

Edgar Filing: QEP CO INC - Form 10-K

QEP CO INC  
Form 10-K  
May 29, 2002

United States  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES  
EXCHANGE ACT OF 1934  
For the fiscal year ended February 28, 2002

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (D)  
OF THE SECURITIES EXCHANGE ACT OF 1934  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 0-21161

Q.E.P. CO., INC.  
(Exact name of registrant as specified in its charter)

DELAWARE  
(State or other jurisdiction of  
incorporation or organization)

13-2983807  
(I.R.S. Employer  
Identification No.)

1081 HOLLAND DRIVE, BOCA RATON, FLORIDA  
(Address of principal executive offices)

33487  
(Zip Code)

Registrant's telephone number, including area code: (561) 994-5550

Securities Registered Pursuant to Section 12(b) of the Act:

Title of each class  
NONE

Name of exchange  
on which registered  
NONE

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

Common Stock, \$0.001 par value  
(Title of Class)

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

The aggregate market value of voting common stock held by non-affiliates as of May 17, 2002 is \$6,736,000, computed by reference to the closing price for such shares on the NASDAQ National Market System as of such date. The registrant does not have any authorized or issued non-voting common equity securities.

## Edgar Filing: QEP CO INC - Form 10-K

The number of shares outstanding of each of the registrant's classes of common stock as of May 17, 2002 is: 3,381,190 shares of Common Stock, par value \$0.001 per share.

### DOCUMENTS INCORPORATED BY REFERENCE

Parts of the definitive Proxy Statement which the Registrant will file with the Securities and Exchange Commission in connection with the Registrant's Annual Meeting of Stockholders to be held on July 12, 2002 are incorporated by reference in Part III of this Form 10-K.

### PART I

#### Item 1. Business

##### General

Founded in 1979, Q.E.P. Co., Inc. (the "Company" or "Q.E.P.") manufactures, markets and distributes a broad line of specialty tools and flooring related products for the home improvement market in the United States and 49 countries throughout the world. Under brand names including Q.E.P.(TM), O'TOOL(TM) and ROBERTS(TM), the Company markets over 3,000 specialty tools and flooring related products used primarily for surface preparation and installation of ceramic tile, carpet and marble. Q.E.P.'s products include trowels, floats, tile cutters, wet saws, spacers, nippers, pliers, carpet trimmers and cutters, carpet adhesives, seaming tape, tack strip, knives, dryset powders, grouts and abrasives. These products are sold to home improvement retailers, including national and regional chains such as Home Depot and Lowe's, specialty distributors to the hardware, construction, flooring and home improvement trades and chain or independent hardware, tile, and carpet retailers for use by the do-it-yourself consumer as well as the construction or remodeling professional.

The Company experienced similar net sales, as adjusted in fiscal 2001 and fiscal 2000 for the Company's licensing of its domestic tack strip business described elsewhere herein, which management attributes to (i) growth experienced by the Company's customers within the home improvement market, particularly among national and regional home center retailers such as Home Depot and Lowe's, (ii) the Company's success in cross-marketing its products among its channels of distribution, (iii) the Company's expansion of its customer base and market share through sales to additional home improvement retailers and distributors and (iv) growth of the home improvement market as a whole.

The Company made several strategic acquisitions during the year ended February 29, 2000, as part of its plan to enhance its leadership in the worldwide flooring market. On June 17, 1999, the Company acquired Neon Australia Pty, Ltd., a leading Australian manufacturer of flooring tapes and metals for the carpet industry. On July 20, 1999, the Company acquired Novafonte, Limitada, a distributor, manufacturer and installer of ceramic tile and ceramic tile accessories located in Santiago, Chile. On July 22, 1999, the Company acquired an additional Australian flooring company, Accessories Marketing Pty, Ltd., the largest distributor of tools and installation products for all types of flooring in the Australian marketplace. On September 21, 1999, the Company acquired Boiardi Products Corp. of Little Falls, NJ. Boiardi is a manufacturer of a full line of thin-set mortars, grouts, self-leveling concrete toppings and crack-suppressing waterproof membranes used in the flooring industry. On September 30, 1999, the Company acquired Trade Mates Pty, Ltd. of Australia, a distributor of ceramic tile tools in the Australian marketplace. On December 6, 1999, the Company acquired Zocalis, SRL, an Argentinean company located in Buenos Aires. Zocalis is a manufacturer of ceramic borders and trim. Collectively, these acquisitions are referred to as the "Fiscal 2000 acquisitions" elsewhere herein.

## Edgar Filing: QEP CO INC - Form 10-K

The Company's acquisitions in fiscal 2001 were predominantly associated with expanding the Company's position as a manufacturer of dryset powder and grouts used in ceramic tile installations. To that end, the Company acquired Stone Mountain Manufacturing of Georgia and Stone Mountain Manufacturing of Florida from the same seller. The Company also acquired the Australian-based Southern Tile Agency PTY, a manufacturer of quality accessories used for the installation of ceramic tile and a New Zealand distributor.

Collectively, Southern Tile Agencies Ltd. Pty., Stone Mountain Manufacturing of Georgia and Florida and the Fiscal 2000 acquisitions are referred to elsewhere herein as the "newly acquired entities."

1

### Market Overview

The Company is a supplier of specialty flooring installation products and sells to the home improvement market. According to the latest industry information published by the Home Channel News ("HCN"), it is expected that the United States retail home improvement market will experience a growth rate in sales of 2.3% in 2002, which is down from 2001 increases of approximately 6% due to the slow recovery of the economy. However, it is expected that long-term growth will be an average of 6%. The Company believes that growth in the home improvement market is being driven by several factors, including (i) aging of the United States housing stock which requires greater repair and maintenance expenditures, (ii) increased housing turnover of both new and existing homes, (iii) favorable demographic trends as "baby boomers," are now reaching the age category historically accounting for the largest home improvement expenditures of any age group, and (iv) changes in consumer preferences, which have caused an increase in the median size of new homes and which have contributed to demand for remodeling and expansion of older homes. Further, according to HCN, home improvement expenditures will increase next year as consumers strive to increase the value and appearance of their home.

Within the home improvement market, distribution channels have continued to consolidate as a result of the success of the warehouse home center format used by large home improvement retailers. The increasing dominance of national home improvement retailers results from their ability to offer broad product lines, project advice and orientation, competitive pricing, aggressive promotions and large-format stores. The Companies two largest customers accounted for over \$75.5 billion of home center sales in fiscal 2002. Based on data available to the Company, the primary beneficiaries of this consolidation among home improvement retailers have been the top two or three companies (ranked by annual sales volume). Thus, while the home improvement market's retail sales have expanded, the market is being increasingly dominated by the largest retailers.

The Company's two largest customers, Home Depot and Lowe's, experienced 5-year compound annual sales growth rates of 22.3% and 18.8%, respectively, from 2000 to 2001, according to their published financial reports and both have announced plans to continue increasing the number of stores each operates. As consolidation continues among home improvement retailers, the Company expects that sales of the largest national and regional home improvement retailers will continue to increase at greater rates than the rate of sales growth in the overall market. The Company expects that the growth trends in the specialty flooring segment of the home improvement market and among its customer base will directly affect the Company's ability to generate growth in its sales and net income, its expansion strategy and the nature of its sales and marketing initiatives.

### Business Strategy

## Edgar Filing: QEP CO INC - Form 10-K

The Company's strategy is to enhance its position as a leading manufacturer and distributor of specialty tools and related products by introducing new products and cross-selling products among its channels of distribution, expanding market share by obtaining new customers, and capitalizing on expected growth of its largest customers and of the home improvement market as a whole. Key elements of the Company's strategy include:

**Pursue Additional Strategic Acquisitions.** Through its acquisitions, detailed elsewhere herein, the Company has broadened its product lines, increased its customer base and increased its manufacturing and marketing capabilities. The Company intends to seek and evaluate acquisitions of both domestic and worldwide specialty tool and adhesive manufacturers, distributors and other companies whose products, distribution channels and brand names are complimentary to those of the Company and which will offer further opportunities for product cross selling, expansion of manufacturing and marketing operations and the addition of new customers.

2

**Increase Sales By Expanding Product Lines and Adding New Customers.** The Company seeks to expand its product lines by introducing new and innovative products, which can be marketed to the Company's existing customer base. Through its acquisitions, the Company has expanded its customer base, the number of products available and its line of flooring installation products. In addition to expanding product offerings through acquisitions, the Company intends to internally develop and offer products in response to customer demands. The Company believes that broadening its product lines will make it a more attractive supplier to the major home improvement retailers and specialty distributors, thereby increasing the Company's sales and market penetration.

**Capitalize on Cross-Selling Opportunities.** The Company believes that there are significant opportunities for "cross selling" its products among its existing markets and channels of distribution. As part of its acquisition strategy, the Company seeks to identify acquisition candidates with complementary product lines and to "cross sell" acquired product lines to its existing customer base and its existing product lines to the customers of the acquired business.

**Enhance Distribution and Manufacturing Capabilities.** The Company currently has approximately 652,000 square feet of distribution and manufacturing capability located throughout the United States, Canada, Holland, Australia and South America. The Company estimates that in fiscal 2002, it manufactured approximately 40% of its Q.E.P. and Roberts product lines.

### Products

The Company manufactures, markets and distributes a broad line of over 3,000 specialty tools and flooring related products. The Company's products are offered under brand names including Q.E.P.(TM), O'TOOL(TM) and ROBERTS(TM) and are used primarily for surface preparation and installation of ceramic tile, carpet and marble.

The Company manufactures and distributes adhesives, grouts, mortars, dry set powders, carpet seaming tape and an assortment of carpet installation tools as well as floats, tile cutters, trowels, electric saws, nippers and other products to the ceramic tile industry. These products are sold to both distributors and do it yourself customers. Although the Company manufactures and distributes over 3,000 products, a majority of the Company's sales are to customers who purchase between 20 and 200 individual stock-keeping units. As the Company seeks to broaden its product lines, the competition for limited shelf space available at home improvement retailers for specialty tools and related products may limit sales of existing or newly introduced products.

## Edgar Filing: QEP CO INC - Form 10-K

The Company maintains a research and development program through which it seeks to identify new product opportunities within its primary markets. Methods by which the Company seeks to identify product opportunities include soliciting product feedback from customers through its outside sales force and manufacturers' representatives, review of product brochures and catalogs issued by foreign and domestic manufacturers of specialty tools, review of product concepts with buyers employed by its customers, and attendance at industry trade shows and conventions at which new product concepts are introduced and discussed. The Company also considers participation in joint ventures and evaluation of product samples to be an important part of its effort to identify new product opportunities. The Company maintains a product quality control program primarily to verify the quality of its existing products and to develop ideas for additional products or enhancements to existing products.

### Relationship With Major Customers

In 1982, the Company began selling products to Home Depot, which is currently the largest home improvement retailer in the world and the second largest retailer in the United States of America based on annual sales volume. In 1993, the Company added Lowe's as a customer, which is now the second largest home improvement retailer in the world and fourteenth largest retailer in the United States of America. Home Depot and Lowe's are the Company's two largest customers accounting for 46.4% and 12.9% of the Company's fiscal 2002 net sales, respectively.

3

Because of the importance of home improvement retailers to its business, the Company has, in consultation with these major customers, developed customer service programs to ensure that the specific needs of these customers are given a high priority with direct attention from senior officers of the Company. Features of the Company's customer service programs for its major customers include providing a range of in-store services, such as, assistance with inventory, maintenance of product displays, introduction of new products, maintaining inventories of tools and related products in multiple locations to permit rapid shipping, delivering orders promptly, holding education classes for retail store personnel, packaging with multilingual labels, prepaying delivery for product shipments with minimum purchase requirements, participating in cooperative promotions and special sales events, providing product research for buyers, operating a customer service hotline, providing parts and repair service, extension of advertising allowances, accepting orders electronically and billing through electronic data interchange, bar coding for each individual stock keeping unit, and incorporating anti-theft tags in packaging. The Company believes that its major customers place considerable value on service and promotional support and frequently evaluates its service and promotional activities in an effort to serve its customers more effectively.

The Company believes that the consolidation among home improvement retailers will continue and that the national and large regional home improvement retailers will continue to increase their market share in the near future. Home Depot and Lowe's have announced plans to increase significantly the number of stores each operates over the next several years. As a result, the Company expects the percentage of its sales to these customers to continue to be significant. Additionally, the Company continues to expand its customer base in other areas through its newly acquired entities.

The loss of Home Depot or Lowe's as a customer of the Company could have a material adverse effect on the financial position of the Company.

### Manufacturing and Suppliers

## Edgar Filing: QEP CO INC - Form 10-K

The Company estimates that in fiscal 2002 it manufactured approximately 40% of its Q.E.P. and Roberts product lines. The Company manufactures adhesives, carpet seaming tape and carpet installation tools at its main manufacturing facility in Mexico, Missouri. Flooring adhesives are produced at the facility in Bramalea, Ontario, Canada and Sliedrecht, Holland. Plastic tile spacers are manufactured at the facility in Boca Raton, Florida. Grouts and related products are manufactured at the Company's New Jersey, Georgia and Ft. Pierce, Florida facilities. In Australia, the Company manufactures accessories used for the installation of ceramic tile. Such tile accessories are also manufactured in Chile. Ceramic trim is manufactured in Argentina.

The Company purchased finished products and components from approximately 250 different suppliers in fiscal 2002. Although the Company believes that multiple sources of supply exist for nearly all of the products and components purchased from outside suppliers and generally maintains at least two sources of supply for each item purchased, interruptions in supply or price changes in the items purchased by the Company could have a material adverse effect on the Company's operations. Further, in fiscal 2002, the Company purchased in excess of \$12 million of finished product from one supplier.

### Distribution, Sales and Marketing

The Company's specialty tools and related products are currently sold through four distinct distribution channels: (i) the Company's sales staff; (ii) independent manufacturing representatives; (iii) an in-house telemarketing sales force; and (iv) outside salaried and commissioned sales representatives. Management estimates that sales through its primary distribution channels in fiscal 2002 were as follows: 60.4% to national and regional home improvement retailers and 39.6% to specialty distributors, other specialty retailers and OEMs.

4

The Company maintains an in-house creative art department through which it produces and develops color product catalogs, signage, point of purchase materials and distinctive packaging to enhance sales per square foot at the retail level and to reinforce the Company's brand images. The Company has developed a direct mail marketing program under which approximately 3,500 product advertising flyers are mailed to customers, usually on a bimonthly basis.

The Company's marketing and sales representatives, or its manufacturers' representatives, conduct regular visits to many customers' individual retail stores. In addition, the Company or its sales representatives provides product knowledge classes for retail store personnel. The Company also evaluates the product mix at its customers' locations from time to time with a view toward changing the product mix, if necessary, to increase sales per square foot. When the Company secures a new customer, the Company generally resets all displays and assists store personnel in becoming familiar with the Company's product line.

### Competition

The Company believes that competition in the home improvement flooring product market is based primarily on product quality, delivery capabilities, brand name recognition, availability of retail shelf space and price. The Company believes that its competitive strengths are the quality of its products, its wide range of products, its delivery capabilities, and the brand recognition. The Company faces competition largely on a product-by-product basis from numerous manufacturing and distribution companies. The Company believes that the

## Edgar Filing: QEP CO INC - Form 10-K

diversity of its product portfolio will allow it to compete effectively with its competitors, although some of such competitors may sell larger quantities of a particular product than the Company.

The Company is aware of a number of competitors, many of which are foreign and may have greater financial, marketing and other resources than the Company. The Company's foreign sales, including Canada, accounted for approximately 22.6% of total sales during fiscal year 2002. Fiscal 2002 sales generated by the Company's Canadian subsidiary were 8.8%, its Holland subsidiary 7.2%, its Australian subsidiaries 3.4%, its South American subsidiaries 1.1% and 2.1% to foreign customers from its domestic subsidiaries. The Company is continuing to penetrate more foreign markets and, as a result, the Company may experience competition from foreign companies, which could adversely affect the Company's gross margins on its foreign sales.

Certain of the Company's larger customers have in the past contacted one or more of the Company's foreign suppliers to discuss purchasing home improvement products directly from these suppliers. Although the Company believes that its diversified product line, brand recognition and customer service will continue to offer benefits not otherwise available to the Company's customers from foreign manufacturers, the Company could experience competition from one or more foreign manufacturers which now serve as suppliers to the Company. If one or more of the Company's larger customers were to begin purchasing products previously supplied by the Company directly from foreign manufacturers, the Company's business would be adversely affected. Increased competition from these manufacturers or others could result in lower sales, price reductions and loss of market share, each of which would have an adverse effect on the Company's results of operations.

### Environmental Matters

The Company is subject to federal, state and local laws, regulations and ordinances governing activities or operations that may have adverse environmental effects, such as discharges to air and water, handling and disposal practices for solid, special and hazardous wastes, and imposing liability for the cost of cleaning up, and certain damages resulting from sites of past spills, disposal or other releases of hazardous substances (together, "Environmental Laws"). Sanctions which may be imposed for violation of Environmental Laws include the payment or reimbursement of investigative and clean up costs, administrative penalties and, in certain cases, prosecution under environmental criminal statutes. The Company's manufacturing facilities are subject to environmental regulation by, among other agencies, the

5

Environmental Protection Agency, the Occupational Safety and Health Administration, and various state authorities in the states where such facilities are located. The activities of the Company, including its manufacturing operations at its leased facilities, are subject to the requirements of Environmental Laws. The Company believes that the cost of compliance with Environmental Laws to date has not been material to the Company. The Company is not currently aware of any situations requiring remedial or other action which would involve a material expense to the Company, or expose the Company to material liability under Environmental Laws. As the operations of the Company involve the storage, handling, discharge and disposal of substances which are subject to regulation under Environmental Laws, there can be no assurance that the Company will not incur any material liability under Environmental Laws in the future or will not be required to expend funds in order to effect compliance with applicable Environmental Laws.

The Company completed testing at its facility in Bramalea, Ontario, Canada for

## Edgar Filing: QEP CO INC - Form 10-K

leakage of hazardous materials and, as a result, in fiscal 1999 the Company prepared a plan to remediate the contamination over a period of years and this plan was subsequently approved by the Canadian Ministry of Environment (MOE). The Company recorded a reserve for potential environmental liability on the closing date of the Roberts acquisition of approximately \$325,000 and this amount was increased during fiscal 1999 by \$275,000 to \$600,000 based on an estimate for the cost of remediation. To date, the Company has spent approximately \$480,000 and anticipates spending additional amounts on ongoing monitoring of wells and other environmental activity at the approximate rate of between \$5,000 and \$25,000 per year for the next few years.

Roberts Consolidated Industries, Inc. has been named as a defendant in an amended complaint filed in *CARGILL, INC. ET AL. V. ABCO CONSTRUCTION ET AL.*, a lawsuit initially filed in the United States District Court for the Southern District of Ohio Western Division on January 29, 1998. The lawsuit, brought under CERCLA and related state environmental laws, alleges that an entity known as "Roberts Consolidated" and the other defendants disposed of hazardous substances at a site located in Dayton, Ohio. The plaintiffs are seeking monetary damages against the defendants, primarily in an amount equal to their respective equitable share of the cost of the environmental clean up of the site. The Company previously reported that based on preliminary investigations, it believed that the entity identified as "Roberts Consolidated", named as a defendant in this lawsuit, was neither the same entity nor a predecessor to any affiliates of the Company. In November, 2001, Roberts Consolidated Industries, Inc. was removed as a defendant and an entity identified as Roberts Holding International, Inc. was joined as a defendant in the case. Based on further investigation, the company believes that Roberts Holdings International, Inc., an inactive subsidiary of the Company, may in fact be a successor in interest to "Roberts Consolidated", but believes that its responsibility for the alleged contamination was assumed by other entities. Roberts Holdings International, Inc. has responded to the Complaint. Based on the information to date, the company believes that it has viable defenses, possible insurance coverage and/or claims against other entities for any damages. The Company has received notice from the United States Environmental Protection Agency (the "EPA") that an entity identified as Roberts Consolidated Industries, Inc. may be involved in the contamination of another landfill site in Clark County, Ohio. At this time, the Company is not aware whether this entity is a predecessor to any of its affiliates or whether it is an unrelated entity.

In June 2001, the Debtor in Possession for Hechinger Investment Company of Delaware, Inc. filed a complaint in the United States Bankruptcy Court to avoid and recover preferential transfers of Property under the United States Bankruptcy Code. The Company answered the complaint and is contesting the action. The Company does not believe the outcome will have a material adverse effect on the Company.

6

### Intellectual Property

The Company markets its specialty tools and related products under various trademarks owned by the Company or its subsidiaries, including Q.E.P.(TM), O'TOOL(TM) and ROBERTS(TM). The Company has devoted substantial time, effort and expense to the development of brand name recognition and goodwill for products sold under its trademarks, has not received any notice that its use of such marks infringes upon the rights of others, and is not aware of any activities which would appear to constitute infringement of any of its marks. Roberts Consolidated Industries, Inc. has secured domestic and foreign patents relating to certain of its carpet seaming products. Although the patents are important to the operation of Roberts Consolidated Industries, Inc., the Company does not believe that the loss of any one or more of these patents would have a material



## Edgar Filing: QEP CO INC - Form 10-K

adverse effect on the Company. These patents are scheduled to expire in the years 2008 and 2013. Roberts Consolidated Industries, Inc. also licenses its name to various foreign distributors.

### Employees

As of May 17, 2002, the Company had 373 employees, including 72 administrative employees, 59 sales and marketing employees, 130 manufacturing employees and 112 employees responsible for shipping activities. There are no part-time employees and 74 of the employees are employed by the Company's international subsidiaries. The Company has not experienced any work stoppages and none of the Company's employees are represented by a union. The Company considers its relations with the employees to be good.

### Item 2. Properties

The Company currently owns the facility in Bramalea, Ontario and leases all other facilities located in the United States, Canada, Europe, South America, New Zealand and Australia. All facilities aggregate approximately 652,000 square feet. The following table sets forth certain information concerning the facilities of the Company.

LOCATION -----	USE ---	SQUARE FEET -----	ANNUALIZED COST -----
Boca Raton, Florida	Executive offices, warehouse; manufacturing	77,000	\$398,710
Sliedrecht, Holland	Administrative; sales; manufacturing	52,544	77,090
Sliedrecht, Holland	Warehouse	63,259	34,404
Morfelden, Germany	Administrative; sales	300	631
Plaisir, France	Administrative; warehouse	1,700	23,847
Henderson, NV	Administrative; warehouse	111,000	387,021
Mexico, Missouri	Administrative; warehouse; manufacturing	155,000	344,609
Bramalea, Ontario	Administrative; warehouse; manufacturing	51,000	000
Mississauga, Ontario	Warehouse	15,000	64,207
Mississauga, Ontario	Warehouse	20,000	67,872
Buenos Aires, Argentina	Administrative; warehouse; manufacturing	4,293	2,911
Auckland, New Zealand	Administrative; warehouse	4,047	12,546
Dandenong, Australia	Manufacturing	26,200	73,408
Hindsmarch, Australia	Administrative; warehouse	7,234	14,903
Santiago, Chile	Administrative; warehouse; manufacturing	3,840	3,840
Little Falls, NJ	Administrative; warehouse; manufacturing	17,000	45,000
Calhoun, GA	Administrative; warehouse; manufacturing	25,000	4,167
Ft. Pierce, FL	Administrative; warehouse; manufacturing	18,000	72,000

The Company believes that its existing facilities are adequate to meet its current needs and that additional facilities can be leased to meet future needs. Further, it is expected that all leases necessary for the continuing operations of the Company expiring in 2002, will be renewed.

### Item 3. Legal Proceedings

The Company is involved in litigation from time to time in the course of its business. In the opinion of management, no material legal proceedings are pending to which the Company or any of its property is subject.

## Edgar Filing: QEP CO INC - Form 10-K

Roberts Consolidated Industries, Inc. has been named as a defendant in an amended complaint filed in CARGILL, INC. ET AL. V. ABCO CONSTRUCTION ET AL., a lawsuit initially filed in the United States District Court for the Southern District of Ohio Western Division on January 29, 1998. The lawsuit, brought under CERCLA and related state environmental laws, alleges that an entity known as "Roberts Consolidated" and the other defendants disposed of hazardous substances at a site located in Dayton, Ohio. The plaintiffs are seeking monetary damages against the defendants, primarily in an amount equal to their respective equitable share of the cost of the environmental clean up of the site. The Company previously reported that based on preliminary investigations, it believed that the entity identified as "Roberts Consolidated", named as a defendant in this lawsuit, was neither the same entity nor a predecessor to any affiliates of the Company. In November, 2001, Roberts Consolidated Industries, Inc. was removed as a defendant and an entity identified as Roberts Holding International, Inc. was joined as a defendant in the case. Based on further investigation, the company believes that Roberts Holdings International, Inc., an inactive subsidiary of the Company, may in fact be a successor in interest to "Roberts Consolidated", but believes that its responsibility for the alleged contamination was assumed by other entities. Roberts Holdings International, Inc. has responded to the Complaint. Based on the information to date, the company believes that it has viable defenses, possible insurance coverage and/or claims against other entities for any damages. The Company has received notice from the United States Environmental Protection Agency (the "EPA") that an entity identified as Roberts Consolidated Industries, Inc. may be involved in the contamination of another landfill site in Clark County, Ohio. At this time, the Company is not aware whether this entity is a predecessor to any of its affiliates or whether it is an unrelated entity.

In June 2001, the Debtor in Possession for Hechinger Investment Company of Delaware, Inc. filed a complaint in the United States Bankruptcy Court to avoid and recover preferential transfers of Property under the United States Bankruptcy Code. The Company answered the complaint and is contesting the action. The Company does not believe the outcome will have a material adverse effect on the Company.

#### Item 4. Submission of Matters to Vote of Security Holders

No matters were submitted to a vote of security holders of the Company during the fourth quarter of the period covered by this report.

## PART II

#### Item 5. Market for Registrant's Common Equity and Related Shareholder Matters

##### Market Price and Dividend Information

The Company's Common Stock is traded on the Nasdaq National Market System. The following table sets forth the high and low sales price per share for the Common Stock for each quarter during fiscal year 2002 and 2001, as reported on the Nasdaq National Market System.

	Fiscal Year Ended February 28,			
	2002		2001	
	High	Low	High	Low
First Quarter	\$5.170	\$3.000	\$7.300	\$5.850
Second Quarter	\$5.000	\$3.520	\$7.938	\$5.813
Third Quarter	\$4.320	\$3.400	\$6.750	\$4.250
Fourth Quarter	\$5.080	\$3.510	\$5.500	\$3.000

Edgar Filing: QEP CO INC - Form 10-K

On May 17 2002, the closing price of the Common Stock on the Nasdaq National Market System was \$4.24 per share. As of that date, there were 26 holders of record of the Common Stock and approximately 642 beneficial owners of the Common Stock.

The Company has not paid cash dividends and does not intend for the foreseeable future to declare or pay any cash dividends on its Common Stock and intends to retain earnings, if any, for the future operation and expansion of the Company's business. Any determination to declare or pay dividends will be at the discretion of the Company's board of directors and will depend upon the Company's future earnings, results of operations, financial condition, capital requirements, considerations imposed by applicable law and other factors deemed relevant by the board of directors. The Company's credit facility also prohibits the payment of dividends without the consent of the lender.

Item 6. Selected Financial Data

The selected consolidated financial data set forth below as of and for the years ended February 28 or 29, 1998, 1999, 2000, 2001 and 2002 have been derived from the audited consolidated financial statements of the Company. The audited financial statements for the years ended February 28, 1998 and 1999 and the audited balance sheet as of February 29, 2000 are not included in this filing. The selected consolidated financial data should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" (Item 7 of this report) and the audited consolidated financial statements and related notes thereto included elsewhere herein. Earnings per share amounts in fiscal 1997 through fiscal 2000 have been adjusted to reflect the five for four stock split discussed elsewhere herein.

		FISCAL YEAR ENDED FEBRUARY 2	
	2002	2001	2000
OPERATING DATA:		(IN THOUSANDS, EXCEPT PER SHARE)	
Net Sales	\$109,675	\$113,003	\$113,571
Cost of goods sold	72,603	76,940	79,037
Gross profit	37,072	36,063	34,534
Shipping	9,589	9,801	8,987
General and administrative	9,512	9,554	9,373
Selling and marketing	11,895	11,616	9,494
Restructuring charge	--	637	--
Foreign exchange losses	11	4	7
Operating income	6,065	4,451	6,673
Interest expense, net	2,557	2,131	1,700
Income before provision for income taxes and extraordinary item	3,508	2,320	4,973
Provision for income taxes	1,405	887	1,951
Net income before extraordinary item	2,103	1,433	3,022
Extraordinary item, gain on early extinguishment of debt	--	--	181
Net income	\$ 2,103	\$ 1,433	\$ 3,203

## Edgar Filing: QEP CO INC - Form 10-K

	=====	=====	=====
Basic and diluted net income per common share			
before extraordinary item	\$ .62	\$ .42	\$ .90
Extraordinary item	--	--	.05
	-----	-----	-----
Basic and diluted earnings per share	\$ .62	\$ .42	\$ .95
	=====	=====	=====
Weighted average number of shares of common stock outstanding	3,390	3,369	3,365
	=====	=====	=====

	FISCAL YEAR ENDED FEBRUARY 2		
	2002	2001	2000
	-----	-----	-----
BALANCE SHEET DATA:			(IN THOUSANDS)
Working capital	\$ 9,710	\$ 9,788	\$ 13,511
Total assets	62,371	64,036	57,715
Long term obligations	9,143	11,241	11,588
Total liabilities	39,321	41,923	36,532
Shareholders' equity	23,050	22,113	21,183

9

### Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

#### General

The Company manufactures, markets and distributes a broad line of specialty tools and flooring related products for the home improvement market. The Company markets over 3,000 specialty tools and related products used primarily for surface preparation and installation of ceramic tile, carpet and marble. The Company's products are sold through home improvement retailers, specialty distributors to the hardware, construction, flooring and home improvement trades, chain or independent hardware, tile and carpet retailers for use by the do-it-yourself consumer as well as the construction or remodeling professional, and original equipment manufacturers. Dollar figures set forth below are rounded to the nearest thousand.

#### Accounting Policies and Estimates

The Securities and Exchange Commission ("SEC") recently issued disclosure guidance for critical accounting policies. The SEC defines "critical accounting policies" as those that require complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in subsequent periods.

Management's discussion and analysis of its financial condition and results of operations are based upon the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The notes to the financial statements include a summary of significant accounting policies used in the preparation of the consolidated financial statements (see Note B).

The Company believes the following critical accounting policies affects its more significant judgments and estimates used in the preparation of its consolidated financial statements:

## Edgar Filing: QEP CO INC - Form 10-K

### Revenue Recognition

The Company recognizes sales when the merchandise is shipped. The Company provides for estimated costs of future anticipated product returns, based on historical experience, when the related revenues are recognized. The Company records estimated reductions to revenue for customer programs including volume-based incentives.

### Inventory Obsolescence

The Company maintains reserves for estimated obsolescence or unmarketable inventory equal to the difference between the cost of inventory and the estimated market value based upon assessments about current and future demand and market conditions. If actual market conditions were to be less favorable than those projected by management, additional inventory reserves could be required.

### Allowance for Doubtful Accounts

The Company maintains allowances for doubtful accounts for estimated losses resulting from the Company's review and assessment of its customers' ability to make required payments. If the financial condition of the Company's customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances might be required.

### Results of Operations

#### Fiscal 2002 as compared to Fiscal 2001

Net sales for the twelve months ended February 28, 2002 ("fiscal 2002", or the "fiscal 2002 period") were \$109,674,000 compared to \$113,003,000 for the twelve months ended February 28, 2001 ("fiscal 2001", or the "fiscal 2001 period"), a decrease of \$3,329,000 or 3.0%. Selling prices remained relatively stable.

10

Net sales for the current year were negatively impacted by the licensing of the Company's domestic distributor tack strip business, which had sales of approximately \$2,957,000 in the prior year. The Company also experienced a decline in its domestic distribution and international business. These negative impacts were partially offset by sales to home center customers which increased primarily as a result of new store openings and new product introduction into existing stores.

Gross profit for fiscal 2002 was \$37,072,000 compared to \$36,063,000 for fiscal 2001, an increase of \$1,009,000 or 2.8%. As a percentage of net sales, gross profit increased to 33.8% in fiscal 2002 from 31.9% in fiscal 2001, primarily due to a change in product mix towards higher margin products, a reduction of certain raw material costs and the discontinuance of the sale to domestic distributors of the low margin tack strip product.

Shipping expenses for the fiscal 2002 period were \$9,589,000 compared to \$9,801,000 for the fiscal 2001 period, a decrease of \$212,000 or 2.2%. As a percentage of net sales, these expenses remained flat at 8.7% of sales in the fiscal 2002 and fiscal 2001 periods, primarily as a result of certain fixed costs being absorbed by a smaller sales volume as a result of the licensing of the domestic distributor tack strip business. The actual increase was substantially attributable to the increased sales volume to the Company's home center customer base and an absorption of a higher percentage of freight costs by the Company to its domestic distributors resulting from the licensing of the tack strip business.

## Edgar Filing: QEP CO INC - Form 10-K

General and administrative expenses for the fiscal 2002 period were \$9,741,000 compared to \$9,650,000 for the fiscal 2001 period, an increase of \$91,000 or 0.9%. As a percentage of net sales, these expenses increased slightly to 8.9% in the fiscal 2002 period from 8.5% in the fiscal 2001 period. This increase was primarily due to the absorption of fixed costs over a reduced sales volume. The actual increase was primarily the result of goodwill amortization resulting from companies acquired in fiscal 2001, offset by a reduction of expenses at the Company's domestic divisions.

Selling and marketing costs for the fiscal 2002 period increased to \$11,895,000 from \$11,616,000 in the fiscal 2001 period, an increase of \$279,000 or 2.4%. As a percentage of net sales, these expenses increased to 10.8% in the fiscal 2002 period from 10.3% in the fiscal 2001 period principally as a result of the reduced sales volume attributable to the licensing of the domestic distributor tack strip business and an increase in commission rates paid to the Company's sales force. The increase in the actual amount of these expenses is attributable to the increase in commissions and higher marketing allowances paid to home center customers resulting principally from the increased sales volume to these customers.

During the third quarter of the fiscal 2001 period, the Company finalized its plan to close its California facility and relocate to Nevada. Additionally, the Company initiated a downsizing of its Holland subsidiary to reduce costs. In connection with these decisions, the Company recorded a restructuring charge of approximately \$637,000 in the fiscal 2001 period.

Interest income for the fiscal 2002 period was approximately \$10,000 compared to \$175,000 in fiscal 2001 as a result of lower interest rates and the repayment of notes receivable in fiscal 2001. Interest expense for the fiscal 2002 period was approximately \$2,567,000 compared to approximately \$2,307,000 in fiscal 2001. Interest expense increased primarily as a result of the increase in short-term borrowings to fund working capital and as a result of the interest rate Swap Agreements that were in place during fiscal 2002.

Provision for income taxes was \$1,405,000 in fiscal 2002 compared to \$887,000 in fiscal 2001, an increase of \$518,000 or 58.3%. The increase is the result of the increase in the Company's taxable income and an additional provision for certain foreign taxes. The effective tax rate was approximately 40.0% in the fiscal 2002 period compared to 38.2% in the fiscal 2001 period. The estimated tax rate is based upon the most recent effective tax rates available.

11

Net income for the fiscal 2002 period increased to \$2,103,000 compared to \$1,433,000 in fiscal 2001, an increase of \$670,000 or 46.8%. Net income as a percentage of sales increased to 1.9% in fiscal 2002 compared to 1.3% in fiscal 2001, reflecting a slightly higher gross profit margin resulting from the licensing of the domestic distributor tack strip business and lower shipping costs offset by higher selling, marketing, general and administrative costs.

### Results of Operations

#### Fiscal 2001 as compared to Fiscal 2000

Net sales for the twelve months ended February 28, 2001 ("fiscal 2001", or the "fiscal 2001 period") were \$113,003,000 compared to \$113,571,000 for the twelve months ended February 29, 2000 ("fiscal 2000", or the "fiscal 2000 period"), a decrease of \$568,000 or .5%. Selling prices remained relatively stable. Sales to home center customers increased primarily as a result of new store openings and expansion of the Company's business to one of its major Home Center customers.

## Edgar Filing: QEP CO INC - Form 10-K

In May 2000, the Company discontinued the sale of its tackless carpet strip product to domestic distributors and licensed the rights of sale to a third party. As a result, sales to the specialty distributor customer base of the Company declined. Also impacting sales were additional incentives provided to one of the Company's major customers. The impact from the licensing of the tackstrip business and additional sales incentive was approximately \$12,158,000.

Gross profit for fiscal 2001 was \$36,063,000 compared to \$34,534,000 for fiscal 2000, an increase of \$1,529,000 or 4.4%. As a percentage of net sales, gross profit increased to 31.9% in fiscal 2001 from 30.4% in fiscal 2000, primarily due to a change in product mix towards higher margin products and the discontinuance of the sale to domestic distributors of the low margin tackstrip product. These increases were slightly offset by the aforementioned additional customer incentives.

Shipping expenses for the fiscal 2001 period were \$9,801,000 compared to \$8,987,000 for the fiscal 2000 period, an increase of \$814,000 or 9.1%. As a percentage of net sales, these expenses increased to 8.6% in the fiscal 2001 period from 7.9% in the fiscal 2000 period, primarily as a result of an increase in freight rates charged by common carriers. In addition, other freight costs remained relatively constant causing costs as a percentage of sales to increase. The actual increase was substantially attributable to the increased sales volume, increased freight costs and an absorption of a higher percentage of freight costs by the Company to its domestic distributors.

General and administrative expenses for the fiscal 2001 period were \$9,650,000 compared to \$9,393,000 for the fiscal 2000 period, an increase of \$257,000 or 2.7%. As a percentage of net sales, these expenses increased slightly to 8.5% in the fiscal 2001 period from 8.3% in the fiscal 2000 period. This increase was primarily due to the absorption of fixed costs over a reduced sales volume. The actual increase was primarily the result of costs associated with the relocation of the Company's California facility to Nevada, approximately \$600,000, offset by a reduction of expenses at the Company's domestic divisions.

Selling and marketing costs for the fiscal 2001 period increased to \$11,616,000 from \$9,494,000 in the fiscal 2000 period, an increase of \$2,122,000 or 22.4%. As a percentage of net sales, these expenses increased to 10.3% in the fiscal 2001 period from 8.4% in the fiscal 2000 period principally as a result of the reduced sales volume, an increase in commission rates paid to the Company's sales force and an increase in marketing allowance rates to one of the Company's major customers. The increase in the actual amount of these expenses is attributable to the increase in commissions paid to sales personnel and marketing allowances to home center customers resulting principally from the increased sales volume.

During the third quarter of the fiscal 2001 period, the Company finalized its plan to close its California facility and relocate to Nevada where it is anticipated that the Company will realize certain manufacturing efficiencies, reduced cost of operations and tax savings. Additionally, the Company initiated a downsizing of its Holland subsidiary to reduce costs. In connection with these decisions, the Company recorded a restructuring charge of approximately \$637,000 in the fiscal 2001 period. As of

12

February 28, 2001, substantially all costs of the plant closing and downsizing were paid and there remained an approximate \$70,000 reserve for the downsizing of Holland.

Interest income for the fiscal 2001 period was approximately \$175,000 compared to \$133,000 in fiscal 2000. Interest expense for the fiscal 2001 period was

## Edgar Filing: QEP CO INC - Form 10-K

approximately \$2,307,000 compared to approximately \$1,834,000 in fiscal 2000. Interest expense increased primarily as a result of the increase in borrowings associated with the funding of the increase in inventory and accounts receivable caused by higher sales volume and an increase in borrowing rates.

Provision for income taxes was \$887,000 in fiscal 2001 compared to \$1,951,000 in fiscal 2000, a decrease of \$1,064,000 or 54.5%. The decrease is the result of the decrease in the Company's taxable income. The effective tax rate was approximately 38.2% in the fiscal 2001 period compared to 39.2% in the fiscal 2000 period. The estimated tax rate is based upon the most recent effective tax rates available.

Net income for the fiscal 2001 period decreased to \$1,433,000 compared to \$3,203,000 in fiscal 2000, a decrease of \$1,770,000 or 55.3%. Net income as a percentage of sales decreased to 1.3% in fiscal 2001 compared to 2.8% in fiscal 2000, reflecting a slightly higher gross profit margin resulting from the licensing of the domestic distributor tack strip business offset by sales incentives provided to a major retailer, higher selling and marketing, shipping, general and administrative and restructuring expenses as a percentage of sales as described above.

### Liquidity and Capital Resources

Working capital decreased to approximately \$9,710,000 at February 28, 2002 from approximately \$9,788,000 at February 28, 2001, a decrease of \$78,000, primarily as a result of the payment of long-term debt, capital expenditures and the purchase of treasury stock. Any cash in excess of anticipated requirements is invested in commercial paper or overnight repurchase agreements with a financial institution. The Company states the value of such investments at market price and classifies them as cash equivalents in its balance sheet.

Net cash provided by operating activities during the fiscal 2002 period was \$2,614,000 compared to \$367,000 for the comparable fiscal 2001 period. The increase in cash from operating activities was primarily the result of an increase in income from operations as adjusted for non-cash charges for depreciation and amortization and a slight increase in accounts receivable and inventory compared to significant prior year increases in receivable and inventory accounts. Net cash used in investing activities was \$577,000 in the fiscal 2002 period compared to \$3,185,000 for the comparable fiscal 2001 period. The fiscal 2002 amount was attributable to capital expenditures whereas the fiscal 2001 amount was the result of capital expenditures and funds expended for certain of the newly acquired entities.

For the fiscal 2002 period, cash used in financing activities was \$1,573,000 that was primarily the result of payments of long-term debt, including acquisition debt. Net cash provided by financing activities was \$2,721,000 in the fiscal 2001 period due primarily to the increase in short term bank debt associated with the newly acquired entities and collections on notes receivable offset by the repayment of long term and acquisition debt.

The Company has a revolving credit and term loan facility agreement with a United States financial institution. This agreement, which was amended on April 5, 2001, provides for borrowings of up to \$18,000,000 (subsequent to February 28, 2002 this was increased to \$20,000,000 through June 3, 2002) against a fixed percentage of eligible accounts receivable and inventory. Interest is payable based on a sliding scale depending on the Company's senior debt to EBITDA ranging from LIBOR plus 1.75% to LIBOR plus 2.5%. This facility terminates in July 2003 and is collateralized by substantially all of the Company's assets. Under the terms of the credit agreement, the Company is required to maintain certain financial ratios and conditions. The credit agreement also prohibits the Company from incurring certain additional indebtedness, limits certain investments, advances or loans and restricts substantial asset sales and capital



## Edgar Filing: QEP CO INC - Form 10-K

expenditures. The terms of the Company's credit facility also prohibits the payment of

13

dividends, except with the lender's consent. Prior to this amendment the Company was allowed to borrow up to \$16,500,000 based on the same fixed percentage of eligible accounts receivable and inventory. Interest was charged on a sliding scale. As of February 28, 2002, interest was at LIBOR (1.85 at February 28, 2002) plus 2.00%. At February 28, 2002, the Company had \$1,113,000 available for future borrowings under the credit facility.

The Company's Chilean subsidiary has a revolving credit facility with a financial institution, which permits borrowings of up to \$100,000 with interest at 18% per year. The facility is secured by a standby letter of credit given by the Company. This facility expires on May 31, 2002 and is expected to be renewed at a reduced amount. At February 28, 2002 the Chilean subsidiary had approximately \$54,000 available for future borrowings under the credit facility. The Company's Australian subsidiary also has an overdraft facility which allows it to borrow against a certain percentage of inventory and receivables. At February 28, 2002 the maximum permitted borrowing was approximately \$361,000 of which approximately \$86,000 was available for future borrowing.

In connection with the acquisition of Roberts Consolidated Industries, Inc., the Company issued \$7,500,000 of subordinated debentures. They were recorded at their fair value on the date of issuance in the amount of \$6,515,000 and the discount was amortized over the life of the debentures. During the third quarter of fiscal 2000, the Company repurchased approximately \$1,229,000 of its debentures at a discount resulting in an extraordinary gain from early extinguishment of debt of approximately \$181,000. At February 28, 2001, the remaining amortized balance of this obligation was \$6,104,000. These debentures matured in April 2001 and bore interest at 8%.

On April 5, 2001 the Company entered into a new \$4,500,000 subordinated credit facility with HillStreet Fund LP. This facility bears an interest rate of 15% and matures in six years. Equal quarterly payments of \$562,500 are required beginning in year five. The agreement also provides for an additional 3% interest if the Company does not meet certain financial covenants. In addition, the Company issued 325,000 10-year warrants at \$3.63. These warrants can be put to the Company after the fifth year based on criteria set forth in the warrant agreement. In addition, the Company may call these warrants after the sixth year based on the same criteria. The Company has recorded a liability for these put warrants based on an independent appraisal. Changes to the fair value of the put warrants will be recognized in earnings of the Company in accordance with SFAS No. 133 "Accounting for Derivative Instruments and Hedging Activities." The resulting discount of the subordinated credit facility will be amortized over the life of the debt.

In connection with the newly acquired entities, the Company issued five notes to the respective sellers. Two of the notes, aggregating approximately \$1,260,000, were paid in fiscal 2001 and were non-interest bearing. The third note, having an original principal balance of \$900,000, is payable in equal installments in October over a three year period with interest at the Company's prevailing borrowing rate. At February 28, 2002 the remaining balance on this note is \$300,000. The fourth note, in the principal amount of \$825,000, is payable in installments: \$312,500 was paid in December 2000, \$312,500 plus interest of \$12,500 originally due in December 2001 was paid \$125,000 in December 2001 and \$200,000 over a ten month period beginning January 2002 and \$200,000 in December 2003. Interest is fixed at \$12,500, \$12,500 and \$25,000, respectively. The fifth note in the original principal amount of \$1,600,000, is payable quarterly at

## Edgar Filing: QEP CO INC - Form 10-K

\$80,000 plus interest at 8% from October 1, 2000 through October 1, 2005.

In October 2000, the Company entered into an agreement to purchase its Bramalea, Ontario facility for approximately \$988,000. In connection with this purchase, the Company paid approximately \$318,000 in cash and obtained a loan for the balance from a Canadian lending institution of approximately \$670,000 payable over 10 years at an interest rate to be set annually (6.1% as of February 28, 2002).

On December 23, 2000, the Company entered into an interest rate swap agreement with its primary lender. The interest rate swap agreement hedges the Company's exposure on certain floating rate obligations in the aggregate principal amount of \$10,000,000. The purpose of the interest rate swap is to convert the Company's floating rate interest obligations to obligations having a fixed rate of 6.0% per annum for a one-year period. Prior to this interest rate swap, the Company had one with the same institution that matured in December 2000. The fixing of the interest rates reduces in part the Company's exposure to the uncertainty of floating interest rates. The differential paid or received by the Company on

14

the interest rate swap agreement is recognized as an adjustment to interest expense in the period incurred. For the year ended February 28, 2002, the Company increased interest expense by approximately \$162,000 as a result of the interest rate swap agreements that were in place during that period. The interest rate swap agreement expired in December 2001 and was not renewed.

The Company believes its existing cash balances, internally generated funds from operations and its available bank lines of credit will provide the liquidity necessary to satisfy the Company's working capital needs, including the growth in inventory and accounts receivable balances, and will be adequate to finance anticipated capital expenditures and debt obligations for the next twelve months. There can be no assurance, however, that the assumptions upon which the Company bases its future working capital and capital expenditure requirements and the assumptions upon which it bases that funds will be available to satisfy such requirements will prove to be correct. If these assumptions are not correct, the Company's assessment of its liquidity position could prove to be incorrect.

### Recently Issued Accounting Standards

On July 20, 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 141, "Business combinations," and SFAS No. 142, "Goodwill and Intangible Assets." SFAS No. 141 is effective for all business combinations completed after June 30, 2001. SFAS No. 142 is effective for fiscal years beginning after December 15, 2001; however, certain provisions of this Statement apply to goodwill and other intangible assets acquired between July 1, 2001 and the effective date of SFAS No. 142. Major provisions of these Statements and their effective dates for the Company are as follows:

- .. All business combinations initiated after June 30, 2001 must use the purchase method of accounting. The pooling-of-interests method of accounting is prohibited except for transactions initiated before July 1, 2001;
- .. Intangible assets acquired in a business combination must be recorded separately from goodwill if they arise from contractual or other legal rights or are separable from the acquired entity and can be sold, transferred, licensed, rented or exchanged, either individually or as part

## Edgar Filing: QEP CO INC - Form 10-K

of a related contract, asset or liability;

- .. Goodwill, as well as intangible assets with indefinite lives, acquired after June 30, 2001, will not be amortized. Effective March 1, 2002, all previously recognized goodwill and intangible assets with indefinite lives will no longer be subject to amortization;
- .. Effective March 1, 2002, goodwill and intangible assts with indefinite lives will be tested for impairment annually and whenever there is an impairment indicator; and,
- .. All acquired goodwill must be assigned to reporting units for purposes of impairment testing and segment reporting.

The Company will continue to amortize goodwill recognized prior to July 1, 2001, under its current method, until March 1, 2002, at which time quarterly and annual goodwill amortization of approximately \$118,000 and \$471,000 respectively, will no longer be recognized.

The Company is in the process of completing its evaluation and believes that there will be an effect on the amount it currently has recorded as intangible assets as they relate to the Company's Latin American and European operations. Any impairment loss will be recorded in the Company's first quarter of fiscal 2003 as a cumulative effect of a change in accounting principle.

15

In August 2001, the FASB issued SFAS No. 144 "Accounting for the Impairment or Disposal of Long Lived Assets". SFAS No. 144 supercedes SFAS No. 121 "Accounting for the Impairment of Long Lived Assets and for Long Lived Assets to be Disposed Of". SFAS 144 retains substantially all of the requirements of SFAS 121 while resolving certain implementation issues. SFAS 144 is effective for fiscal years beginning after December 15, 2001 with earlier implementation encouraged. The Company is currently evaluating the impact on its financial statements of adopting SFAS 144.

### Forward-Looking Statements

This report contains certain forward-looking statements which are made pursuant to the safe harbor provisions of the Securities Litigation Reform Act of 1995. Statements as to what the Company "believes," "intends," "expects," or "anticipates" and other similar anticipatory expressions, are generally forward-looking and are made only as of the date of this report and are not related to historical results. Such statements include statements relating to the Company's anticipated revenues from its distribution agreement for tackless carpet strip and the adequacy of the Company's liquidity sources to meet the Company's working capital needs and anticipated expenditures. Additionally, the report is subject to risks and uncertainties which could cause actual results to differ materially from those discussed in the forward-looking statements and from historical results of operations. Among the risks and uncertainties which could cause such a difference are the Company's anticipation of performance by distributors of its tackless carpet strip, the assumptions upon which the Company bases its assessments of its future working capital and capital expenditure requirements and those relating to the Company's ability to satisfy its working capital needs and to finance its anticipated capital expenditures which could prove to be different than expected, the Company's dependence upon a limited number of customers for a substantial portion of its sales, the Company's reliance upon suppliers and sales agents for the purchase of finished products which are then resold by it, the level of demand for the Company's products among existing and potential new customers, the Company's ability to

## Edgar Filing: QEP CO INC - Form 10-K

successfully manage and integrate the business and operations of its newly acquired entities, the Company's dependence upon certain key personnel and its ability to successfully integrate new management personnel into the Company, the Company's ability to accurately predict the number and type of employees required to conduct its European operations and the compensation required to be paid to such personnel, its ability to manage its growth, the risk of economic and market factors affecting the Company or its customers and other risks and uncertainties described elsewhere herein.

### Item 7A. Quantitative and Qualitative Disclosures about Market Risk

On December 23, 2000, the Company entered into an interest rate swap agreement with its primary lender. The interest rate swap agreement hedges the Company's exposure on certain floating rate obligations in the aggregate principal amount of \$10,000,000. The purpose of the interest rate swap is to convert the Company's floating rate interest obligations to obligations having a fixed rate of 6.0% per annum for a one-year period. Prior to this interest rate swap, the Company had a similar arrangement with the same institution that matured in December 2000. The fixing of the interest rates reduces in part the Company's exposure to the uncertainty of floating interest rates. The differential paid or received by the Company on the interest rate swap agreement is recognized as an adjustment to interest expense in the period incurred. For the year ended February 28, 2002, the Company increased interest expense by approximately \$162,000 as a result of the interest rate swap agreements that were in place during that period. The interest rate swap agreement expired in December 2001 and was not renewed.

The Company averaged approximately \$10,202,000 of variable rate debt not covered by the interest rate swap agreement during fiscal 2002. If interest rates would have increased by 10%, the effect on the Company would have been an increase in interest expense of approximately \$43,000.

The Company issued 325,000 warrants associated with certain of its subordinated debt. These warrants contain put and call provisions as defined in the agreement of the price of the warrant charges by \$0.10, the effect on the Company would be an adjustment to Earnings of \$32,500.

### Item 8. Financial Statements and Supplementary Financial Data

The response to this item is submitted on pages F1 - F24 of this Report.

### Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure

None.

16

## PART III

### Item 10. Directors and Executive Officers of the Registrant

Information required by this item regarding directors and officers is incorporated by reference from the definitive Proxy Statement to be filed by the Company for the Annual Meeting of Stockholders to be held on July 12, 2002.

### Item 11. Executive Compensation

Information required by this item regarding compensation of officers and directors is incorporated by reference from the definitive Proxy Statement to be filed by the Company for the Annual Meeting of Stockholders to be held on July 12, 2002.

### Item 12. Security Ownership of Certain Beneficial Owners and Management

## Edgar Filing: QEP CO INC - Form 10-K

Information required by this item is incorporated by reference from the definitive Proxy Statement to be filed by the Company for the Annual Meeting of Stockholders to be held on July 12, 2002.

### Item 13. Certain Relationships and Related Transactions

Information required by this item is incorporated by reference from the definitive Proxy Statement to be filed by the Company for the Annual Meeting of Stockholders to be held on July 12, 2002.

## PART IV

### Item 14. Exhibits, Financial Statement Schedules, and Reports on Form 8-K

(a) The following documents are filed as part of the report:

1. and 2. The financial statements filed as part of this report are listed separately in the index to Financial Statements beginning on page F-1 of this report.

3. For Exhibits see Item 14 (c), below. Exhibit Nos. 10.1 and 10.1.1 consist of management contracts or compensatory plans or arrangements required to be filed as exhibits to this report.

(b) Reports on Form 8-K

-----  
None

(c) List of Exhibits:

Exhibit	Description
-----	-----
No.	
---	
2.1	Form of Agreement and Plan of Merger regarding the change in incorporation of the Company from a New York Corporation to a Delaware Corporation*
2.1.1	Stock Purchase Agreement dated October 21, 1997 between the Company and RCI Holdings, Inc.****
3.1.1	Certificate of Incorporation of the Company*
3.1.2	Bylaws of the Company**
3.3	Form of Indemnification Agreement executed by Officers and Directors of the Company*
17	
4.1	Form of specimen certificate for Common Stock of the Company*
4.1.1	Form of Warrant issued by the Company to the representative of the underwriters of the Company's initial public offering*
9	Voting Trust Agreement, dated August 3, 1996, by and between Lewis Gould and Susan J. Gould*
10.1	Employment Agreement, dated August 3, 1996, by and between Lewis Gould

## Edgar Filing: QEP CO INC - Form 10-K

and the Company\*

- 10.1.1 Q.E.P. Co., Inc. Omnibus Stock Plan of 1996\*\*
- 10.2.6 Lease Agreement, dated September 17, 1996, by and among the Company and Lawrence Z. Crockett, as Trustee of the Lawrence Z. Crockett Trust dated March 31, 1994 and Marilyn M. Crockett, as Trustee of the Marilyn M. Crockett Trust dated March 31, 1994, including amendment thereto dated January 22, 1997\*\*
- 10.2.7 Industrial Lease, dated August 1, 1996, by and between JMB/Pennsylvania Advisors - IV, L.P., and the Company\*\*
- 10.3.1.1 Revolving Loan and Security Agreement and Assignment of Leases, dated October 13, 1995, by and between Shawmut Bank Connecticut, N.A., a national banking association, and the Company, including Promissory Note dated October 13, 1995, Limited Guaranty of Lewis Gould dated October 13, 1995, and form of Guaranty executed by the Company's subsidiaries\*
- 10.3.2 First Amendatory Agreement to Revolving Loan and Security Agreement, dated as of July 25, 1997, by and among Q.E.P. Co., Inc. and its subsidiaries and Fleet National Bank (f/k/a Shawmut Bank Connecticut, N.A.), including Amended and Restated Revolving promissory Note dated July 25, 1997 and Release of Limited Guaranty of Lewis Gould, dated July 25, 1997.\*\*\*
- 10.3.3 Amended and Restated Loan Agreement by and among Q.E.P. Co., Inc., Q.E.P.-O'Tool, Inc., Marion Tool Corporation, Westpoint Foundry, Inc., Roberts Consolidated Industries, Inc., Roberts Holding International, Inc., and Roberts Company Canada Limited and Fleet National Bank dated as of October 21, 1997.\*\*\*\*\*
- 10.3.3A First Amendatory Agreement to the Amended and Restated Loan Agreement by and among Q.E.P. Co., Inc., Q.E.P.-O'Tool, Inc., Marion Tool Corporation, Westpoint Foundry, Inc., Roberts Consolidated Industries, Inc., Roberts Holding International, Inc., and Roberts Company Canada Limited and Fleet National Bank dated as of October 21, 1997.\*\*\*\*\*
- 10.3.4 Stock Purchase Agreement effective January 1, 1998 between Q.E.P. Holding B.V. and Roberts Beheer B.V.\*\*\*\*\*
- 10.3.5 Purchase and Sale Agreement effective as of December 31, 1997 between Roberts Beheer B.V., Q.E.P. Co., Inc. and Roberts Consolidated Industries, Inc.\*\*\*\*\*
- 10.3.6 Subordinated Loan and Security Agreement, dated April 5, 2001, by and between The HillStreet Fund, L.P. and the Company, including Subordinated Term Promissory Note dated April 5, 2001, Warrant Agreement dated April 5, 2001, and Warrant dated April 5, 2001.\*\*\*\*\*
- 10.3.7. Fourth Agreement of Amendment, dated April 5, 2001, by and between Fleet Capital Corporation and the Company, including 2001 Term Note dated April 5, 2001, Guaranty of Lewis Gould dated April 5, 2001, Amended Trademark Collateral Security Agreement\*\*\*\*\*
- 21 Subsidiaries of the Company\*\*\*\*\*

## Edgar Filing: QEP CO INC - Form 10-K

- 99.1 Form of Warrant issued to the following persons in the following amounts: RCI Holdings, Inc. (100,000) and Marlborough Capital Fund, Ltd. (100,000) \*\*\*\*
- 99.2 Form of 8% Convertible Subordinated Debenture issued to the following persons in the following amounts: RCI Holdings, Inc. (\$1,911,673.30), Marlborough Capital Fund, Ltd. (\$5,088,326.70), and IBJ Schroeder as Escrow Agent (\$500,000).\*\*\*\*
- 99.3 Escrow Agreement dated October 21, 1997 among the Company, RCI Holdings, Inc., and IBJ Schroeder.\*\*\*\*

- 
- \* Incorporated by reference to Exhibit of the same number filed with the Company's Registration Statement on Form S-1 (Reg. No. 333-07477).
- \*\* Incorporated by reference to Exhibit of the same number filed with the Company's Annual Report on Form 10-K filed on May 28, 1997.
- \*\*\* Incorporated by reference to Exhibit of the same number filed with the Company's Quarterly Report on Form 10-Q filed on October 14, 1997.
- \*\*\*\* Incorporated by reference to Exhibit of the same number filed with the Company's Report on Form 8-K filed on November 3, 1997 (except that Exhibit 2.1.1 above was numbered 2.1 in the Form 8-K).
- \*\*\*\*\* Incorporated by reference to Exhibit of the same number filed with the Company's Quarterly Report on Form 10-Q filed on January 14, 1998.
- \*\*\*\*\* Incorporated herein by reference to Exhibit of the same number filed with the Company's Annual Report on Form 10-K filed on May 28, 1998.
- \*\*\*\*\* Incorporated herein by reference to Exhibit of the same number filed with the Company's Annual Report on Form 10-K filed on May 27, 2000.
- \*\*\*\*\* Incorporated herein by reference to Exhibit of the same number filed with the Company's Annual Report on Form 10-K filed on May 28, 2001.
- (d) The financial statement schedule filed as part of this report is listed separately in the Index to Financial Statements beginning on page F-1 of this report.

19

### SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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, in the City of Boca Raton, Florida, State of Florida, on May 28, 2002.

Q.E.P. CO., INC,  
By: /s/ Lewis Gould

-----  
Lewis Gould  
Chairman and Chief Executive Officer

KNOW ALL MEN BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Lewis Gould and Marc Applebaum and each of them, his true and lawful attorney-in-fact and agents, with full power of substitution and

## Edgar Filing: QEP CO INC - Form 10-K

resubstitution for him and in his name, place and stead, in any and all capacities, to sign any and all amendments to this report, and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents full power and authority to do and perform each and every act and thing requisite and necessary to be done in and about the premises, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that each of said attorneys-in-fact or his substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

/s/ Lewis Gould ----- Lewis Gould	Chairman, Chief Executive Officer and Director (Principal Executive Officer)	May 28, 2002
/s/ Marc Applebaum ----- Marc Applebaum	Senior Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)	May 28, 2002
/s/ Robert Feuerzeig ----- Robert Feuerzeig	Director	May 28, 2002
/s/ Emil Vogel ----- Emil Vogel	Director	May 28, 2002
/s/ Christian Nast ----- Christian Nast	Director	May 28, 2002
/s/ Leonard Gould ----- Leonard Gould	Director	May 28, 2002
/s/ David Malizia ----- David Malizia	Director	May 28, 2002
/s/ Pierre Simard ----- Pierre Simard	Director	May 28, 2002
/s/ Ernst Ohnell ----- Ernst Ohnell	Director	May 28, 2002

### C O N T E N T S

	Page
	----
Report of Independent Certified Public Accountants	F-2



## Edgar Filing: QEP CO INC - Form 10-K

### Financial Statements

Consolidated Balance Sheets	F-3
Consolidated Statements of Income	F-4
Consolidated Statement of Shareholders' Equity	F-5
Consolidated Statements of Cash Flows	F-6
Notes to Consolidated Financial Statements	F-7 to F-24
Schedule II - Valuation and Qualifying Accounts	S-1

F-1

### REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors and Shareholders  
Q.E.P. Co., Inc. and Subsidiaries

We have audited the accompanying consolidated balance sheets of Q.E.P. Co., Inc. (a Delaware corporation) and Subsidiaries as of February 28, 2002 and February 28, 2001, and the related consolidated statements of income, shareholders' equity, and cash flows for each of the three years in the period ended February 28, 2002. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to maintain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Q.E.P. Co., and Subsidiaries as of February 28, 2002 and February 28, 2001, and the results of their operations and their cash flows for each of the three years in the period ended February 28, 2002 in conformity with accounting principles generally accepted in the United States of America.

We have also audited Schedule II of Q.E.P. Co., Inc. and Subsidiaries for each of the three years in the period ended February 28, 2002. In our opinion, this schedule presents fairly, in all material respects, the information required to be set forth therein.

/s/ Grant Thornton LLP  
Grant Thornton LLP

Miami, Florida  
April 15, 2002

Edgar Filing: QEP CO INC - Form 10-K

F-2

Q.E.P. CO., INC. AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS

ASSETS	February 28, 2002	Febru
	-----	-----
CURRENT ASSETS		
Cash and cash equivalents	\$ 435,320	\$
Accounts receivable, less allowance for doubtful accounts of approximately \$422,000 and \$662,000 as of February 28, 2002 and February 28, 2001, respectively.	17,267,501	
Notes receivable	21,845	
Inventories	19,878,478	
Prepaid expenses	1,798,773	
Deferred income taxes	485,770	
	-----	-----
Total current assets	39,887,687	
Property and equipment, net	6,300,022	
Deferred income taxes	1,232,031	
Intangible assets, net	14,709,988	
Notes receivable	28,586	
Other assets	212,205	
	-----	-----
Total assets	\$ 62,370,519	\$
	=====	=====
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Lines of credit	\$ 16,763,214	\$
Current maturities of long term debt	2,053,179	
Acquisition notes payable	767,500	
Accounts payable	8,208,136	
Accrued liabilities	2,385,755	
	-----	-----
Total current liabilities	30,177,784	
Notes payable	3,118,629	
Acquisition notes payable	1,000,000	
Subordinated long term debt	3,944,792	
Deferred income taxes	504,740	
Warrant Put Liability	575,000	
Commitments and Contingencies		
SHAREHOLDERS' EQUITY		
Preferred stock, 2,500,000 shares authorized, \$1.00 par value; 336,660 shares issued and outstanding at February 28, 2002 and February 28, 2001	336,660	
Common stock; 20,000,000 shares authorized, \$.001 par value; 3,381,190 shares issued and outstanding at February 28, 2002 and February 28, 2001	3,381	
Additional paid-in capital	9,068,703	

Edgar Filing: QEP CO INC - Form 10-K

Retained earnings	15,842,783
Cost of stock held in treasury	(390,642)
Accumulated other comprehensive income	(1,811,311)
	-----
	23,049,574
	-----
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$ 62,370,519
	=====

The accompanying notes are an integral part of these statements

F-3

Q.E.P. CO., INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF INCOME

	Year ended		
	February 28, 2002	February 28, 2001	February 29, 2000
	-----	-----	-----
Net sales	\$109,674,723	\$113,003,087	\$113,571,475
Cost of goods sold	72,602,550	76,939,755	79,036,635
	-----	-----	-----
Gross profit	37,072,173	36,063,332	34,534,840
	-----	-----	-----
Costs and expenses:			
Shipping	9,588,832	9,801,247	8,987,252
General and administrative	9,740,543	9,650,354	9,393,494
Selling and marketing	11,894,600	11,616,403	9,494,325
Restructuring charge	---	637,462	---
Other (income) expense, net	(217,133)	(93,527)	(13,458)
	-----	-----	-----
	31,006,842	31,611,939	27,861,613
	-----	-----	-----
Operating income	6,065,331	4,451,393	6,673,227
Interest income	9,897	175,389	133,287
Interest expense	(2,567,455)	(2,306,584)	(1,833,675)
	-----	-----	-----
Income before provision for income taxes and extraordinary item	3,507,773	2,320,198	4,972,839
Provision for income taxes	1,404,795	887,493	1,951,447
	-----	-----	-----
Net income before extraordinary item	2,102,978	1,432,705	3,021,392
Extraordinary item, gain on early extinguishment of debt	--	--	181,559
	-----	-----	-----
Net income	\$ 2,102,978	\$ 1,432,705	\$ 3,202,951
	=====	=====	=====

Edgar Filing: QEP CO INC - Form 10-K

Basic and diluted earnings per common share:

Income before extraordinary item	\$	0.62	\$	0.42	\$	0.90
Extraordinary item		---		---		.05
Net income	\$	0.62	\$	0.42	\$	0.95

The accompanying notes are an integral part of these statements

F-4

Q.E.P. CO. INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

	Preferred Stock		Common Stock		Paid-in capital
	Shares	Amount	Shares	Amount	
Balance at February 28, 1999	336,660	\$336,660	2,654,894	\$2,655	\$8,746,876
Net income					
Other comprehensive income:					
Foreign currency translation adjustment					
Exercise of stock options			30,000	30	199,185
Dividends					
Balance at February 29, 2000	336,660	\$336,660	2,684,894	\$2,685	\$8,946,061
Net income					
Other comprehensive income:					
Foreign currency translation adjustment					
Purchase of Treasury Stock					
Stock Dividend			673,796	673	
Exercise of stock options			22,500	23	136,026
Dividends					
Balance at February 28, 2001	336,660	\$336,660	3,381,190	\$3,381	\$9,082,087
Net income					
Other comprehensive income:					
Foreign currency translation adjustment					
Purchase of Treasury Stock					
Purchase of Warrants					(13,384)
Dividends					
Balance at February 28, 2002	336,660	\$336,660	3,381,190	\$3,381	\$9,068,703

Edgar Filing: QEP CO INC - Form 10-K

	Treasury stock	Other Comprehensive Income
	-----	-----
Balance at February 28, 1999	(57,900)	
Net income		3,202,951
Other comprehensive income:		
Foreign currency translation adjustment		(105,875)
Exercise of stock options		
Dividends		
	-----	-----
Balance at February 29, 2000	(57,900)	\$3,097,076
		=====
Net income		1,432,705
Other comprehensive income:		
Foreign currency translation adjustment		(334,058)
Purchase of Treasury Stock	(293,093)	
Stock Dividend		
Exercise of stock options		
Dividends		
	-----	-----
Balance at February 28, 2001	(\$350,993)	\$1,098,647
		=====
Net income		2,102,978
Other comprehensive income:		
Foreign currency translation adjustment		(1,094,378)
Purchase of Treasury Stock	(39,649)	
Purchase of Warrants		
Dividends		
	-----	-----
Balance at February 28, 2002	(\$390,642)	\$1,008,600
	=====	=====

The accompanying notes are an integral part of these statements

F-5

Q.E.P. CO., INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended	
	-----	-----
	February 28, 2002	February 28, 2001
	----	----

## Edgar Filing: QEP CO INC - Form 10-K

Cash flows from operating activities:		
Net income	\$ 2,102,978	\$ 1,432,705
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,524,090	1,356,927
Amortization of costs in excess of assets acquired	471,126	457,081
Amortization of discount on long term debt	18,080	213,092
Bad debt expense	94,909	127,119
Loss on sale of property and equipment	---	26,023
Deferred income taxes	210,520	147,207
Gain on early extinguishments of debt	---	---
Changes in assets and liabilities, net of acquisitions:		
Accounts receivable	(172,907)	(1,446,741)
Inventories	(292,666)	(2,230,277)
Prepaid expenses	(224,234)	(609,635)
Other assets	(218,487)	(368,620)
Accounts payable and accrued liabilities	(899,185)	1,262,131
	-----	-----
Net cash provided by operating activities	2,614,224	367,012
	-----	-----
Cash flows from investing activities		
Capital expenditures	(576,907)	(2,018,793)
Purchase of trademarks and licenses	---	(200,000)
Acquisitions, net of cash acquired	---	(1,116,517)
Proceeds from sale of property & equipment	---	150,000
	-----	-----
Net cash used in investing activities	(576,907)	(3,185,310)
	-----	-----
Cash flows from financing activities:		
Net borrowings under lines of credit	1,278,592	5,069,876
Borrowings of long term debt	6,000,000	---
Repayments of long term debt	(7,999,681)	(1,384,925)
Repayments of acquisition debt	(785,000)	(2,462,843)
Purchase of subordinated debt	---	---
Purchase of treasury stock	(39,649)	(293,093)
Proceeds from exercise of stock options	---	136,047
Payments on notes receivable	5,300	1,667,818
Purchase of common stock warrants	(13,384)	---
Dividends	(18,742)	(11,770)
	-----	-----
Net cash (used in) provided by financing activities	(1,572,564)	2,721,110
	-----	-----
Cumulative currency translation adjustment	(427,250)	(334,058)
	-----	-----
Net increase (decrease) in cash	37,503	(431,246)
	-----	-----
Cash and cash equivalents at beginning of year	397,817	829,063
	-----	-----
Cash and cash equivalents at end of year	\$ 435,320	\$ 397,817
	=====	=====

The accompanying notes are an integral part of these statements.

# Edgar Filing: QEP CO INC - Form 10-K

## Q.E.P. CO., INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### NOTE A - DESCRIPTION OF BUSINESS

Q.E.P. Co., Inc. is a leading manufacturer, marketer and distributor of a broad line of specialty tools and flooring related products for the home improvement market. Under brand names including Q.E.P.(TM), O'TOOL(TM) and ROBERTS(TM) the Company markets specialty tools and flooring related products used primarily for the surface preparation and installation of ceramic tile, carpet and marble. During fiscal 2002 the Company reduced the amount of items it sells through its subsidiaries. Total products marketed by Q.E.P. and subsidiaries now approximate 3,000. The Company sells its products to large home improvement retail centers, as well as traditional distribution outlets in 50 states and more than 49 countries worldwide.

### NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### 1. Principles of Consolidation

The consolidated financial statements include the accounts of Q.E.P. Co., Inc. and its wholly owned subsidiaries, after eliminating all significant inter-company accounts and transactions.

#### 2. Warrants

In connection with an acquisition, the Company has issued a total of 250,000 warrants to purchase common stock at \$8.00 per share. These warrants expire on October 21, 2002. In connection with the refinancing of certain subordinated debt (see Note K), the Company issued 325,000 warrants at \$3.63, which will to expire on April 4, 2011. These warrants can be put to the Company after the fifth year based on certain criteria. Further, the Company may call these warrants, based on certain criteria, after the sixth year.

#### 3. Cash Equivalents

The Company considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents.

#### 4. Inventories

Inventories are stated at the lower of standard cost or market.

#### 5. Property and Equipment

Property and equipment are stated at cost. Depreciation is provided by straight-line methods in amounts sufficient to relate the cost of depreciable assets to operations over their estimated service lives. Leasehold improvements are amortized over their expected useful life or the life of the respective lease, whichever is shorter.

The following are the estimated lives of the Company's property and equipment:

Machinery and warehouse equipment	5 to 10 years
Furniture and equipment	5 to 10 years
Capital leases	3 to 5 years
Building	30 to 33 years
Leasehold improvements	5 to 15 years

## Edgar Filing: QEP CO INC - Form 10-K

### Q.E.P. CO., INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Maintenance and repairs are charged to expense, and significant renewals and betterments are capitalized. When property is sold or otherwise disposed of, the cost and related depreciation are removed from the accounts, and any resulting gain or loss is reflected in operations for the period.

#### 6. Intangible Assets

Intangible assets (predominately goodwill which represents the cost in excess of net assets of businesses acquired) are recorded and amortized over periods ranging from five to thirty five years using the straight-line method. The Company will adopt FASB No. 142 "Goodwill and Other Intangibles" beginning March 1, 2002; consequently, amortization of goodwill will cease (See Note U).

#### 7. Impairment of Long-Lived Assets and Long-Lived Assets To Be Disposed Of

The Company evaluates its long-lived assets and certain intangibles for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets or intangibles may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such an asset is considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the asset exceeds the fair value of the assets (See Note U). Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

#### 8. Income Taxes

Deferred income taxes are recorded to reflect the tax consequences on future years of differences between the tax basis of assets and liabilities and their financial reporting amounts each year-end.

#### 9. Leases

Leases which meet certain criteria are classified as capital leases. For such leases, assets and obligations are recorded initially at the fair market values of the leased assets. The capitalized leases are amortized using the straight-line method over the assets' estimated economic lives. Interest expense relating to the lease liabilities is recorded to affect a constant rate of interest over the terms of the obligations. Leases not meeting capitalization criteria are classified as operating leases and related rentals are charged to expense as incurred.

#### 10. Stock-Based Compensation

The Company grants stock options for a fixed number of shares to employees and directors with an exercise price equal to at least 85% of the fair market value of the shares at the date of grant. The Company has adopted the disclosure-only provision of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation," which permits the Company to account for stock option grants in accordance with APB Opinion No. 25, "Accounting for Stock Issued to Employees." Under APB 25, compensation expense is recorded when the exercise price of the Company's employee stock option is less than the market price of the underlying stock at the date of grant.



Q.E.P. CO., INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

11. Earnings Per Share

Basic earnings per share is computed based on weighted average shares outstanding during the period. Diluted earnings per share is computed using the weighted average number of common and dilutive common stock equivalent shares outstanding during the period. Dilutive common stock equivalent shares consist of stock options and warrant common stock equivalent shares which are not utilized when the effect is antidilutive.

12. Comprehensive Income

The Company records comprehensive income in accordance with SFAS No. 130, "Reporting Comprehensive Income." SFAS 130 requires foreign currency translation adjustments to be included in other comprehensive income.

The components of comprehensive income and the effect on earnings for the year ended February 28, 2002 are detailed in the Company's accompanying Consolidated Statement of Shareholders' Equity.

13. Post Employment Benefits

The Company has a policy which provides service benefits to its salaried employees. The Company records a liability for post employment benefits in accordance with SFAS No. 112, "Employers Accounting for Post Employment Benefits". Since the Company cannot reasonably estimate post employment benefits, including severance benefits, on an ongoing basis, these costs are recorded only when the probability of payment and the amount of such payment can be reasonably determined.

14. Derivative Instruments and Hedging Activities

In June 1998, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 133, "Accounting for Derivative Instruments and Hedging Activities." SFAS No. 133 establishes accounting and reporting standards requiring that every derivative instrument (including certain derivative instruments embedded in other contracts) be recorded in the balance sheet as either an asset or liability at its fair value. The Statement requires that changes in the derivative's fair value be recognized currently in earnings unless specific hedge accounting criteria are met. In June 2000, the FASB issued SFAS No. 138, "Accounting for Certain Derivative Instruments and Certain Hedge Activities - an Amendment of FASB Statement No. 133." See Note K(B)

15. Interest Rate Swap

The interest rate swap agreement, (the "Swap") involves the exchange of fixed and floating interest rate payment obligations over various terms without the exchange of the underlying notional principal amount. The differential to be paid or received is recognized as an adjustment to interest expense in the period incurred. The swap agreement expired in December, 2001.

## Edgar Filing: QEP CO INC - Form 10-K

### Q.E.P. CO., INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

#### 16. Fair Value of Financial Instruments

The following methods and assumptions were used in estimating the indicated fair values of financial instruments:

**Cash and cash equivalents:** The carrying amount approximates fair value due to the short maturity of these instruments.

**Short term debt:** The carrying amount approximates fair value due to the short maturity of these instruments.

**Long term debt:** The fair value of the Company's borrowings approximates the carrying value based on current rates offered to the Company for similar debt.

**Warrant put liability:** The carrying amount approximates fair value based on the market value of the Company's stock or contract value as defined.

#### 17. Foreign Currencies

The financial statements of subsidiaries outside the United States are generally measured using the local currency as the functional currency. Assets and liabilities recorded in foreign currencies on the books of foreign subsidiaries are translated at the exchange rate on the balance sheet date. Translation adjustments resulting from this process are charged or credited to equity. Revenues, costs, and expenses are translated at average rates of exchange prevailing during the year. Gains and losses on foreign currency transactions are included in operating expenses.

#### 18. Revenue Recognition

Sales are recognized when merchandise is shipped and such revenue is recorded net of estimated sales returns, discounts and allowances. The Company establishes reserves for returns and allowances based on current and historical information and trends. Sales and accounts receivable have been reduced by such amounts.

#### 19. Shipping and Handling Costs

Shipping and handling costs are classified as a separate operational expense on the accompanying Consolidated Statements of Income.

#### 20. Advertising Cost

Advertising costs are expensed in the period incurred except those costs which result in tangible assets, such as catalogs, which are treated as prepaid supplies and charged to operations as consumed.

#### 21. Research and Development

Research and development costs are charged to expense in the period incurred.

#### 22. Use of Estimates

In preparing financial statements in conformity with accounting principles generally accepted in the United States, management is required to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities

## Edgar Filing: QEP CO INC - Form 10-K

at the date of the financial statements and revenues and expenses during the reporting period. Actual results could differ from those estimates.

F-10

### Q.E.P. CO., INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The Company estimates an allowance for doubtful accounts based on the creditworthiness of its customers as well as general economic conditions. Management has used reasonable assumptions in deriving these estimates; however, actual results could differ from these estimates. Consequently, an adverse change in those conditions could affect the Company's estimate.

23. Certain amounts in the fiscal year 2001 presentation have been reclassified to conform with the fiscal year 2002 presentation.

#### NOTE C - ACQUISITIONS

Acquisitions are accounted for as purchases and, accordingly, have been included in the Company's consolidated results of operations since the acquisition date. The purchase price is allocated based on the estimated fair values of assets acquired and liabilities assumed. Purchase price allocations are subject to refinement until all pertinent information regarding the acquisitions is obtained.

During fiscal 2001, the Company made three strategic acquisitions. The purchase price for these acquisitions, most of which were domestic companies, was approximately \$2,800,000. The excess of aggregate purchase price over the fair market value of net assets acquired of approximately \$500,000 was being amortized on a straight line basis over 20 years.

During fiscal 2000, the Company made six strategic acquisitions. The purchase price for all of these acquisitions, the majority of which were international companies, was approximately \$8,750,000. The excess of aggregate purchase price over the fair market value of net assets acquired of approximately \$3,500,000 was being amortized on a straight line basis over 20 years.

Effective March 1, 2002 the Company will stop amortizing goodwill. See Note U.

The unaudited pro forma consolidation of the acquisitions occurring in fiscal 2001 showing the results of operations assuming the above purchases occurred on March 1, 2000 are not material and are not included herein.

#### NOTE D - EARNINGS PER SHARE

Basic earnings per share is computed by dividing net income, after deducting preferred stock dividends accumulated during the period, by the weighted average number of shares of common stock outstanding during each period. Diluted earnings per share is computed by dividing net income, after deducting preferred stock dividends accumulated during the period, by the weighted average number of shares of common and dilutive common stock equivalent shares outstanding during each period. Diluted common stock equivalent shares consist of stock options and warrant common stock equivalent shares which are not used when the effect is antidilutive. For the three years ended February 28, 2002, the weighted average number of basic shares of common stock outstanding amounted to 3,381,190 in 2002, 3,343,868 in 2001 and 3,345,701 in 2000. For the three years ended February 28, 2002 the weighted average number of diluted shares of common stock outstanding amounted to 3,390,028 in 2002, 3,368,818 in 2001 and 3,364,668 in 2000.

## Edgar Filing: QEP CO INC - Form 10-K

### NOTE E - EQUITY

On June 6, 2000, the Board of Directors declared a five for four stock split of the Company's common stock, affected in the form of a stock dividend which was paid on August 1, 2000. As a result of this action, approximately 673,000 shares were issued to shareholders of record on July 17, 2000. Par value of the common stock remained at \$0.001 per share and, accordingly, \$673 was transferred from retained earnings to common stock.

F-11

### Q.E.P. CO., INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the years ended February 28, 2001 and 2000, the effect on earnings per share was a reduction of \$0.11 and \$0.24, respectively. All references to the number of common shares and per common share amounts have been restated to give retroactive effect to the stock split for all periods presented.

### NOTE F - LICENSE AGREEMENT

Effective May 15, 2000, the Company entered into an agreement to license the distribution rights of its tackless carpet strip product to U.S. flooring products distributors. Under the terms of the agreement, the Company will receive a total of \$2,750,000 at a predetermined rate based on cartons of tack strip sold by the licensee. The Company is guaranteed to receive a minimum of \$400,000 per year. In addition, the Company will retain the right and will continue to sell tackless carpet strip to the home center and international markets. For the two years ended February 28, 2001, the Company sold approximately \$2,957,000 and \$14,114,000, respectively. There were no sales of this product to these distributors for the fiscal year ended February 28, 2002.

### NOTE G - SEGMENT INFORMATION

The Company operates in one business segment -- flooring-related products because of the similarity of economic conditions, products, production processes, customers and expected long-term performance. The Company manufactures and distributes flooring-related products to the residential new construction, do-it-yourself and professional remodeling and renovation markets and home centers.

Information attributable to the Company's geographic areas is as follows:

	United States of America -----	Canada/ Latin America -----	New Zealand/ Australia -----	Europe -----	Inter-comp Eliminatio -----
2002 ----					
Sales	\$87,197,283	\$10,866,127	\$3,761,605	\$7,849,708	\$ -
Transfers between areas	2,534,283	3,001,319	---	---	(5,535,600)
Total Sales	\$89,731,566	\$13,867,446	\$3,761,605	\$7,849,708	(5,535,600)
Long-lived Assets	\$41,431,650	\$ 2,325,823	\$ 584,501	\$ 823,820	\$ (23,943,500)

Edgar Filing: QEP CO INC - Form 10-K

2001					
----					
Sales	\$87,261,192	\$12,846,153	\$4,112,636	\$8,783,106	\$ -
Transfers between areas	1,300,127	---	---	4,102	(1,304,2
Total Sales	\$88,561,319	\$12,846,153	\$4,112,636	\$8,787,208	\$ (1,304,2
Long-lived Assets	\$41,136,460	\$ 2,696,467	\$ 785,885	\$ 950,062	\$ (22,879,1
=====					
2000					
----					
Sales	\$89,366,768	\$13,104,460	\$2,192,192	\$8,908,055	\$ -
Transfers between areas	947,927	---	---	---	(947,9
Total Sales	\$90,314,695	\$13,104,460	\$2,192,192	\$8,908,055	\$ (947,9
Long-lived Assets	\$36,628,219	\$ 1,632,748	\$ 291,024	\$1,172,581	\$ (21,324,9
=====					

F-12

Q.E.P. CO., INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE H - NOTE RECEIVABLE

Concurrent with the acquisition of Roberts, the Company sold certain production equipment (at their stated value) to an unrelated third party for a note in the amount of \$3,750,000. Such note was collateralized by the equipment. At the time of issuance, the note was recorded at its net present value of \$3,250,000 utilizing its effective interest rate of approximately 9% and was payable through a reduction in purchase price of goods sold to the Company under a supply agreement. As a result of the license agreement, with the same third party (see Note F), this note was paid in its entirety in fiscal 2001.

NOTE I - INVENTORIES

Inventories consisted of the following:

	February 28, 2002	February 28, 2001
	----	----
Raw materials and work-in-process	\$ 3,837,402	\$ 4,957,226
Finished goods	16,041,076	15,175,359
	-----	-----
	\$19,878,478	\$20,132,585
	=====	=====

NOTE J - PROPERTY AND EQUIPMENT

February 28,  
2002  
----

Feb

Property and equipment consisted of the following:

Edgar Filing: QEP CO INC - Form 10-K

Machinery and warehouse equipment	\$ 4,259,073	\$ 4
Office furniture, equipment and computer equipment	3,556,645	3
Building and leasehold improvements	2,055,511	2
	-----	-----
	9,871,229	9
Less accumulated depreciation and amortization	(3,571,207)	(2)
	-----	-----
	\$ 6,300,022	\$ 7
	=====	=====

NOTE K - DEBT

Total debt consists of the following:

	February 28, 2002	Feb
	----	
(A) Payable to banks under revolving credit facilities	\$16,763,214	\$15
(B) Subordinated debt	4,500,000	4
(C) Payable to a bank under term loan credit facilities	4,080,357	5
(D) Payable to a bank under a mortgage agreement	556,559	
(E) Acquisition notes payable	1,767,500	2
Other debt, including capital leases	534,892	
	-----	-----
	28,202,522	29
Less current installments	19,583,893	18
	-----	-----
	8,618,629	11
Less unamortized discount	(555,208)	
	-----	-----
Long Term	\$ 8,063,421	\$11
	=====	=====

F-13

Q.E.P. CO., INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(A) The Company has a revolving credit and term loan facility agreement with a United States financial institution. This agreement, which was amended on April 5, 2001, provides for borrowings of up to \$18,000,000 (subsequent to February 28, 2002 this amount was increased to \$20,000,000 through June 3, 2002) against a fixed percentage of eligible accounts receivable and inventory. Interest is payable based on a sliding scale depending on the Company's senior debt to EBITDA ranging from LIBOR plus 1.75% to LIBOR plus 2.5%. The facility terminates in July 2003 and is collateralized by substantially all of the Company's assets. Under the terms of the credit agreement, the Company is required to maintain certain financial ratios and conditions. The credit agreement also prohibits the Company from incurring certain additional indebtedness, limits certain investments, advances or loans and restricts substantial asset sales and capital expenditures. The terms of the Company's credit facility also prohibits the payment of dividends, except with the lender's consent. Interest was charged based on a sliding scale. As of February 28, 2002 interest was at LIBOR (1.85% at February 28, 2002) plus 2.00%. At February 28, 2002 the Company had \$1,113,000 available for future borrowings under the credit facility, net

## Edgar Filing: QEP CO INC - Form 10-K

of approximately \$444,000 in outstanding letters of credit. The Company's Chilean subsidiary has a revolving credit facility with a financial institution, which permits borrowings of up to \$100,000 with interest at 18% per year. The facility is secured by a standby letter of credit given by the Company. This facility expires on May 31, 2002 and is expected to be renewed at a reduced amount. At February 28, 2002, the Chilean subsidiary had approximately \$54,000 available for future borrowings under the credit facility. The Company's Australian subsidiary also has an overdraft facility, which allows it to borrow against a certain percentage of inventory and receivables. At February 28, 2002 the maximum permitted borrowing was approximately \$361,000 and approximately \$86,000 was available for future borrowings.

- (B) In connection with the acquisition of Roberts, the Company issued \$7,500,000 of subordinated debentures bearing an interest rate of 8%. During fiscal 2000, the Company repurchased approximately \$1,229,000 of such debentures at a discount resulting in an extraordinary gain from early extinguishments of debt of approximately \$181,000. The remaining bonds matured in April 2001 and were paid. On April 5, 2001, the Company entered into a new \$4,500,000 subordinated credit facility with HillStreet Fund LP. This facility bears an interest rate of 15% and matures on April 5, 2007. Beginning July 1, 2005, the Company is required to make equal quarterly principal payments of \$562,500 through April 5, 2007. The agreement also provides for an additional 3% interest if the Company does not meet certain financial covenants. In addition, the Company issued 325,000 10-year warrants at \$3.63. These warrants can be put to the Company on and after April 5, 2006 based on criteria set forth in the warrant agreement. In addition, the Company may call these warrants on and after April 5, 2007 based on the same criteria. The Company has recorded a liability for these put warrants based on an independent appraisal. Changes to the fair value of the put warrants will be recognized in earnings of the Company in accordance with SFAS No. 133 "Accounting for Derivative Instruments and Hedging Activities." The resulting discount of the subordinated credit facility will be amortized over the life of the debt.
- (C) The original term loan is payable in equal quarterly installments over a seven year period. The loan is collateralized by substantially all of the assets of the Company. The interest rate varies based on conditions, as defined in the agreement and was approximately 3.90% at February 28, 2002. The balance of the term loan at February 28, 2002 and February 28, 2001 was \$3,142,857 and \$4,285,713, respectively. The Company obtained an additional term loan ("2001 Term Loan") from its primary lending institution, the proceeds of which were utilized repay its subordinated debt which matured in April 2001. This loan in the amount of \$1,500,000 is payable in equal quarterly installments, which commenced on July 1, 2001 and will end on April 1, 2003. The interest rate for this loan is LIBOR plus 2.75%. At February 28, 2002, the balance of the 2001 Term Loan was \$937,500.

F-14

### Q.E.P. CO., INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

- (D) During fiscal 2001, the Company purchased the land and building from its then existing landlord where it operates in Bramalea, Ontario, Canada. The cost of the facility was approximately \$988,000 of which the Company obtained a mortgage in the approximate amount of \$670,000 from a Canadian financial institution. This facility is payable over 10 years at an interest rate to be set annually (6.1% as of February 28, 2002) and is collateralized by the land and building. The facility also requires the

## Edgar Filing: QEP CO INC - Form 10-K

Company to continue remediation efforts on the property as approved by the Canadian Ministry of Environment. See Note M.

- (E) In connection with the acquisitions of certain newly acquired entities, the Company issued five notes to the respective sellers. During fiscal 2001, the Company issued a note for \$1,600,000, payable in equal quarterly payments over a five-year period. The note bears an interest rate of 8%. As of February 28, 2002, the Company is obligated for two additional notes for prior year acquisitions. One, having an original balance of \$900,000, is payable in equal annual installments over a three year period with interest at the Company's prevailing borrowing rate. The balance at February 28, 2002, is \$300,000. The other note has a balance of \$340,000 and is payable in installments of \$20,000 per month for seven months and \$200,000 in December 2003.

On December 23, 2000, the Company entered into an interest rate swap agreement with its primary lender. The interest rate swap agreement hedges the Company's exposure on certain floating rate obligations in the aggregate principal amount of \$10,000,000. The purpose of the interest rate swap is to convert the Company's floating rate interest obligations to obligations having a fixed rate of 6.0% per annum for a one-year period. Prior to this interest rate swap, the Company had a similar arrangement with the same institution that matured in December 2000. The fixing of the interest rates reduces in part the Company's exposure to the uncertainty of floating interest rates. The differential paid or received by the Company on the interest rate swap agreement is recognized as an adjustment to interest expense in the period incurred. For the year ended February 28, 2002, the Company increased interest expense by approximately \$162,000 as a result of the interest rate swap agreements that were in place during that period. The interest rate swap agreement expired in December 2001 and was not renewed.

Interest paid for all debt was approximately \$2,189,600, \$2,025,100 and \$1,486,000 in fiscal 2002, 2001 and 2000 respectively.

The aggregate maturities of all debt, excluding the put liability, maturing during each of the next five years as of February 28, 2002 is as follows:

2003	\$19,583,893
2004	2,268,431
2005	1,246,633
2006	1,353,298
2007	2,293,500
Thereafter	901,559
	-----
Total	\$27,647,314
	=====
Current	\$19,583,893
Long Term	8,063,421
	-----
TOTAL	\$27,647,314
	=====

F-15

Q.E.P. CO., INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE L - ACCRUED LIABILITIES



## Edgar Filing: QEP CO INC - Form 10-K

Accrued liabilities consisted of the following:

February 28, 2002

Accrued payroll and employee benefits	\$ 707,595
Accrued volume and advertising discount	885,031
Accrued interest	290,709
Accrued liabilities - other	502,420
	-----
	\$2,385,755
	=====

### NOTE M - COMMITMENTS AND CONTINGENCIES

The Company provides accruals for all direct costs associated with the estimated resolution of contingencies at the earliest date at which it is deemed probable that a liability has been incurred and the amount of such liability can be reasonably estimated.

The Company is involved in litigation from time to time in the course of its business. In the opinion of management, no material legal proceedings are pending to which the Company or any of its property is subject.

#### 1. Future Minimum Obligations

The Company conducts its operations from various leased facilities. Future minimum payments under non-cancelable operating leases consist of the following in fiscal years ending after February 28, 2002:

2003		\$1,783,104
2004		998,411
2005		560,967
2006		408,665
2007		741,790
		-----
Total		\$4,492,937
		=====

Total rent expense under non-cancelable operating leases approximated \$2,201,000, \$2,045,000 and \$1,891,000 in fiscal 2002, 2001 and 2000, respectively.

#### 2. Roberts Consolidated Industries, Inc.

The Company is subject to federal, state and local laws, regulations and ordinances governing activities or operations that may have adverse environmental effects, such as discharges to air and water, handling and disposal practices for solid, special and hazardous wastes, and imposing liability for the cost of cleaning up, and certain damages resulting from sites of past spills, disposal or other releases of hazardous substances (together, "Environmental Laws"). Sanctions which may be imposed for violation of Environmental Laws include the payment or reimbursement of investigative and clean up costs, administrative penalties and, in certain cases, prosecution under environmental criminal statutes. The Company's manufacturing facilities are

F-16

## Edgar Filing: QEP CO INC - Form 10-K

subject to environmental regulation by, among other agencies, the Environmental Protection Agency, the Occupational Safety and Health Administration, and various state authorities in the states where such facilities are located. The activities of the Company, including its manufacturing operations at its leased facilities, are subject to the requirements of Environmental Laws. The Company believes that the cost of compliance with Environmental Laws to date has not been material to the Company. The Company is not currently aware of any situations requiring remedial or other action, which would involve a material expense to the Company, or expose the Company to material liability under Environmental Laws. As the operations of the Company involve the storage, handling, discharge and disposal of substances which are subject to regulation under Environmental Laws, there can be no assurance that the Company will not incur any material liability under Environmental Laws in the future or will not be required to expend funds in order to effect compliance with applicable Environmental Laws.

The Company completed testing at its facility in Bramalea, Ontario, Canada for leakage of hazardous materials and, as a result, in fiscal 1999 the Company prepared a plan to remediate the contamination over a period of years and this plan was subsequently approved by the Canadian Ministry of Environment (MOE). The Company recorded a reserve for potential environmental liability on the closing date of the Roberts acquisition of approximately \$325,000 and this amount was increased during fiscal 1999 by \$275,000 to \$600,000 based on an estimate for the cost of remediation. To date, the Company has spent approximately \$480,000 and anticipates spending additional amounts on ongoing monitoring of wells and other environmental activity at the approximate rate of between \$5,000 and \$25,000 per year for the next few years.

### NOTE N - PENSION AND RETIREMENT PLANS

#### Profit Sharing and 401(k) Plan

The Company and its subsidiaries offers a 401(k) benefit plan which provides for voluntary contributions by employees subject to a maximum annual contribution. The Company may, at the discretion of the Board of Directors, make contributions to the plan. For the three years ended February 28, 2002, the Company contributed approximately \$62,000, \$70,000 and, \$68,000, respectively.

Subsequent to the acquisition of Roberts, the Company terminated the Roberts Salaried Employees Defined Benefit Pension Plan. As of May 31, 1998, the projected benefit obligation was estimated to be \$2,452,000 and the plan assets were approximately \$2,947,000. The Company initially recorded an asset in excess of projected benefit of approximately \$700,000. During fiscal 1999, the Company had an actuarial valuation prepared which adjusted this amount and goodwill by approximately \$226,000. During fiscal 2001, the Plan distributed its remaining assets to its participants under a new defined contribution plan and, with the approval of regulatory authorities, the remainder reverted to the Company. This new defined contribution plan expects to distribute its assets upon the retirement of all of its participants. No pension expense was recorded in each of the three years ended February 28, 2002.

F-17

## Q.E.P. CO., INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### NOTE O - INCOME TAXES

## Edgar Filing: QEP CO INC - Form 10-K

Income (loss) before provision for income taxes and extraordinary item consisted of the following:

	Year Ended February 28 or 29,		
	2002	2001	2000
	-----	-----	-----
United States	\$4,192,810	\$ 3,335,414	\$4,607,810
Foreign	(685,037)	(1,015,216)	365,000
	-----	-----	-----
Total	\$3,507,773	\$ 2,320,198	\$4,972,810
	=====	=====	=====

The components of the provision for income taxes are as follows:

	Year Ended February 28 or 29,		
	2002	2001	2000
	-----	-----	-----
Current:			
Federal	\$1,089,993	\$ 623,400	\$1,529,000
State	51,848	99,296	261,000
Foreign	52,436	17,590	154,000
	-----	-----	-----
	1,194,277	740,286	1,944,000
	-----	-----	-----
Deferred:			
Federal	447,443	437,943	143,000
State	35,357	44,052	(11,000)
Foreign	(272,282)	(334,788)	(127,000)
	-----	-----	-----
	210,518	147,207	5,000
	-----	-----	-----
Total income tax provision	\$1,404,795	\$ 887,493	\$1,951,000
	=====	=====	=====

The tax effects of temporary differences which give rise to deferred tax assets are as follows:

	February 28, 2002	February 28,
	-----	-----
Provision for doubtful accounts	\$ 126,383	\$ 45,660
Accrued expenses	218,274	230,230
Fixed assets	(468,534)	(177,620)
Inventory	141,113	149,050
Net operating loss - U.S.	292,928	320,670
Foreign credit carryforwards and net operating loss	939,103	666,820
Other	(36,206)	188,760
	-----	-----

Edgar Filing: QEP CO INC - Form 10-K

Net deferred tax asset

\$1,213,061  
=====

\$1,423,58  
=====

The Company has approximately \$794,000 in net operating loss carry forwards which expire in the years 2011 through 2018, all of which relates to the Company's Fiscal 2000 acquisitions. The net operating loss carry forward is subject to separate IRC Section 382 Limitation. The Section 382 limitation limits the Company's utilization of its net operating losses to an annual amount after an ownership change.

The Company has net operating losses in various foreign countries of approximately \$2,760,000. The Company has recorded a deferred tax asset based on its estimate of the recoverability prior to their expiration. If the Company determines in future years that net operating losses will not be realized, then the asset will be adjusted accordingly. Further, \$200,000 of these losses expire in 2006 and the remainder have no limitation on their expiration.

F-18

Q.E.P. CO., INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following is a reconciliation of the statutory federal income tax rate to the effective rate reported in the financial statements:

	Year Ended February 28 or 29,			
	2002		2001	
	Amount	%	Amount	%
Provision for federal income taxes				
at the statutory rate	\$1,192,643	34.0	\$788,867	34.0
State and local income taxes -				
net of federal income tax benefit	101,725	2.9	79,351	3.4
Other	110,427	3.1	19,275	0.8
Actual provision	\$1,404,795	40.0	\$887,493	38.2

Cash paid for income taxes was approximately \$984,000, \$1,504,000 and \$2,031,000 fiscal 2002, 2001 and 2000, respectively.

NOTE Q - SIGNIFICANT CUSTOMER AND VENDOR INFORMATION

1. Significant Customer Information

The Company sells products to a large number of customers which are primarily in the United States. The Company performs ongoing credit evaluations of its customers' financial condition and, generally, requires no collateral from its customers. The Company's customer base includes a high concentration of home center chains with two such customers accounting for a total of 59%, 50% and 39% of sales in fiscal 2002, 2001 and 2000, respectively. One customer represented 46%, 41% and 35% and the other customer represented 13%, 9% and 4% of sales in fiscal 2002, 2001 and 2000, respectively. These same two customers represented 35% and 10% of accounts

## Edgar Filing: QEP CO INC - Form 10-K

receivable at February 28, 2002 and 29% and 13% of accounts receivable at February 28, 2001. Although the Company is directly affected by the well-being of the home center industry, management does not believe significant credit risk exists at February 28, 2002.

### 2. Significant Vendor Information

The Company purchased approximately 28% and 12%, 19% and 15% and 19% and 10% of purchases for the fiscal years ended 2002, 2001 and 2000 respectively through two vendors.

### NOTE R - SHAREHOLDERS' EQUITY

The Company is authorized to issue a maximum of 2,500,000 shares of \$1 preferred stock.

#### Series A

500,000 of the Company's 2,500,000 authorized shares of preferred stock, \$1 par value per share, are designated as Series A Preferred Stock. The holders of each share of Series A Preferred Stock shall be entitled to receive, before any dividends shall be declared or paid on or set aside for the Company's common stock, out of funds legally available for that purpose, cumulative dividends in cash at the rate of \$.035 per share per annum through September 30, 2000, payable in semiannual installments, accruing from the date of issuance of the shares. Commencing October 1, 2000, the rate of dividends will equal the prime interest rate on the first day of the month in which the dividends are payable, less 1-1/4%.

F-19

### Q.E.P. CO., INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The Company may redeem any or all of the shares of Series A Preferred Stock outstanding at a price per share of \$1.07 plus an amount equal to any accrued but unpaid dividends thereon during the first year following the issuance of such shares and such price shall be reduced by one percent (1%) each year thereafter until \$1.00 per share is reached. The Series A Preferred Stock has no voting rights. During fiscal 1995, the Company issued 425,547 shares of Series A preferred stock in connection with a business acquisition. In fiscal 1997, 106,387 of these shares were converted to 3,129 shares of common stock. At February 28, 2002 and February 28, 2001, there were 319,160 shares of Series A Preferred Stock issued and outstanding. There were \$18,142 and \$11,170 of dividends declared and paid during the fiscal years 2002 and 2001.

#### Series B

1,000,000 of the Company's 2,500,000 authorized shares of preferred stock, \$1 par value per share, are designated as Series B Preferred Stock. The holder of each share of Series B Preferred Stock shall be entitled to receive, out of the surplus of the Company, a non-cumulative dividend at the rate of \$.05 per share per annum, payable annually before any dividend shall be set apart for or paid on the common shares for such years. The Series B Preferred Stock has no voting rights. The Company may redeem any or all of the shares of Series B Preferred Stock then outstanding at a price per share of \$1.00. At February 28, 2002 and 2001, there were no outstanding shares of Series B preferred stock.

#### Series C

1,000,000 of the Company's 2,500,000 authorized shares of preferred stock, \$1

## Edgar Filing: QEP CO INC - Form 10-K

par value per share, are designated as Series C Preferred Stock. The holder of each share of Series C Preferred Stock shall be entitled to receive, before any dividends shall be declared or paid on or set aside for the Company's common stock, out of funds legally available for that purpose, cumulative dividends at the rate of \$.035 per share per annum, payable in annual installments, accruing from the date of issuance of the shares. The Series C Preferred Stock has no voting rights. The Company may redeem any or all of the shares of Series C Preferred Stock then outstanding at a price per share of \$1.00. During fiscal year 1995, 17,500 shares of Series C Preferred Stock were issued in connection with a business acquisition. In fiscal year 2002, the fiscal 2000 dividends of approximately \$600 were paid. In fiscal year 2002, dividends of approximately \$600 were declared and were unpaid at February 28, 2002.

### Treasury Stock

Total common shares purchased in fiscal year 1996 and held in treasury were 15,152 shares for an aggregate cost \$57,900. In fiscal 2001, pursuant to a resolution passed by the Board of Directors, the Company repurchased 42,000 shares of common stock at an aggregate cost of \$293,093. Further, pursuant to the same resolution, the Company repurchased 12,000 shares of common stock at an aggregate cost of \$39,649 in fiscal 2002.

### NOTE S - STOCK OPTION PLAN

The Company has adopted a stock option plan (the "Plan") for employees, consultants and directors of the Company. Stock options granted pursuant to the Plan shall be authorized by the Board of Directors. The aggregate number of shares which may be issued under the Plan shall not exceed 400,000 shares of common stock. Stock options are granted at prices not less than 85% of the fair market value on the date of the grant. All options granted, for the periods presented, have been at fair market value. Option terms, vesting and exercise periods vary, except that the term of an option may not exceed ten years.

F-20

### Q.E.P. CO., INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The Company continues to account for options issued under the intrinsic value method of APB 25. Had compensation cost been determined based on the fair value at the grant date for stock option awards consistent with the provisions of SFAS No. 123, the Company's net income and diluted earnings per share for the year ended February 28 or 29, 2002, 2001 and 2000 would have been as follows:

	(in thousands, except per share)	
	2002	2001
	-----	-----
Net income		
As reported	\$2,103	\$1,432
Pro forma	\$1,996	\$1,110
Net income per share		
As reported	\$ 0.62	\$ 0.42
Pro forma	\$ 0.56	\$ 0.33

The weighted average fair value at date of grant for options granted during

## Edgar Filing: QEP CO INC - Form 10-K

2002, 2001 and 2000 was \$1.18, \$1.94 and \$3.40 per option, respectively. The fair value of each option at date of grant was estimated using the Black-Scholes option pricing model with the following weighted average assumptions for grants.

	2002 ----	2001 ----
Expected stock price volatility	36.7%	33.7%
Expected lives of options		
Directors and officers	3 years	3 years
Employees	3 years	3 years
Risk-free interest rate	4.4%	5.9%
Expected dividend yield	0.0%	0.0%

	Shares -----
Options outstanding at February 28, 1999	451,500
Exercised	(37,500)
Granted	107,000
Cancelled or forfeited	(123,750)
	-----
Options outstanding at February 29, 2000	397,250
Exercised	(25,000)
Granted	36,000
Cancelled or forfeited	(16,187)
	-----
Options outstanding at February 28, 2001	392,063
Exercised	0
Granted	123,750
Expired	(157,813)
Cancelled or forfeited	(1,000)
	-----
Options outstanding at February 28, 2002	357,000
Options currently exercisable	197,868 =====

F-21

Q.E.P. CO., INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table summarizes information about stock options outstanding as of February 28, 2002:

Weighted average	Weighted
------------------	----------

Edgar Filing: QEP CO INC - Form 10-K

Range of exercise prices -----	Number outstanding -----	remaining contractual life -----	average exercise price -----	Number exercisable -----
\$3.65 - \$8.56	357,000	6.68	\$5.52	197,868

During fiscal 2002, the Company issued 50,000 non-Qualified stock options to an officer of the Company. These options have an exercise price of \$4.00 and expire in ten years.

NOTE T - NONCASH INVESTING AND FINANCING ACTIVITIES

During fiscal 2001, the Company acquired certain businesses. In connection with these acquisitions, liabilities were assumed as follows:

Cash paid	\$ 1,116,517
Liabilities assumed	75,710
Issuance of notes to related sellers	1,620,000
	-----
Purchase price	\$ 2,812,227
Fair value of net assets acquired	2,305,131
	-----
Excess of purchase price over fair value of net assets acquired	\$ 507,096
	=====

Also, during fiscal 2001, the Company made certain capital expenditures as follows:

Total capital expenditures	\$ 2,885,675
Amounts representing capitalized leases and other secured financing	\$ 866,882
	=====
Capital expenditures paid in cash	\$ 2,018,793
	=====

During fiscal 2000, the Company made six strategic acquisitions. In connection with these acquisitions, liabilities were assumed as follows:

Cash paid	\$ 2,668,000
Liabilities assumed	3,105,061
Issuance of notes to related sellers	2,985,000
	-----
Purchase price	\$ 8,758,061
Fair value of net assets acquired	5,258,061
	-----
Excess of purchase price over fair value of net assets acquired	\$ 3,500,000
	=====

NOTE U - NEW ACCOUNTING PRONOUNCEMENTS



## Edgar Filing: QEP CO INC - Form 10-K

On July 20, 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 141, "Business combinations," and SFAS No. 142, "Goodwill and Intangible Assets." SFAS No. 141 is effective for all business combinations completed after June 30, 2001. SFAS No. 142 is effective for fiscal years beginning after December 15, 2001; however, certain provisions of this Statement apply to goodwill and other intangible assets acquired between July 1, 2001 and the effective date of SFAS No. 142. Major provisions of these Statements and their effective dates for the Company are as follows:

All business combinations initiated after June 30, 2001 must use the purchase method of accounting. The pooling-of-interests method of accounting is prohibited except for transactions initiated before July 1, 2001;

F-22

### Q.E.P. CO., INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

. Intangible assets acquired in a business combination must be recorded separately from goodwill if they arise from contractual or other legal rights or are separable from the acquired entity and can be sold, transferred, licensed, rented or exchanged, either individually or as part of a related contract, asset or liability;

. Goodwill, as well as intangible assets with indefinite lives, acquired after June 30, 2001, will not be amortized. Effective January 1, 2002, all previously recognized goodwill and intangible assets with indefinite lives will no longer be subject to amortization;

. Effective March 1, 2002, goodwill and intangible assets with indefinite lives will be tested for impairment annually and whenever there is an impairment indicator; and,

. All acquired goodwill must be assigned to reporting units for purposes of impairment testing and segment reporting.

The Company will continue to amortize goodwill recognized prior to July 1, 2001, under its current method, until March 1, 2002, at which time annual and quarterly goodwill amortization of approximately \$118,000 and \$471,000, respectively, will no longer be recognized. The Company is in the process of completing its evaluation and believes that there will be an effect on the amount it currently has recorded as intangible assets as they relate to the Company's Latin American and European operations. Any impairment lost will be recorded in the Company's 1st quarter of fiscal 2003 as a cumulative effect of a change in accounting principle.

In August 2001, the FASB issued SFAS No. 144 "Accounting for the Impairment or Disposal of Long Lived Assets". SFAS No. 144 supercedes SFAS No. 121 "Accounting for the Impairment of Long Lived Assets and for Long Lived Assets to be Disposed Of". SFAS 144 retains substantially all of the requirements of SFAS 121 while resolving certain implementation issues. SFAS 144 is effective for fiscal years beginning after December 15, 2001 with earlier implementation encouraged. The Company is currently evaluating the impact on its financial statements of adopting SFAS 144.

F-23

### SUPPLEMENTAL FINANCIAL DATA QUARTERLY FINANCIAL DATA (UNAUDITED)

## Edgar Filing: QEP CO INC - Form 10-K

The quarterly results for the two years ended February 28, 2002 are set forth in the following table:

	Sales -----	Gross Profit -----	Net Earnings (Loss) -----	Earnings (Loss) per share -----	
2002 ----					
First quarter	\$ 28,886,441	\$ 9,755,096	\$ 604,294	\$ 0.18	(1)
Second quarter	27,267,023	9,154,028	609,003	0.18	
Third quarter	26,645,951	8,897,944	338,428	0.10	
Fourth quarter	26,875,308	9,265,105	551,253	0.16	
	-----	-----	-----	-----	
Total	\$109,674,723 =====	\$37,072,173 =====	\$ 2,102,978 =====	\$ 0.62 =====	
2001 ----					
First quarter	\$ 31,571,511	\$ 9,815,888	\$ 942,845	\$ 0.28	(1)
Second quarter	28,220,925	9,413,031	855,029	0.25	
Third quarter	26,350,670	7,650,377	(796,785)	(0.24)	(2)
Fourth quarter	26,859,981	9,184,036	431,616	0.13	
	-----	-----	-----	-----	
Total	\$113,003,087 =====	\$36,063,332 =====	\$ 1,432,705 =====	\$ 0.42 =====	

(1) Includes the impact on sales resulting from the Company's decision to license the rights of its tackless carpet strip product to U.S. flooring products distributors in May 2000. Sales of tackless carpet strip amounted to approximately \$2,957,000 predominantly made in the first quarter of fiscal 2001. There were no sales of this product to these distributors in fiscal 2002.

(2) Includes the impact of additional sales incentives offered by the Company to one of its major customers, certain non-recurring charges related to the Company's decision to relocate its California manufacturing facility to Nevada and a downsizing of the Company's Holland subsidiary to improve performance. In connection with these decisions, the Company expensed approximately \$2,000,000 of non-recurring charges in the third quarter of fiscal 2001. The resultant effect on earnings per share was a reduction of \$0.37 after tax.

F-24

### Q.E.P. CO., INC. AND SUBSIDIARIES SCHEDULE II - VALUATION AND QUALIFYING ACCOUNTS

Column A -----	Column B -----	Column C ----- Additions		Column D -----	Column E -----
Description	Balance at beginning of period	Charged to costs and expenses	Charged to other accounts	Deductions (a)	Balance end of period

Edgar Filing: QEP CO INC - Form 10-K

Year ended February 29, 2000					
Deducted from asset accounts					
Allowance for doubtful					
accounts	\$381,628	\$277,734	(b) 191,466	\$110,290	\$740,538
Year ended February 28, 2001					
Deducted from asset accounts					
Allowance for doubtful					
accounts	\$740,538	\$127,119	--	\$205,831	\$661,826
Year ended February 28, 2002					
Deducted from asset accounts					
Allowance for doubtful					
accounts	\$661,826	\$ 94,909	--	\$335,129	\$421,600

(a) Accounts written off as uncollectable, net of recoveries.

(b) Reserve associated with the Fiscal 2000 acquisitions at the date of acquisition.

S-1