts for grants of options to employees to purchase its common stock using the intrinsic value method in accordance with APB Opinion No. 25 and FIN No. 44, "Accounting for Certain Transactions Involving Stock Compensation". As permitted by SFAS No. 123 and as amended by SFAS No. 148, the Company has chosen to continue to account for such option grants under APB Opinion No. 25 and provide the expanded disclosures specified in SFAS No. 123, as amended by SFAS No. 148.

Had compensation cost for the Company's option grants been determined based on their fair value at the grant date for awards consistent with the provisions of SFAS No. 123, the Company's net income attributable to common stockholders and earnings per share for the three and nine months ended September 30, 2004 and 2005 would have been the adjusted pro forma amounts indicated below:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2005	2004	2005
	(Unaudited)			
	(Dollars in thousands, except per share data)			
Net income:				
As reported	\$ 7,191	\$ 10,518	\$ 25,474	\$ 57,464
Equity-based employee compensation cost, net of related tax effects, included in as reported net income	89	83	179	265
Equity-based employee compensation cost, net of related tax effects, that would have been included in the determination of net income if the fair value method had been applied	(122)	(106)	(290)	(350)
Proforma	<u>\$ 7,158</u>	<u>\$ 10,495</u>	<u>\$ 25,363</u>	<u>\$ 57,379</u>
Basic earnings per share:				
As reported	\$ 0.20	\$ 0.24	\$ 0.72	\$ 1.37
Equity-based employee compensation cost, net of related tax effects, included in as reported net income	—	—	0.01	0.01
Equity-based employee compensation cost, net of related tax effects, that would have been included in the determination of net income if the fair value method had been applied	—	—	(0.01)	(0.01)
Proforma	<u>\$ 0.20</u>	<u>\$ 0.24</u>	<u>\$ 0.72</u>	<u>\$ 1.37</u>
Diluted earnings per share:				
As reported	\$ 0.19	\$ 0.23	\$ 0.68	\$ 1.33
Equity-based employee compensation cost, net of related tax effects, included in as reported net income	—	—	—	0.01
Equity-based employee compensation cost, net of related tax effects, that would have been included in the determination of net income if the fair value method had been applied	—	—	(0.01)	(0.01)
Proforma	<u>\$ 0.19</u>	<u>\$ 0.23</u>	<u>\$ 0.67</u>	<u>\$ 1.33</u>

For purposes of computing the pro forma disclosures required by SFAS No. 123, the fair value of each option granted to employees and directors is estimated using the Black-Scholes option-pricing model with the following weighted-average assumptions for the three months and nine months ended September 30, 2004 and 2005: dividend yields of 0% for all periods; expected volatility of 32.4% and 28.3%, respectively; risk-free interest rates of 3.0% and 2.9%, respectively; and expected lives of 2.5 years for all periods.

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The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options, which do not have vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions, including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

During 2004, the Company granted 307,915 options to purchase common membership units to employees with exercise prices ranging from \$5.62 to \$6.85 per unit. The fair market value of the Company's common member units on the date of grant was \$16 per unit. In connection with the issuances, the Company recorded a deferred compensation charge of \$3.1 million in connection with the issuance as the exercise price of the units was less than the estimated fair market value of the Company's membership units as of the date of grant after giving consideration to the anticipated fair value of the membership units during the one-year period preceding the Company's initial public offering which was consummated on February 9, 2005. The Company will amortize the deferred compensation charge over the vesting period of the options, generally five years. As of September 30, 2005, the Company has cumulatively amortized \$1.0 million of the deferred compensation charge.

During the third quarter of 2005, the company issued 206,600 shares of its common stock resulting from exercises of stock options in accordance with the American Reprographics Company 2005 Stock Plan which the Company adopted in connection with the consummation of its IPO in February 2005. Such options were exercised at prices ranging from \$4.87 to \$6.85 per option, resulting in approximately \$1.0 million of cash proceeds to the company.

In December 2004, the FASB issued SFAS No. 123R (revised 2004), "Share-Based Payment." SFAS No. 123R addresses the accounting for share-based payment transactions in which a company receives employee services in exchange for either equity instruments of the company or liabilities that are based on the fair value of the company's equity instruments or that may be settled by the issuance of such equity instruments. SFAS No. 123R eliminates the ability to account for share-based compensation transactions using the intrinsic method that is currently used and requires that such transactions be accounted for using a fair value-based method and recognized as expense in the consolidated statement of operations. The effective date of SFAS No. 123R was originally set for interim and annual periods beginning after June 15, 2005. On April 15, 2005, the SEC adopted an amendment to Regulation S-X that delays the date by which the Company must adopt SFAS No. 123R. Under these new rules, the Company is required to adopt SFAS 123R on January 1, 2006, although earlier adoption is permitted. The Company is in the process of reviewing the provisions of SFAS No. 123R and plans to adopt this statement on January 1, 2006. However, the Company has made no definitive decisions regarding transition methods or option valuation methods.

### 3. Employee Stock Purchase Plan

The Company adopted the American Reprographics Company 2005 Employee Stock Purchase Plan (the ESPP) in connection with the consummation of its IPO in February 2005. Under the ESPP, purchase rights may be granted to eligible employees subject to a calendar year maximum per eligible employee of the lesser of (i) 400 shares of common stock, or (ii) a number of shares of common stock having an aggregate fair market value of \$10,000 as determined on the date of purchase. The purchase price of shares of common stock offered under the ESPP is equal to the lesser of 85% of the fair market value of such shares of common stock (i) on the offering date, or (ii) on the purchase date. The first day of an offering period is designated as the offering date.

In January 2005, the Company's Board of Directors authorized an initial offering of purchase rights under the ESPP. The initial offering period began on February 3, 2005 and will end on April 30, 2007. Five purchase dates have been designated under such initial offering period, as follows: July 31, 2005, December 31, 2005, June 30, 2006, December 31, 2006 and April 30, 2007.

During the third quarter of 2005, the Company issued 177,058 shares of its common stock to approximately 840 eligible employees in accordance with the ESPP at a purchase price of \$11.05 per share, resulting in approximately \$2.0 million of cash proceeds to the Company.

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### 4. Long-Term Debt

Long-term debt consists of the following:

	December 31, 2004	September 30, 2005 (Unaudited)
	(Dollars in thousands)	
Borrowings from senior secured First Priority — Revolving Credit Facility; any unpaid principal and interest due December 18, 2008	\$ —	\$ —
Borrowings from senior secured First Priority — Term Loan Credit Facility; variable interest payable quarterly (5.26% and 5.52% interest rate at December 31, 2004 and September 30, 2005, respectively); principal payable in varying quarterly installments; any unpaid principal and interest due June 18, 2009	94,800	73,106
Borrowings from senior secured Second Priority — Term Loan Credit Facility; variable interest payable quarterly (8.92% and 10.64% interest rate at December 31, 2004 and September 30, 2005, respectively); any unpaid principal and interest due December 18, 2009	208,231	157,500
Various subordinated notes payable; interest ranging from 5% to 11%; principal and interest payable monthly through September 2010	4,833	10,170
Various capital leases; interest rates ranging to 15.9%; principal and interest payable monthly through September 2009	14,688	18,705
	<u>322,552</u>	<u>259,481</u>
Less debt discount on Second Priority Credit Facility	(1,719)	(1,180)
	<u>320,833</u>	<u>258,301</u>
Less current portion	(10,276)	(12,426)
	<u>\$ 310,557</u>	<u>\$ 245,875</u>

On February 9, 2005, the Company used a portion of the proceeds from its initial public offering to prepay \$50.7 million of its \$225 million senior second priority secured term loan facility and \$9 million of its \$100 million senior first priority secured term loan facility. As a result of these debt prepayments, the Company wrote off \$1.5 million of deferred financing costs in February 2005 which is included in interest expense in the accompanying consolidated financial statements.

On July 5, 2005, the Company entered into an Amended and Restated Credit and Guaranty Agreement (the Amended Credit Agreement) with its senior lenders which amended the structure of the Company's senior secured first priority credit facilities in order to (i) support the Company's growth initiatives which include, among others, strategic acquisitions and capital expenditures for the opening of new branches and the expansion of facilities management programs, and (ii) reduce the interest rate on the Company's borrowings under the First Priority Term Loan Credit Facility. The significant amendments to the terms of the Company's senior secured credit facilities include the following:

- The Company's existing First Priority Revolving Credit Facility and First Priority Term Loan Credit Facility was restructured into a new senior secured credit facility aggregating up to \$122.3 million, consisting of a \$77.3 million Tranche C Term Loan Facility, a \$30 million Revolving Credit Facility, and permits the Company, as needed for the purpose of financing any future business acquisitions, to request the establishment of one or more new term loan commitments by an amount not to exceed \$15 million in the aggregate. The terms and provisions of any such new term loans will be identical to the Tranche C Term Loan Facility, including, without limitation, with respect to amortization, interest and maturity.
- Borrowings under the new Tranche C Term Loan Facility will bear an interest rate calculated at either (i) a Eurodollar rate plus 1.75% per annum, or (ii) an Index Rate, as defined in the Amended Credit Agreement, plus 0.75% per annum. This represents a 125-basis point reduction in the annual interest rate as compared to the annual interest rate on the Company's borrowings under the existing First Priority Term Loan Credit Facility which, prior to July 5, 2005, were subject to an interest rate equal to either (i) a Eurodollar rate plus 3.0% per annum, or (ii) an Index Rate, as defined in the existing credit agreement, plus 2.0% per annum.
- Certain debt covenant thresholds were adjusted to make them less restrictive and thereby providing the Company with greater operating flexibility. Such adjustments include the following:
  - o An increase in the aggregate purchase price limitation for business acquisitions for the fiscal year ending December 31, 2005;

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- o An increase in the limitation for the aggregate amount of new seller notes payable that may be issued in connection with business acquisitions;
- o An increase in the annual threshold for earnout obligations that the Company may undertake in connection with business acquisitions;
- o An increase in the threshold for capital expenditures during any trailing twelve-month period;
- o An increase in the limitation on capital lease obligations outstanding;
- o A reduction in the maximum leverage ratio threshold, as defined in the Amended Credit Agreement, from 4.90 to 3.75;
- o Elimination of the scheduled increase in the fixed charge coverage ratio threshold. In accordance with the Amended Credit Agreement, the fixed charge coverage ratio threshold will remain constant at 1.10.

Except as described above, all other material terms and conditions, including the maturity dates, of the Company's existing senior secured credit facilities remained similar to those as described in Note 4 – "Long-Term Debt" to our consolidated financial statements included in our 2004 Annual Report on Form 10-K.

The Amended Credit Agreement is not considered to represent a significant modification for financial reporting purposes. As a result, the Company capitalized the \$0.2 million of amendment fees incurred as debt issuance costs which will be amortized over the term of the Amended Credit Agreement. Professional fees and other related costs incurred in connection with the Amended Credit Agreement were expensed as incurred.

## 5. Income Taxes

Holdings and Opco, through which a substantial portion of the Company's business was operated prior to the Reorganization, are limited liability companies which are taxed as partnerships. As a result, the members of Holdings pay income taxes on the earnings of Opco, which are passed through to Holdings. In accordance with Holdings' operating agreement, Holdings made cash distributions to its members to provide them with funds to pay taxes owed for their share of Holdings profits as a limited liability company.

Certain divisions are consolidated in Holdings and are treated as separate corporate entities for income tax purposes (the consolidated corporations). Prior to the Reorganization, these consolidated corporations paid income taxes and recorded provisions for income taxes in their financial statements. As a result of the Company's reorganization to a Delaware corporation in February 2005, ARC's consolidated earnings became subject to federal, state and local taxes at a combined statutory rate of approximately 42%.

The Company's income tax provision (benefit) for the three and nine months ended September 30, 2004 and 2005 are as follows:

	<u>Three Months Ended</u>		<u>Nine Months Ended</u>	
	<u>September 30,</u>		<u>September 30,</u>	
	<u>2004</u>	<u>2005</u>	<u>2004</u>	<u>2005</u>
	(Unaudited)			
	(Dollars in thousands)			
Current:				
Federal	\$ 1,527	\$ 5,136	\$ 4,930	\$ 13,747
State	444	1,293	1,321	3,156
	<u>1,971</u>	<u>6,429</u>	<u>6,251</u>	<u>16,903</u>
Deferred:				
Deferred income tax provision, excluding the effects of the Reorganization	<u>(12)</u>	<u>589</u>	<u>689</u>	<u>2,719</u>
Income tax provision, excluding the effects of the Reorganization	<u>1,959</u>	<u>7,018</u>	<u>6,940</u>	<u>19,622</u>
Deferred income tax benefit as a result of the Reorganization	<u>—</u>	<u>—</u>	<u>—</u>	<u>(27,701)</u>
Income tax provision (benefit)	<u>\$ 1,959</u>	<u>\$ 7,018</u>	<u>\$ 6,940</u>	<u>\$ (8,079)</u>

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The Company's net income tax benefit of \$8.1 million during the nine months ended September 30, 2005 includes a one-time deferred income tax benefit of \$27.7 million recorded in February 2005 in connection with the Company's reorganization from a California limited liability company (LLC) to a Delaware corporation. This non-recurring income tax benefit is related to the setting up of the deferred income tax accounts from the assets and liabilities that were previously in the LLC, primarily comprised of tax-deductible goodwill and other temporary differences. This resulted in an increase in net deferred tax assets of \$27.7 million and a corresponding deferred income tax benefit for the same amount.

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The Company's consolidated deferred tax assets and liabilities as of December 31, 2004 and September 30, 2005 consist of the following:

	<u>December 31,</u> <u>2004</u>	<u>September 30,</u> <u>2005</u> (Unaudited)
	(Dollars in thousands)	
Deferred tax assets (liabilities):		
Current portion:		
Financial statement accruals not currently deductible	\$ 1,206	\$ 2,738
State taxes	<u>158</u>	<u>159</u>
Net current deferred tax assets	1,364	2,897
Non-current portion:		
Excess of income tax basis over net book value for financial reporting purposes of intangible assets	—	32,172
Excess of income tax basis over net book value for financial reporting purposes of property, plant and equipment	—	2,276
Deferred stock-based compensation	—	388
Excess of net book value for financial reporting purposes over income tax basis of property, plant and equipment	(1,653)	—
Excess of net book value for financial reporting purposes over income tax basis of intangible assets	<u>(3,981)</u>	<u>(17,021)</u>
Net non-current deferred tax assets (liabilities)	(5,634)	17,815
Net deferred tax assets (liabilities)	<u>\$ (4,270)</u>	<u>\$ 20,712</u>

A reconciliation of the statutory federal income tax rate to the Company's effective tax rate is as follows:

	<u>Three Months Ended</u> <u>September 30,</u>		<u>Nine Months Ended</u> <u>September 30,</u>	
	<u>2004</u>	<u>2005</u>	<u>2004</u>	<u>2005</u>
	(Unaudited)			
Statutory federal income tax rate	34.0%	35.0%	34.0%	35.0%
State taxes	3.5%	4.8%	3.5%	4.8%
Income of the LLC not taxed at the LLC level	(17.7)%	—	(17.7)%	(0.3)%
Other	<u>1.6%</u>	<u>0.3%</u>	<u>1.6%</u>	<u>0.2%</u>
Effective income tax rate before non-recurring income tax benefit due to Reorganization	21.4%	40.1%	21.4%	39.7%
Non-recurring income tax benefit due to reorganization	<u>—</u>	<u>—</u>	<u>—</u>	<u>(56.0)%</u>
Effective income tax rate	<u>21.4%</u>	<u>40.1%</u>	<u>21.4%</u>	<u>(16.3)%</u>

## 6. Commitments and Contingencies

The Company is a creditor and participant in the Chapter 7 Bankruptcy of Louis Frey Company, Inc., or LF Co., which is pending in the United States Bankruptcy Court, Southern District of New York. The Company managed LF Co. under a contract from May through September of 2003. LF Co. filed for Bankruptcy protection in August 2003, and the proceeding was converted to a Chapter 7 liquidation in October 2003. On or about June 30, 2004, the Bankruptcy Estate Trustee filed a complaint in the LF Co. Bankruptcy proceeding against the Company, which was amended on or about July 19, 2004, alleging, among other things, breach of contract, breach of fiduciary duties, conversion, unjust enrichment, tortious interference with contract, unfair competition and false commercial promotion in violation of The Lanham Act, misappropriation of trade secrets and fraud regarding the Company's handling of the assets of LF Co. The Trustee claims damages of not less than \$9.5 million, as well as punitive damages and treble damages with respect to the Lanham Act claims. Previously, on or about October 10, 2003, a secured creditor of LF Co., Merrill Lynch Business Financial Services, Inc., or Merrill, had filed a complaint in the LF Co. Bankruptcy proceeding against the Company, which was most recently amended on or about July 6, 2004. Merrill's claims are duplicated in the Trustee's suit. The Company, in turn, has filed answers and counterclaims denying liability to the Trustee and seeking reimbursement of all costs and damages sustained as a result of the Trustee's actions and in the Company's efforts to assist LF Co. The Company believes that it has meritorious defenses as well as substantial counterclaims against Merrill Lynch and the Trustee. The Company intends to vigorously contest the above matters. Based on the discovery and depositions to date, the Company does not believe



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In December 2004, the FASB issued SFAS No. 153, “Exchanges of Nonmonetary Assets, an amendment of APB Opinion No. 29.” SFAS No. 153 is based on the principle that exchanges of nonmonetary assets should be measured based on the fair value of the assets exchanged. APB Opinion No. 29, “Accounting for Nonmonetary Transactions,” provided an exception to its basic measurement principle (fair value) for exchanges of similar productive assets. Under APB Opinion No. 29, an exchange of a productive asset for a similar productive asset was based on the recorded amount of the asset relinquished. SFAS No. 153 eliminates this exception and replaces it with an exception of exchanges of nonmonetary assets that do not have commercial substance. The Company does not believe that the adoption of SFAS No. 153 will have a material impact on its consolidated financial statements.

### **Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations**

*The following discussion should be read in conjunction with our consolidated financial statements and the related notes included in this report, as well as Management’s Discussion and Analysis included in our 2004 Annual Report on Form 10-K .*

*In addition to historical information, this report on Form 10-Q contains certain forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. These statements relate to future events or future financial performance, and include statements regarding the Company’s business strategy, timing of, and plans for, the introduction of new products and enhancements, future sales, market growth and direction, competition, market share, revenue growth, operating margins and profitability. All forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements, expressed or implied, by these forward looking statements. In some cases, you can identify forward-looking statements by terminology such as “may,” “will,” “should,” “expects,” “intends,” “plans,” “anticipates,” “believes,” “estimates,” “predicts,” “potential,” “continue,” or the negative of these terms or other comparable terminology. These statements are only predictions and are based upon information available to the Company as of the date of this report. We undertake no on-going obligation, other than that imposed by law, to update these forward-looking statements.*

*Actual results could differ materially from our current expectations. Factors that could cause actual results to differ materially from current expectations, include among others, the following: (i) general economic conditions, such as changes in non-residential construction spending, GDP growth, interest rates, employment rates, office vacancy rates, and government expenditures; (ii) a downturn in the architectural, engineering and construction industry; (iii) competition in our industry and innovation by our competitors; (iv) our failure to anticipate and adapt to future changes in our industry; (v) failure to continue to develop and introduce new products and services successfully; (vi) our inability to charge for value-added services we provide our customers to offset potential declines in print volume; (vii) adverse developments affecting the State of California, including general and local economic conditions, macroeconomic trends, and natural disasters; (viii) our inability to successfully identify and manage our acquisitions or open new branches; (ix) our inability to successfully monitor and manage the business operations of our subsidiaries and uncertainty regarding the effectiveness of financial and management policies and procedures we established to improve accounting controls; (x) adverse developments concerning our relationships with certain key vendors; and (xi) the loss of key personnel and qualified technical staff.*

*Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. These forward-looking statements are subject to numerous risks and uncertainties, including, but not limited to, the risks and uncertainties described in the “Risk Factors” section of our 2004 Annual Report on Form 10-K . You are urged to carefully consider these factors. All forward-looking statements attributable to us are expressly qualified in their entirety by the foregoing cautionary statements.*

### **Overview**

We are the leading reprographics company in the United States providing business-to-business document management services to the architectural, engineering and construction industry, or AEC industry. We also provide

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these services to companies in non-AEC industries, such as the technology, financial services, retail, entertainment, and food and hospitality industries, that also require sophisticated document management services.

We operate more than 200 reprographics service centers in over 150 cities in 30 states throughout the United States and the District of Columbia including four reprographics service centers in the Toronto metropolitan area and one in Mexico City, Mexico. Our reprographics service centers are located in close proximity to the majority of our customers and offer pickup and delivery services within a 15 to 30 mile radius. These service centers are arranged in a hub and satellite structure and are digitally connected as a cohesive network, allowing us to provide our services both locally and nationally. We serve more than 65,000 active customers and employ over 3,600 people, including a sales force of approximately 280 employees.

On February 9, 2005, the Company closed an initial public offering (IPO) of its common stock at \$13.00 per share, consisting of 7,666,667 newly issued shares sold by the company and 5,683,333 outstanding shares sold by the selling stockholders. The Company used net proceeds from its IPO to prepay \$50.7 million of its \$225 million senior second priority secured term loan facility and \$9 million of its \$100 million senior first priority secured term loan facility. As required by the operating agreement of Holdings, the Company also repurchased all of the preferred equity of Holdings upon the closing of the Company's initial public offering with \$28.3 million of the net proceeds from the IPO. Please see our Quarterly Report on Form 10-Q for the quarter ended March 31, 2005 and our 2004 Annual Report on Form 10-K for additional information concerning our IPO.

The key financial measures used by our management to operate and assess the performance of our business are Net Sales and Costs and Expenses. These factors are discussed in the "Key Financial Measures" section of Management's Discussion and Analysis of Financial Condition and Results of Operation in our 2004 Annual Report on Form 10-K.

### Non-GAAP Measures

EBIT and EBITDA (and related ratios presented in this report) are supplemental measures of our performance that are not required by, or presented in accordance with GAAP. These measures are not measurements of our financial performance under GAAP and should not be considered as alternatives to net income, income from operations, or any other performance measures derived in accordance with GAAP or as an alternative to cash flow from operating, investing or financing activities as a measure of our liquidity.

EBIT represents net income before interest and taxes. EBITDA represents net income before interest, taxes, depreciation and amortization. We present EBIT and EBITDA (and related ratios presented in this report) because we consider them important supplemental measures of our performance and liquidity and believe that such measures are meaningful to investors because they are used by management for the reasons discussed below.

We use EBIT as a metric to measure and compare the performance of our divisions. We operate our 40 divisions as separate business units, but manage debt and taxation at the corporate level. As a result, EBIT is the best measure of divisional profitability and the most useful metric by which to measure and compare the performance of our divisions. We also use EBIT as a metric to measure performance for the purpose of determining compensation at the division level and use EBITDA to measure performance and determine compensation at the consolidated level. We also use EBITDA as a metric to manage cash flow from our divisions to the corporate level and to determine the financial health of each division. As noted above, because our divisions do not incur interest or income tax expense, the cash flow from each division should be equal to the corresponding EBITDA of each division, assuming no other changes to a division's balance sheet. As a result, we reconcile EBITDA to cash flow on a monthly basis as one of our key internal controls. We also use EBIT and EBITDA to evaluate potential acquisitions and to evaluate whether to incur capital expenditures. In addition, certain covenants in our credit agreements require compliance with financial ratios based on EBITDA, adjusted for certain items as defined in our credit agreements.

EBIT and EBITDA (and related ratios presented in this report) have limitations as analytical tools, and you should not consider them in isolation, or as a substitute for analysis of our results as reported under GAAP. Some of these limitations are:

- they do not reflect our cash expenditures, or future requirements for capital expenditures and contractual commitments;



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The following is a reconciliation of net income to EBIT and EBITDA:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2005 (Unaudited)	2004	2005
Net income	\$ 7,191	\$ 10,518	\$ 25,474	\$ 57,464
Interest expense, net	8,559	6,131	25,089	20,649
Income tax provision (benefit)	1,959	7,018	6,940	(8,079)
EBIT	17,709	23,667	57,503	70,034
Depreciation and amortization	4,753	5,018	14,006	13,907
EBITDA	<u>\$ 22,462</u>	<u>\$ 28,685</u>	<u>\$ 71,509</u>	<u>\$ 83,941</u>

The following is a reconciliation of our net income margin to our EBIT margin and EBITDA margin:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2005 (Unaudited)	2004	2005
Net income margin	6.5%	8.3%	7.6%	15.6%
Interest expense, net	7.8%	4.8%	7.5%	5.6%
Income tax provision (benefit)	1.8%	5.5%	2.1%	(2.2%)
EBIT margin	16.1%	18.6%	17.1%	18.9%
Depreciation and amortization	4.3%	3.9%	4.2%	3.8%
EBITDA margin	<u>20.4%</u>	<u>22.5%</u>	<u>21.3%</u>	<u>22.7%</u>

### Impact of Conversion from an LLC to a Corporation

Immediately prior to our initial public offering in February 2005, we reorganized from a California limited liability company (LLC) to a Delaware corporation, American Reprographics Company (the Reorganization). In connection with the Reorganization, we recorded a one-time deferred income tax benefit of \$27.7 million in February 2005 related to the setting up of the deferred income tax accounts from the assets that were previously in the LLC, primarily comprised of tax-deductible goodwill. This resulted in an increase in our deferred tax assets of \$27.7 million and a corresponding deferred income tax benefit for the same amount. See Note 5 – “Income Taxes” to our consolidated financial statements included in this report for additional details concerning this non-recurring deferred income tax benefit recorded in connection with the Reorganization.

Going forward after the consummation of the Reorganization, we do not expect any significant impact on our operations as a result of the Reorganization apart from an increase in our effective tax rate due to corporate level taxes, which will be offset by the elimination of tax distributions to our members and the recognition of deferred income taxes upon our conversion from a California limited liability company to a Delaware corporation.

### Income Taxes

Holdings and Opco, through which a substantial portion of our business was operated prior to our reorganization in February 2005, are limited liability companies which are taxed as partnerships. As a result, the members of Holdings paid income taxes on the earnings of Opco which were passed through to Holdings. Certain divisions were consolidated in Holdings and were treated as separate corporate entities for income tax purposes (the consolidated corporations). These consolidated corporations paid income tax and record provisions for income taxes

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in their financial statements. See Note 5 – “Income Taxes” to our consolidated financial statements included in this report for additional details concerning income taxes.

The unaudited pro forma incremental income tax provision and unaudited proforma earnings per common member unit amounts reflected in the following table were calculated as if our Reorganization became effective on January 1, 2004, and excludes the one-time deferred income tax benefit of \$27.7 million recorded in February 2005 in connection with our Reorganization. Our effective income tax rate during the three and nine months ended September 30, 2005, calculated as if our Reorganization became effective on January 1, 2004 and excluding the \$27.7 million non-recurring deferred income tax benefit, was 40.0% and 40.4%, respectively. These are lower than our proforma effective income tax rate of 45.2% for the same periods in 2004 primarily due to the nondeductible interest expense on our preferred equity which was redeemed in February 2005.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2005	2004	2005
	(Unaudited)			
	(Dollars in thousands, except per share data)			
Net income	\$ 7,191	\$ 10,518	\$ 25,474	\$ 57,464
Deferred income tax benefit due to Reorganization	—	—	—	(27,701)
Proforma net income, excluding deferred income tax benefit due to Reorganization	7,191	10,518	25,474	29,763
Unaudited pro forma incremental income tax provision	(2,178)	—	(7,714)	(333)
Unaudited pro forma net income	<u>\$ 5,013</u>	<u>\$ 10,518</u>	<u>\$ 17,760</u>	<u>\$ 29,430</u>
Unaudited pro forma earnings per share:				
Basic	\$ 0.14	\$ 0.24	\$ 0.50	\$ 0.70
Diluted	\$ 0.13	\$ 0.23	\$ 0.47	\$ 0.68

## Results of Operations

The following table provides information on the percentages of certain items of selected financial data compared to total net sales for the periods indicated:

	As a Percentage of Net Sales			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2005	2004	2005
	(Unaudited)			
Reprographics services	74.9%	74.3%	75.3%	75.0%
Facilities management	16.8	16.9	16.0	16.7
Equipment and supplies sales	8.3	8.8	8.7	8.3
Total net sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	<u>59.8</u>	<u>58.8</u>	<u>58.5</u>	<u>58.2</u>
Gross profit	40.2	41.2	41.5	41.8
Selling, general and administrative expenses	23.8	22.2	24.2	22.6
Amortization of intangibles	<u>0.4</u>	<u>0.5</u>	<u>0.4</u>	<u>0.4</u>
Income from operations	16.1	18.5	16.9	18.9
Other income	0.0	0.0	0.2	0.1
Interest expense, net	<u>(7.8)</u>	<u>(4.8)</u>	<u>(7.5)</u>	<u>(5.6)</u>
Income before income tax provision (benefit)	8.3	13.8	9.6	13.4
Income tax provision (benefit)	<u>1.8</u>	<u>5.5</u>	<u>2.1</u>	<u>(2.2)</u>
Net income	<u>6.5%</u>	<u>8.3%</u>	<u>7.6%</u>	<u>15.6%</u>

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Our operating results remained strong during the third quarter of 2005 due to continued high demand for commercial office space nationwide driven by strong job creation and continued expansion of the overall economy. Our efforts to expand our national footprint of reprographics centers as well as our facilities management programs have also been important contributors to the growth in our net sales.

We continue to focus on our key opportunities, which include: the expansion of our market share, our national footprint of reprographics centers, and our facilities management programs; the establishment of our PlanWell technology as the industry standard for procuring digital reprographics online; and the expansion of our service offerings to non-AEC related industries.

### Three and Nine Months Ended September 30, 2005 Compared to Three and Nine Months Ended September 30, 2004

	Three Months Ended September 30,		Incr (Decr)		Nine Months Ended September 30,		Incr (Decr)	
	2004	2005	\$	%	2004	2005	\$	%
(Unaudited) (Dollars in thousands)								
Reprographics services	82.5	94.7	12.2	14.8%	253.4	277.1	23.7	9.4%
Facilities management	18.5	21.6	3.1	16.8%	53.7	61.8	8.1	15.1%
Equipment and supplies sales	<u>9.2</u>	<u>11.2</u>	<u>2.0</u>	<u>21.7%</u>	<u>29.2</u>	<u>30.6</u>	<u>1.4</u>	<u>4.8%</u>
Total net sales	110.2	127.5	17.3	15.7%	336.3	369.5	33.2	9.9%
Gross profit	44.3	52.5	8.2	18.5%	139.6	154.5	14.9	10.7%
Selling, general and administrative expenses	26.2	28.3	2.1	8.0%	81.4	83.3	1.9	2.3%
Interest expense, net	8.6	6.1	(2.5)	-29.1%	25.1	20.6	(4.5)	-17.9%
Income tax provision (benefit)	2.0	7.0	5.0	250.0%	6.9	(8.1)	(15.0)	-217.4%
Net income	7.2	10.5	3.3	45.8%	25.5	57.5	32.0	125.5%
EBITDA	22.5	28.7	6.2	27.6%	71.5	83.9	12.4	17.3%

**Net Sales.** Net sales during the three and nine months ended September 30, 2005 continued to increase compared to last year primarily due to the continued overall improvement of the U.S. economy, the growth of our facilities management business, the expansion of our revenue base through the opening of new branches and acquisitions, and by increasing our market share in certain markets. Prices during this period remained relatively stable, indicating that our revenue increases were primarily volume driven.

**Gross Profit.** Our gross profit increased by \$8.2 million and \$14.9 million during the three and nine months ended September 30, 2005, respectively, compared to the same periods in the prior year, primarily due to the increase in our net sales. Our production overhead as a percentage of net sales during the third quarter of 2005 continued to decrease due to the fixed cost nature of this expense coupled with the increase in our net sales. As a result, our overall gross margin during the three months ended September 30, 2005 increased to 41.2% compared to 40.2% during the same period last year.

**Selling, General and Administrative Expenses.** Selling, general and administrative expenses (SG&A) increased by \$2.1 million or 8.0% during the three months ended September 30, 2005 from a year earlier due to an increase in our selling and marketing costs due to higher sales commissions related to increased sales, higher legal and accounting fees as a result of the reporting and compliance requirements we became subject to since our initial public offering in February 2005, and higher incentive bonus accruals related to improved operating results compared to last year. As a percentage of net sales during the three months ended September 30, 2005, SG&A decreased from 23.8% in 2004 to 22.2% in 2005 due to our successful cost cutting efforts and gains in operating efficiency, combined with higher net sales.

**Interest Expense.** Net interest expense during the three months ended September 30, 2005 decreased by \$2.5 million compared to 2004 because we have made approximately \$119.3 million of net principal paydowns on our debt obligations since September 30, 2004. Of this amount, approximately \$89 million came from proceeds from our IPO in February 2005, and the remainder of our debt paydowns came from our internally generated cash flow. Our net interest expense during the nine months ended September 30, 2005 reflects a \$1.5 million write-off of deferred financing costs in February 2005 resulting from the principal prepayment on our senior credit facilities with

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the proceeds from our IPO. Excluding this \$1.5 million write-off, our net interest expense during the nine months ended September 30, 2005 decreased by \$6 million from the same period in 2004. The decline in our net interest expense resulting from the reduction of our total debt obligations has been partially offset by rising interest rates. The weighted average interest rate on our variable rate debt has increased to 9.0% as of September 30, 2005 compared to 7.4% as of September 30, 2004.

**Income Taxes.** Our income tax provision during the third quarter increased from \$2.0 million in 2004 to \$7.0 million in 2005 because of our reorganization from a California limited liability company (LLC) to a Delaware corporation in February 2005 in conjunction with our IPO. Prior to our reorganization, a substantial portion of our company's business was operated in an LLC, taxed as a partnership. As a result, the members of the LLC pay the income taxes on the earnings, not the LLC. Accordingly, no income taxes were provided on these earnings. During the third quarter of 2004, the LLC had book income of \$16.9 million which was not subject to tax at the LLC level. Including the proforma incremental income tax provision that would have applied had we been a Delaware corporation since the beginning of last year, our income tax provision increased from \$4.1 million during the third quarter of 2004 to \$7.4 million for the same period in 2005 due to an increase in our taxable income. Our proforma effective income tax rate during the third quarter decreased from 45.2% in 2004 to 40.0% in 2005 primarily due to the nondeductible interest expense on our preferred equity which was redeemed in February 2005.

We have a net income tax benefit of \$8.1 million during the nine months ended September 30, 2005 resulting from the one-time income tax benefit of \$27.7 million recorded in connection with our reorganization from an LLC to a Delaware corporation in February 2005. This non-recurring income tax benefit is related to the setting up of the deferred income tax accounts from the assets that were previously in the LLC, primarily comprised of tax-amortizable goodwill. This resulted in an increase in our deferred tax assets of \$27.7 million and a corresponding deferred income tax benefit for the same amount. Excluding this non-recurring deferred income tax benefit, our income tax provision during the nine months ended September 2005 amounted to \$19.6 million compared to \$6.9 million in 2004, or an increase of \$12.7 million over the same period in 2004. This is primarily due to (i) our reorganization from an LLC to a Delaware corporation in February 2005, and (ii) an increase in our pretax income during the nine months ended September 2005. During the nine months ended September 30, 2004, the LLC had book income of \$16.9 million which was not subject to tax at the LLC level compared to \$0.4 million during the same period in 2005.

Our overall proforma effective income tax rate during the three and nine months ended September 30, 2005 decreased to 40.0% and 40.4%, respectively, compared to 45.2% for the same periods in 2004 primarily due to the nondeductible interest expense on our preferred equity which was redeemed in February 2005.

**Net Income.** Net income increased by \$3.3 million or 45.8% in the third quarter of 2005 compared to the same period in 2004 primarily due to higher revenues and lower interest expense. Net income during the nine months ended September 2005 increased by \$32.0 million primarily due to the \$27.7 million non-recurring income tax benefit recognized during 2005 due to our reorganization in February 2005. This was offset by the increase in our income tax provision due to our company's reorganization from an LLC to a Delaware corporation and the \$1.5 million write-off of deferred financing costs during the first quarter of 2005.

**EBITDA.** Our EBITDA margin during the three and nine months ended September 30, 2005 increased to 22.5% and 22.7%, respectively, compared to 20.4% and 21.3% for the comparable periods in 2004, respectively, primarily due to higher revenues. For a reconciliation of EBITDA to net income, please see "- Non-GAAP Measures" above.

### Liquidity and Capital Resources

Our principal sources of cash have been cash provided by our operations and borrowings under our bank credit facilities or debt agreements. Our historical uses of cash have been for payment of principal and interest on outstanding debt obligations, acquisitions of reprographics businesses, capital expenditures, and, prior to the Reorganization in February 2005, tax-related distributions to Holdings' members. Supplemental information pertaining to our historical sources and uses of cash is presented as follows and should be read in conjunction with our consolidated statements of cash flows and notes thereto included in this report.

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	Nine Months Ended September 30,	
	2004	2005
	(Unaudited)	
	(Dollars in thousands)	
Net cash provided by operating activities	\$ 42,419	\$ 42,587
Net cash used in investing activities	\$ (7,611)	\$ (19,710)
Net cash used in financing activities	\$ (40,115)	\$ (23,875)

Net cash provided by operating activities of \$42.6 million for the nine months ended September 30, 2005 was primarily comprised of net income, net of non-cash related expenses which include a \$1.5 million non-recurring write-off of our deferred financing costs in connection with the early retirement of debt from our IPO proceeds during February 2005. This was offset by the non-cash related benefit from net deferred income taxes of \$25.0 million during the nine months ended September 2005. The primary working capital uses of cash during the nine months ended September 2005 were the increase in our accounts receivables of \$7.1 million primarily related to our increased sales and the \$3.5 million decrease in our accounts payable and accrued expenses mainly due to the timing of interest payments, as well as payments on trade payables and other accrued expenses.

Net cash used in investing activities of \$19.7 million for the nine months ended September 30, 2005 primarily relates to acquisition of businesses and capital expenditures. Our cash used in investing activities increased during the first nine months of 2005 because of higher cash outlays for business acquisitions, which was offset by lower cash outlays for capital expenditures due to our increased use of capital leases in 2005 to finance our procurement of production equipment.

Net cash used in financing activities of \$23.9 million for the nine months ended September 30, 2005 primarily relates to payments on long-term debt under our debt agreements and cash distributions to members. These are offset by the proceeds from borrowings under our debt agreements, as well as proceeds from the issuance of our common stock. We utilized the net proceeds from our IPO in February 2005 to redeem Holdings' preferred equity and to pay down our senior secured credit facilities. In connection with our IPO, we also made a cash distribution of \$8.2 million to certain members of Holdings which we funded through borrowings on our revolving credit facility during the first quarter of 2005. Because of strong cash flow generated from our operations, we did not utilize our revolving credit facility during the third quarter of 2005 and we currently have no outstanding borrowings on our revolving credit facility.

Our cash position, working capital and debt obligations as of December 31, 2004 and September 30, 2005 are shown below and should be read in conjunction with our consolidated balance sheets and notes thereto included in this report.

	December 31, 2004	September 30, 2005
	(Unaudited)	
	(Dollars in thousands)	
Cash and cash equivalents	\$ 13,826	\$ 12,828
Working capital	22,773	31,119
Debt obligations:		
Borrowings from senior secured credit facilities	301,312	229,426
Mandatorily redeemable preferred membership units	27,814	—
Other debt obligations	19,521	28,875
Total debt obligations	\$ 348,647	\$ 258,301

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We expect a positive impact on our liquidity and results of operations going forward due to lower interest expense resulting from the approximately \$119.3 million of net principal paydowns we have made on our total debt obligations since September 30, 2004. As discussed in Note 4 – “Long-Term Debt” to our consolidated financial statements set forth in Item 1 of this report, we entered into an amendment to our senior secured credit facilities in July 2005 which, among other amendments, reduced the interest rate applicable to borrowings on our First Priority Term Loan Credit Facility by 125 basis points.

The factors discussed above which are expected to reduce our interest expense will be offset to a certain extent by rising market interest rates on our debt obligations under our senior secured credit facilities which are subject to variable interest rates. As discussed in “Quantitative and Qualitative Disclosure About Market Risk,” we had \$258.3 million of total debt obligations outstanding as of September 30, 2005 of which \$229.4 million was bearing interest at variable rates approximating 9.0% on a weighted average basis as of September 30, 2005. A 1.0% change in interest rates on our variable rate debt would have resulted in interest expense fluctuating by approximately \$0.6 million and \$1.9 million during the three and nine months ended September 30, 2005, respectively.

We believe that our cash flow provided by operations will be adequate to cover our 2005 working capital needs, debt service requirements and planned capital expenditures to the extent such items are known or are reasonably determinable based on current business and market conditions. However, we may elect to finance certain of our capital expenditure requirements through borrowings under our credit facilities or the issuance of additional debt through capital lease agreements.

We continually evaluate potential acquisitions. We expect to fund future acquisitions through cash flow provided by operations, additional borrowings or the issuance of our equity. The extent to which we will be willing or able to use our equity or a mix of equity and cash payments to make acquisitions will depend on the market value of our shares from time to time and the willingness of potential sellers to accept equity as full or partial payment.

### **Off-Balance Sheet Arrangements**

As of December 31, 2004 and September 30, 2005, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

**Contractual Obligations and Other Commitments**

Our future contractual obligations as of September 30, 2005 by fiscal year are as follows:

	Three Months Ending December 31, 2005	2006	Twelve Months Ending December 31, (Unaudited)			Thereafter
			2007	2008	2009	
			(Dollars in thousands)			
Debt obligations	\$ 1,191	\$ 3,167	\$ 2,223	\$ 39,446	\$ 192,603	\$ 1,074
Capital lease obligations	2,032	6,720	5,124	2,913	1,143	662
Operating lease obligations	9,008	25,732	17,951	11,415	7,601	16,674
Total	<u>\$ 12,231</u>	<u>\$ 35,619</u>	<u>\$ 25,298</u>	<u>\$ 53,774</u>	<u>\$ 201,347</u>	<u>\$ 18,410</u>

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

Our primary exposure to market risk is interest rate risk associated with our debt instruments. We use both fixed and variable rate debt as sources of financing. We had an interest rate hedge agreement which expired in September 2005 and two interest rate collar agreements, one of which expired in September 2005 and the other expires in December 2006. Except as set forth below, there have been no material changes in market risk from the information reported in Item 7A – “Quantitative and Qualitative Disclosures about Market Risk” in our 2004 Annual Report on Form 10-K.

At September 30, 2005, we had \$258.3 million of total debt obligations of which \$229.4 million was bearing interest at variable rates approximating 9.0% on a weighted average basis. A 1.0% change in interest rates on our variable rate debt would have resulted in interest expense fluctuating by approximately \$0.6 million and \$1.9 million during the three and nine months ended September 30, 2005, respectively.

We have not, and do not plan to, enter into any derivative financial instruments for trading or speculative purposes. As of September 30, 2005, we had no other significant material exposure to market risk, including foreign exchange risk and commodity risks.

**Item 4. Controls and Procedures**

**Disclosure Controls and Procedures**

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports under the Securities Exchange Act of 1934 is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosures.

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer we conducted an evaluation of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of September 30, 2005. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that as of September 30, 2005, these disclosure controls and procedures were effective.

**Changes in Internal Controls Over Financial Reporting**

There were no changes to internal controls over financial reporting during the third quarter ended September 30, 2005 that has materially affected, or is reasonably likely to materially affect, our internal controls over financial reporting.

**PART II**

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

Our senior secured credit facilities contain restrictive covenants which, among other things, provide limitations on capital expenditures, restrictions on indebtedness and dividend distributions to our stockholders. Additionally, we are required to meet debt covenants based on certain financial ratio thresholds, including minimum interest coverage, maximum leverage and minimum fixed charge coverage ratios. The credit facilities also limit our ability and the ability of our domestic subsidiaries to, among other things, incur liens, make certain investments, sell certain assets, engage in reorganizations or mergers, or change the character of our business. We are in compliance with all such covenants as of September 30, 2005.

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### Item 6. Exhibits

#### INDEX TO EXHIBITS

<u>Number</u>	<u>Description</u>
10.1	Amendment to Lease for the premises commonly known as 17721 Mitchell North, Irvine, CA, effective as of August 2, 2005, by and between SUMO HOLDINGS IRVINE, LLC, Lessor and AMERICAN REPROGRAPHICS COMPANY, L.L.C., Lessee. *
10.2	Amendment to Lease for the premises commonly known as 934 and 940 Venice Boulevard, Los Angeles, CA, effective as of August 2, 2005, by and between SUMO HOLDINGS LA, LLC, Landlord and AMERICAN REPROGRAPHICS COMPANY, L.L.C. (formerly known as FORD GRAPHICS GROUP, L.L.C.) Tenant.*
10.3	Amendment to Lease for the premises commonly known as 18810 Woodfield Road, Gaithersburg, MD, effective as of August 2, 2005, by and between SUMO HOLDINGS MARYLAND, LLC, Landlord and LEET-MELBROOK, INC., Tenant. *
10.4	Amendment to Lease for the premises commonly known as 1322 V Street, Sacramento, CA, effective as of August 2, 2005, by and between SUMO HOLDINGS SACRAMENTO, LLC, Landlord and AMERICAN REPROGRAPHICS COMPANY, L.L.C. (formerly known as FORD GRAPHICS GROUP, L.L.C.) Tenant. *
31.1	Certification by the Chief Executive Officer pursuant to Rules 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934. *
31.2	Certification by the Chief Financial Officer pursuant to Rules 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934. *
32.1	Certification by the Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. *

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\* Filed herewith

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**SIGNATURE PAGE**

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 on November 14, 2005.

AMERICAN REPROGRAPHICS COMPANY

By: /s/ Sathiyamurthy Chandramohan  
Chairman of the Board of Directors and  
Chief Executive Officer

By: /s/ Mark W. Legg  
Chief Financial Officer and Secretary



**AMENDMENT TO**  
**LEASE**

This Amendment (this "Amendment") to Lease is entered into effective as of the 2nd day of August, 2005 by and between SUMO HOLDINGS IRVINE, LLC, a California limited liability company (hereinafter referred to as "Lessor") and AMERICAN REPROGRAPHICS COMPANY, L.L.C., a California limited liability company (hereinafter referred to as "Lessee").

**RECITALS**

A. In 1999, Lessor and Lessee entered into a Lease Agreement ("Lease") for the premises commonly known as 17721 Mitchell North, Irvine, California (the "Premises"). A copy of the Lease is attached hereto as Exhibit A.

B. The parties now desire to amend the Lease on the terms and conditions set forth in this Amendment.

**AGREEMENT**

NOW, THEREFORE, for good and valuable consideration, the receipt of which is hereby acknowledged, the parties hereby amend the Lease upon the terms and subject to the conditions set forth in this Amendment:

1. Capitalized Terms. Capitalized terms not defined in this Amendment shall have the meanings set forth in the Lease.
2. Paragraph 51 of the Lease is hereby amended to read in full as follows:

“(A) Provided the Lessee is not then in Default, Lessee shall have the right, exercisable not less than six (6) months prior to the date the option period would commence, to extend this Lease for three (3) additional periods of five (5) years each (each such five (5) year period shall be referred to as an “Option Period”), upon the same terms and conditions as set forth in this Lease, other than the amount of Base Rent which shall be determined as provided in Paragraph 51(B), below. Options (if there are more than one) may only be exercised consecutively. This Option is personal to the original Lessee, and cannot be assigned or exercised by anyone other than said original Lessee and only while the original Lessee is in full possession of the Premises and without the intention of thereafter assigning or subletting.

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(B) The Base Rent payable by Lessee during the Option Periods shall equal the fair market rental rate for the Premises as of the first day of each such five (5) year Option Period; however, in no event shall such Base Rent be less than the Base Rent payable for the month immediately preceding the Rent adjustment. At least ninety (90) days prior to the date that the term of each five (5) year Option Period shall commence, Lessor will notify Lessee in writing of its determination of the fair market rental rate for the Premises. If Lessee does not provide Lessor with written objection of Lessor's value within ten (10) days of Lessor's notification, Lessee shall be deemed to have accepted Lessor's value. If Lessee notifies Lessor in writing that Lessee does not accept Lessor's value, then each party hereto shall within twenty (20) days of Lessor's notification appoint one representative who shall be an MAI real estate appraiser experienced in the appraisal of commercial space in Irvine, California to act as appraiser. The two appraisers so appointed shall determine the fair market rental rate for the Premises in writing within thirty (30) days of Lessor's notification.

In the event the two appraisers cannot agree on the fair market rental rate for the Premises, they shall appoint a third appraiser who shall be similarly qualified. In the event the first two appraisers cannot agree on a third appraiser, either Lessor or Lessee may apply to the presiding judge of the Superior Court in Orange County, California for the appointment of such third appraiser. The third appraiser shall independently determine the fair market rental rate for the Premises and shall within ten (10) days of his or her appointment select the fair market rental rate of one of the first two appraisers which most closely approximates his own. The third appraiser shall have no right to adopt a compromise or middle ground or any modification of either fair market rental rate proposed by the first two appraisers. The fair market rental rate chosen by the third appraiser as most closely approximating his or her determination shall constitute the final fair market rental rate, or "Base Rent", for the Premises.

Each party shall pay the charges of the appraiser appointed by it and any expenses incurred by such appraiser. The charges and expenses of the third appraiser shall be paid by the parties hereto in equal shares. In the event Lessor or Lessee fails to appoint an appraiser within the time specified or such appraiser fails to present a fair market rental rate for the Premises within the time specified, the determination of the other party's appraiser shall be final. In the event the third or any subsequent appraiser fails to choose a fair market rental rate for the Premises of one of the first two appraisers within the time specified, then the first two





**AMENDMENT TO**  
**LEASE**

This Amendment (this "Amendment") to Lease is entered into effective as of the 2nd day of August, 2005 by and between SUMO HOLDINGS LA, LLC, a California limited liability company (hereinafter referred to as "Landlord") and AMERICAN REPROGRAPHICS COMPANY, L.L.C., a California limited liability company (formerly known as FORD GRAPHICS GROUP, L.L.C.) (hereinafter referred to as "Tenant").

**RECITALS**

A. On November 19, 1997, Landlord and Tenant entered into a Lease Agreement ("Lease") for the premises commonly known as 934 and 940 Venice Boulevard, Los Angeles, California (the "Premises"). A copy of the Lease is attached hereto as Exhibit A.

B. The parties now desire to amend the Lease on the terms and conditions set forth in this Amendment.

**AGREEMENT**

NOW, THEREFORE, for good and valuable consideration, the receipt of which is hereby acknowledged, the parties hereby amend the Lease upon the terms and subject to the conditions set forth in this Amendment:

1. Capitalized Terms. Capitalized terms not defined in this Amendment shall have the meanings set forth in the Lease.
2. Section 1.02 of the Lease is hereby amended to read in full as follows:

**“ 1.02 Option To Extend Term:**

Tenant shall have an option to extend the term of this Lease for three (3) additional periods of five (5) years each commencing on expiration of the original term specified in Section 1.01 of this Lease provided:

(a) Tenant has fully and faithfully performed all the terms, covenants, and conditions of this Lease for the original term specified in Section 1.01 herein.

(b) Written notice of Tenant's election to renew the term of this Lease is delivered by Tenant to Landlord at least

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six (6) months prior to the expiration of the Lease's original term or, if applicable, upon expiration of the renewed term then in effect.

(c) The renewed term of this Lease shall be subject to the same terms and conditions as are contained in this Lease, except that the amount of rent payable under this Lease for the renewed term shall be adjusted based on the then fair market value of the Premises, determined in accordance with Section 2.01(b) of this Lease.”

3. Section 2.01(b) of the Lease is hereby amended to read in full as follows:

**“2.01 Fixed Rent :**

(b) Should Tenant elect to extend the term of this Lease, the annual rent to be paid by Tenant under this Lease during the extended term described in Section 1.02 shall equal one hundred percent (100%) of the property's fair market rental value three (3) months prior to the expiration of the Lease, or the adjusted monthly rental amount payable for the month immediately preceding the rent adjustment, whichever is greater. Should Tenant dispute Landlord's determination of the property's fair market rental value, the parties agree that the fair market rental value shall be determined by arbitration held in accordance with the rules of the American Arbitration Association in effect at that time. The written decision of the arbitrators shall be binding on Tenant and Landlord. The costs of such arbitration shall be borne equally by Tenant and Landlord. Such arbitration hearing shall be held in Los Angeles, California.

The annual rent for each renewed term shall be payable in equal monthly installments and otherwise paid in the same manner as rent is required under Section 2.01 to be paid during the original term of the Lease. Landlord shall give Tenant written notice at least six (6) months prior to expiration of the then term of any expected rent increase determined under this section.”

4. Counterparts. This Amendment may be executed in counterparts, each of which shall be deemed an original and all of which shall constitute one instrument.

5. Other Terms and Conditions. All other terms and conditions of the Lease will continue in full force and effect except as expressly modified in this Amendment. The terms and conditions of the Lease are incorporated by reference and the terms and conditions of this Amendment are incorporated into the Lease.

IN WITNESS WHEREOF, the parties have executed this Amendment effective as of August 2, 2005.

SUMO HOLDINGS LA, LLC, a California  
limited liability company

By: /s/ Sathiyamurthy Chandramohan  
SATHIYAMURTHY CHANDRAMOHAN  
Its: Manager

“LANDLORD”

AMERICAN REPROGRAPHICS COMPANY, L.L.C.,  
a California limited liability company (formerly  
known as FORD GRAPHICS GROUP, L.L.C.)

By: /s/ Mark W. Legg  
MARK W. LEGG  
Its: CHIEF FINANCIAL OFFICER

“TENANT”



**AMENDMENT TO  
LEASE**

This Amendment (this "Amendment") to Lease is entered into effective as of the 2nd day of August, 2005 by and between SUMO HOLDINGS MARYLAND, LLC, a California limited liability company (hereinafter referred to as "Landlord") and LEET-MELBROOK, INC. (hereinafter referred to as "Tenant").

**RECITALS**

A. On December 7, 1995, Richard L. Dietrick and Garnetta J. Dietrick (collectively referred to as "the Dietricks") and Tenant entered into a Lease Agreement ("Lease") for the premises commonly known as 18810 Woodfield Road, Gaithersburg, Maryland (the "Demised Premises"). A copy of the Lease is attached hereto as Exhibit A.

B. On November 8, 2001 the Dietricks assigned all of their right, title and interest in and to the Lease to Landlord (the "Assignment"). A copy of the Assignment is attached hereto as Exhibit B.

C. The parties now desire to amend the Lease on the terms and conditions set forth in this Amendment.

**AGREEMENT**

NOW, THEREFORE, for good and valuable consideration, the receipt of which is hereby acknowledged, the parties hereby amend the Lease upon the terms and subject to the conditions set forth in this Amendment:

1. **Capitalized Terms** . Capitalized terms not defined in this Amendment shall have the meanings set forth in the Lease.
2. Section 2(b) of the Lease is hereby amended to read in full as follows:

“(b) Provided the Tenant is not then in Default, Tenant shall have the right, exercisable not less than six (6) months prior to the Termination Date, to extend this Lease for an additional period of five (5) years (“First Option Period”), upon the same terms and conditions as set forth herein for the initial term (other than this option to extend). Provided that Tenant is not then in Default, Tenant shall have the right, exercisable not less than six (6) months prior to the expiration of the extended term, to extend this Lease for two (2) additional periods of five (5) years each (each such five (5) year period shall be referred to as a “Subsequent Option Period”), upon the same terms and conditions as set forth in this Lease, other than the amount of rent which shall be determined as provided in Section 3(f) of this Lease.”

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3. Section 3(b) of the Lease is hereby amended to read in full as follows:

“(b) Commencing with the second lease year and for each subsequent lease year during the original term and during the First Option Period, basic annual rent shall be increased annually by an amount equal to two percent (2%) of the basic annual rent payable during the preceding lease year.”

4. Section 3 “Rent and Other Charges” is hereby amended by adding the following subparagraph (f):

“(f) The basic annual rent payable by Tenant during each of the Subsequent Option Periods shall equal the fair market rental rate for the Demised Premises as of the first day of each such five (5) year Subsequent Option Period; however, in no event shall such basic annual rent be less than the basic annual rent payable for the month immediately preceding the rent adjustment. At least ninety (90) days prior to the date of the commencement of the term of the applicable Subsequent Option Period, Landlord will notify Tenant in writing of its determination of the fair market rental rate for the Demised Premises. If Tenant does not provide Landlord with written objection of Landlord’s value within ten (10) days of Landlord’s notification, Tenant shall be deemed to have accepted Landlord’s value. If Tenant notifies Landlord in writing that Tenant does not accept Landlord’s value, then each party hereto shall within twenty (20) days of Landlord’s notification appoint one representative who shall be an MAI real estate appraiser experienced in the appraisal of commercial space in Gaithersburg, Maryland to act as appraiser. The two appraisers so appointed shall determine the fair market rental rate for the Demised Premises in writing within thirty (30) days of Landlord’s notification.

In the event the two appraisers cannot agree on the fair market rental rate for the Demised Premises, they shall appoint a third appraiser who shall be similarly qualified. In the event the first two appraisers cannot agree on a third appraiser, either Landlord or Tenant may apply to the presiding judge of the Circuit Court in the County of Montgomery for the appointment of such third appraiser. The third appraiser shall independently determine the fair market rental rate for the Demised Premises and shall within ten (10) days of his or her appointment select the fair market rental rate of one of the first two appraisers which most closely approximates his own. The third appraiser shall have no right to adopt a compromise or middle ground or any modification of either fair market rental rate proposed by the first two appraisers. The fair market rental rate chosen by the third appraiser as most closely approximating his or her determination shall constitute the final fair market rental rate for the Demised Premises.

Each party shall pay the charges of the appraiser appointed by it and any expenses incurred by such appraiser. The charges and expenses of the third appraiser shall be paid by the parties hereto in equal shares. In the event Landlord or Tenant fails to appoint an appraiser within the time specified or such appraiser fails to present a fair market rental rate for the Demised Premises within the time specified, the determination of the other party's appraiser shall be final. In the event the third or any subsequent appraiser fails to choose a fair market rental rate for the Demised Premises of one of the first two appraisers within the time specified, then the first two appraisers shall select a subsequent third appraiser and a new ten (10) day period shall begin.

The basic annual rent payable by Tenant for each Subsequent Option Period shall be determined in accordance with the procedures and provisions of this section 3(f)."

5. Counterparts. This Amendment may be executed in counterparts, each of which shall be deemed an original and all of which shall constitute one instrument.

6. Other Terms and Conditions. All other terms and conditions of the Lease will continue in full force and effect except as expressly modified in this Amendment. The terms and conditions of the Lease are incorporated by reference and the terms and conditions of this Amendment are incorporated into the Lease.

IN WITNESS WHEREOF, the parties have executed this Amendment effective as of August 2, 2005.

**LANDLORD:**

SUMO HOLDINGS MARYLAND, LLC, a  
California limited liability company

By: /s/ Sathiyamurthy Chandramohan

SATHIYAMURTHY CHANDRAMOHAN

Its: Manager

**TENANT**

LEET-MELBROOK, INC.

By: /s/ Mark W. Legg

MARK W. LEGG

Its: CFO



**AMENDMENT TO**  
**LEASE**

This Amendment (this "Amendment") to Lease is entered into effective as of the 2nd day of August, 2005 by and between SUMO HOLDINGS SACRAMENTO, LLC, a California limited liability company (hereinafter referred to as "Landlord") and AMERICAN REPROGRAPHICS COMPANY, L.L.C., a California limited liability company (formerly known as FORD GRAPHICS GROUP, L.L.C.) (hereinafter referred to as "Tenant").

**RECITALS**

A. On December 1, 1977, Landlord and Tenant entered into a Lease Agreement ("Lease") for the premises commonly known as 1322 V Street, Sacramento, California (the "Premises"). A copy of the Lease is attached hereto as Exhibit A.

B. The parties now desire to amend the Lease on the terms and conditions set forth in this Amendment.

**AGREEMENT**

NOW, THEREFORE, for good and valuable consideration, the receipt of which is hereby acknowledged, the parties hereby amend the Lease upon the terms and subject to the conditions set forth in this Amendment:

1. Capitalized Terms. Capitalized terms not defined in this Amendment shall have the meanings set forth in the Lease.
2. Section 1.02 of the Lease is hereby amended to read in full as follows:

**“ 1.02 Option To Extend Term:**

Tenant shall have an option to extend the term of this Lease for three (3) additional periods of five (5) years each commencing on expiration of the original term specified in Section 1.01 of this Lease provided:

- (a) Tenant has fully and faithfully performed all the terms, covenants, and conditions of this Lease for the original term specified in Section 1.01 herein.
  - (b) Written notice of Tenant's election to renew the term of this Lease is delivered by Tenant to Landlord at least
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six (6) months prior to the expiration of the Lease's original term or, if applicable, upon expiration of the renewed term then in effect.

(c) The renewed term of this Lease shall be subject to the same terms and conditions as are contained in this Lease, except that the amount of rent payable under this Lease for the renewed term shall be adjusted based on the then fair market value of the Premises, determined in accordance with Section 2.01(b) of this Lease.”

3. Section 2.01(b) of the Lease is hereby amended to read in full as follows:

**“2.01 Fixed Rent :**

(b) Should Tenant elect to extend the term of this Lease, the annual rent to be paid by Tenant under this Lease during the extended term described in Section 1.02 shall equal one hundred percent (100%) of the property's fair market rental value three (3) months prior to the expiration of the Lease, or the adjusted monthly rental amount payable for the month immediately preceding the rent adjustment, whichever is greater. Should Tenant dispute Landlord's determination of the property's fair market rental value, the parties agree that the fair market rental value shall be determined by arbitration held in accordance with the rules of the American Arbitration Association in effect at that time. The written decision of the arbitrators shall be binding on Tenant and Landlord. The costs of such arbitration shall be borne equally by Tenant and Landlord. Such arbitration hearing shall be held in Los Angeles, California.

The annual rent for each renewed term shall be payable in equal monthly installments and otherwise paid in the same manner as rent is required under Section 2.01 to be paid during the original term of the Lease. Landlord shall give Tenant written notice at least six (6) months prior to expiration of the then term of any expected rent increase determined under this section.”

4. Counterparts. This Amendment may be executed in counterparts, each of which shall be deemed an original and all of which shall constitute one instrument.

5. Other Terms and Conditions. All other terms and conditions of the Lease will continue in full force and effect except as expressly modified in this Amendment. The terms and conditions of the Lease are incorporated by reference and the terms and conditions of this Amendment are incorporated into the Lease.

IN WITNESS WHEREOF, the parties have executed this Amendment effective as of August 2, 2005.

SUMO HOLDINGS SACRAMENTO, LLC, a  
California limited liability company

By: /s/ Sathiyamurthy Chandramohan  
SATHIYAMURTHY CHANDRAMOHAN

Its: Manager

“LANDLORD”

AMERICAN REPROGRAPHICS COMPANY, L.L.C.,  
a California limited liability company (formerly  
known as FORD GRAPHICS GROUP, L.L.C.)

By: /s/ Mark W. Legg  
MARK W. LEGG

Its: CFO

“TENANT”



**CERTIFICATIONS**

**CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER  
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT**

I, Sathiyamurthy Chandramohan, certify that:

1. I have reviewed this report on Form 10-Q of American Reprographics Company;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) Designed such disclosure controls and procedures or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's third fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Date: November 14, 2005

/s/ Sathiyamurthy Chandramohan  
Chairman of the Board of Directors and  
Chief Executive Officer



**CERTIFICATIONS**

**CERTIFICATION OF THE CHIEF FINANCIAL OFFICER  
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT**

I, Mark W. Legg, certify that:

1. I have reviewed this report on Form 10-Q of American Reprographics Company;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:
  - a) Designed such disclosure controls and procedures or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's third fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Date: November 14, 2005

/s/ Mark W. Legg  
Chief Financial Officer and Secretary



**CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND  
CHIEF FINANCIAL OFFICER  
PURSUANT TO 18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of American Reprographics Company (the "Company") on Form 10-Q for the quarterly period ended September 30, 2005 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Sathiyamurthy Chandramohan, as Chief Executive Officer of the Company, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to the best of my knowledge, that (1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, and (2) the information contained in the Report fairly presents in all material respects, the financial condition and results of operations of the Company.

Date: November 14, 2005

/s/ Sathiyamurthy Chandramohan  
Chairman of the Board of Directors and  
Chief Executive Officer

In connection with the Quarterly Report of American Reprographics Company (the "Company") on Form 10-Q for the quarterly period ended September 30, 2005 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Mark W. Legg, as Chief Financial Officer of the Company, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to the best of my knowledge, that (1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, and (2) the information contained in the Report fairly presents in all material respects, the financial condition and results of operations of the Company.

Date: November 14, 2005

/s/ Mark W. Legg  
Chief Financial Officer and Secretary