

CHAMPION INDUSTRIES INC  
Form 10-K  
January 26, 2007

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 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 October 31, 2006

OR

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

Commission File No. 0-21084

CHAMPION INDUSTRIES, INC.

(Exact name of registrant as specified in its charter)

West Virginia  
(State or other jurisdiction of  
incorporation or organization)

55-0717455  
(I.R.S. Employer Identification  
No.)

2450 First Avenue  
P.O. Box 2968  
Huntington, West Virginia  
(Address of Principal Executive  
Offices)

25728  
(Zip Code)

Registrant's telephone number, including area code: (304) 528-2700

Securities registered pursuant to Section 12(b) of Act: Common Stock,  
\$1.00 par value

The Nasdaq Stock Market, LLC  
(Name of each exchange on which registered)

Securities registered pursuant to Section 12(g) of Act:  
None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes  No

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Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act.

Yes  No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark if the 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.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in rule 12b-2 of the Exchange Act).

Yes  No

As of April 30, 2006, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was \$28,720,863 based on the closing price as reported on the National Association of Securities Dealers Automated Quotation System National Market System.

The outstanding common stock of the Registrant at the close of business on January 4, 2007 consisted of 9,949,913 shares of Common Stock, \$1.00 par value.

Total number of pages including cover page 131.

DOCUMENTS INCORPORATED BY REFERENCE: Portions of the registration statement on Form S-2/A No. 333-47585, filed on March 16, 1998, are incorporated by reference into Part IV, Item 15. Portions of the Registrant's definitive proxy statement dated February 19, 2007 with respect to its Annual Meeting of Shareholders to be held on March 19, 2007 are incorporated by reference into Part III, Items 10-13. Exhibit Index located in Part IV Item 15.

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## **SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS**

Certain statements contained in this Annual Report or in documents incorporated herein by reference, including without limitation statements including the word “believes,” “anticipates,” “intends,” “expects” or words of similar import constitute “forward-looking statements” within the meaning of section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements of the Company expressed or implied by such forward-looking statements. Such factors include, among others, general economic and business conditions, general economic and business conditions in the Company’s market areas affected by Hurricane Katrina, changes in business strategy or development plans and other factors referenced in this Annual Report, including without limitations under the captions “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and “Business.” Given these uncertainties, prospective investors are cautioned not to place undue reliance on such forward-looking statements. The Company disclaims any obligation to update any such factors or to publicly announce the results of any revisions to any of the forward-looking statements contained herein to reflect future events or developments.

### **PART I**

#### **ITEM 1 - BUSINESS**

##### **HISTORY**

Champion Industries, Inc. (“Champion” or the “Company”) is a major commercial printer, business forms manufacturer and office products and office furniture supplier in regional markets east of the Mississippi River. The Company's sales offices and production facilities are located in Huntington, Charleston, Parkersburg, Clarksburg, Wheeling and Morgantown, West Virginia; Lexington and Owensboro, Kentucky; Baton Rouge and New Orleans, Louisiana; Cincinnati, Ohio; Kingsport and Knoxville, Tennessee; Evansville, Indiana; Bridgeville and Altoona, Pennsylvania; and Asheville, North Carolina. The Company's sales force of approximately 120 salespeople sells printing services, business forms management services, office products and office furniture.

The Company was chartered as a West Virginia corporation on July 1, 1992. Prior to the public offering of the Company's Common Stock on January 28, 1993 (the “Offering”), the Company's business was operated by The Harrah and Reynolds Corporation (“Harrah and Reynolds”), doing business as Chapman Printing Company, together with its wholly-owned subsidiaries, The Chapman Printing Company, Inc. and Stationers, Inc. Incident to the Offering, Harrah and Reynolds and the Company entered into an Exchange Agreement, pursuant to which, upon the closing date of the Offering: (i) Harrah and Reynolds contributed to the Company substantially all of the operating assets of its printing division, including all inventory and equipment (but excluding any real estate and vehicles) and all issued and outstanding capital stock of its subsidiaries, The Chapman Printing Company, Inc. and Stationers, Inc.; (ii) the Company assumed certain of the liabilities relating to the operations of the printing divisions of Harrah and Reynolds and its subsidiaries, The Chapman Printing Company, Inc. and Stationers, Inc., excluding debts associated with real estate, certain accounts payable to affiliates and certain

other liabilities; and (iii) Harrah and Reynolds was issued 2,000,000 shares of Common Stock of the Company.

The Company and its predecessors have been headquartered in Huntington since 1922. Full scale printing facilities, including web presses for manufacturing business forms, and sales and customer service operations are located in Huntington. The Company's Charleston division was established in 1974 through the acquisition of the printing operations of Rose City Press. Sales and customer service operations, as well as the pre-press departments, are located in Charleston. The Parkersburg division opened in 1977 and was expanded by the acquisitions of Park Press and McGlothlin Printing Company. In addition to sales and customer service operations, this division houses a large full-color printing facility and a state-of-the-art studio, with scanners, electronic color retouching equipment and 4-, 5- and 6-color presses.

The Lexington division commenced operations in 1983 upon the acquisition of the Transylvania Company. This location includes a pre-press department, computerized composition facilities, as well as sales and customer service operations.

The Company acquired Stationers, Inc. ("Stationers"), an office product, office furniture and retail bookstore operation located in Huntington, in 1987 and consolidated its own office products and office furniture operations with Stationers. On August 30, 1991, Stationers, Inc. sold the assets, primarily inventory and fixtures, of its retail bookstore operation. In July 1993, Stationers expanded through acquisition and began operations in Marietta, Ohio, under the name "Garrison Brewer." The Company's Garrison Brewer operation was relocated across the Ohio river to the nearby Chapman Printing Parkersburg location in 2002.

The Bourque Printing division ("Bourque" or "Champion Graphic Communications - Baton Rouge") commenced operations in June 1993, upon the acquisition of Bourque Printing, Inc. in Baton Rouge, Louisiana. This location includes a pre-press department, computerized composition facilities, a pressroom with up to 6-color presses and a bindery department, as well as sales and customer service operations. Bourque was expanded through the acquisition of Strother Forms/Printing in Baton Rouge in 1993, through the acquisition of the assets of E. S. Upton Printing Company, Inc. ("Upton" or "Champion Graphic Communications - New Orleans") in New Orleans in 1996 and through the acquisition of Transdata Systems, Inc. in Baton Rouge and New Orleans in 2001. The Upton production operations were relocated to Baton Rouge in the fourth quarter of 2005 as a result of Hurricane Katrina. However, the sales and customer service staff continue to operate in New Orleans.

The Dallas Printing division ("Dallas" or "Champion Jackson") commenced operations in September 1993, upon the acquisition of Dallas Printing Company, Inc. in Jackson, Mississippi. This location includes a pre-press department, computerized composition facilities, as well as sales and customer service operations. The operations of Dallas were moved to Baton Rouge, Louisiana in August 2005 and consolidated into an existing facility.

On November 2, 1993, a wholly-owned subsidiary of the Company chartered to effect such acquisition purchased selected assets of Tri-Star Printing, Inc., a Delaware corporation doing business as "Carolina Cut Sheets" in the manufacture and sale of business forms in Timmonsville, South Carolina. The Company's subsidiary has changed its name to "Carolina Cut

Sheets, Inc.” Carolina Cut Sheets manufactures single-part business forms for sale to dealers and through the Company's other divisions. Carolina Cut Sheets was relocated to Huntington, West Virginia in 2001.

On February 25, 1994, Bourque acquired certain assets of Spectrum Press Inc. (“Spectrum”), a commercial printer located in Baton Rouge, Louisiana.

On June 1, 1994, the Company acquired certain assets of Premier Data Graphics, a distributor of business forms and data supplies located in Clarksburg, West Virginia.

On August 30, 1994, Dallas acquired certain assets of Premier Printing Company, Inc. (“Premier Printing”) of Jackson, Mississippi. This operation was moved to Baton Rouge, Louisiana with the Dallas relocation.

On June 1, 1995, in exchange for issuance of 52,383 shares of its common stock, the Company acquired U.S. Tag & Ticket Company, Inc. (“U.S. Tag”), a Baltimore, Maryland based manufacturer of tags used in the manufacturing, shipping, postal, airline and cruise industries. The operations of U.S. Tag were moved to Huntington, West Virginia in August 2003 and they were consolidated into an existing facility.

On November 13, 1995, the Company acquired Donihe Graphics, Inc. (“Donihe”), a high-volume color printer based in Kingsport, Tennessee.

On July 1, 1996, the Company acquired Smith & Butterfield Co., Inc. (“Smith & Butterfield”), an office products company located in Evansville, Indiana and Owensboro, Kentucky. Smith & Butterfield is operated as a division of Stationers, Inc.

On August 21, 1996, the Company purchased the assets of The Merten Company (“Merten”), a commercial printer headquartered in Cincinnati, Ohio.

On December 31, 1996, the Company acquired all outstanding capital stock of Interform Corporation (“Interform”), a business form manufacturer in Bridgeville, Pennsylvania.

On May 21, 1997, the Company acquired all outstanding common shares of Blue Ridge Printing Co., Inc. of Asheville, North Carolina and Knoxville, Tennessee (“Blue Ridge”). During the second quarter of 2004, the Blue Ridge Knoxville plant was consolidated into the Asheville plant. The Company continues to maintain a sales office in Knoxville.

On February 2, 1998, the Company acquired all outstanding common shares of Rose City Press (“Rose City”) of Charleston, West Virginia.

On May 18, 1998, the Company acquired all outstanding common shares of Capitol Business Equipment, Inc. (“Capitol”), doing business as Capitol Business Interiors, of Charleston, West Virginia.

On May 29, 1998, the Company acquired all outstanding common shares of Thompson's of Morgantown, Inc. and Thompson's of Barbour County, Inc. (collectively, "Thompson's" or "Champion Morgantown") of Morgantown, West Virginia.

Rose City, Capitol and Thompson's are operated as divisions of Stationers.

On June 1, 1999, the Company acquired all of the issued and outstanding common stock of Independent Printing Service, Inc. ("IPS") of Evansville, Indiana. IPS is operated as a division of Smith & Butterfield.

On July 16, 1999, the Company's Blue Ridge subsidiary acquired certain assets and assumed certain liabilities of AIM Printing ("AIM") of Knoxville, Tennessee.

On November 30, 1999, the Company acquired all of the issued and outstanding common stock of Diez Business Machines ("Diez") of Gonzales, Louisiana. Diez was operated as a subsidiary of Stationers until 2004 when it was relocated to the Bourque facility in Baton Rouge, Louisiana.

On November 6, 2000, the Company acquired certain assets of the Huntington, West Virginia paper distribution division of the Cincinnati Cordage Paper Company ("Cordage"). On April 30, 2001, the Company entered into a strategic alliance with Xpedx resulting in the assumption by Xpedx of the Cordage customer list and the sale of certain inventory items.

On October 10, 2001, the Company acquired Transdata Systems, Inc. ("Transdata") of Baton Rouge and New Orleans, Louisiana. In 2004, Transdata was relocated to existing facilities in New Orleans and Baton Rouge. In 2005, Transdata New Orleans operations were relocated to Baton Rouge.

On June 18, 2003, the Company acquired certain assets of Contract Business Interiors ("CBI") of Wheeling, West Virginia pursuant to acceptance by the U.S. Bankruptcy Court for the Northern District of West Virginia. As a result of this transaction, the Company also assumed certain customer deposit liabilities in the ordinary course of business.

On July 1, 2003, the Company acquired certain assets of Pittsburgh based Integrated Marketing Solutions, the direct sales division and distributorship of Datatel Resources Corporation.

On May 13, 2004, the Company acquired certain assets of Cincinnati, Ohio Westerman Print Company ("Westerman"). The assets of Westerman were moved to the Company's Merten operation in Cincinnati, Ohio.

On September 7, 2004, the Company acquired all the issued and outstanding capital stock of Syscan Corporation ("Syscan"), a West Virginia corporation, for a gross cash price of \$3,500,000 and a contingent purchase price, dependent upon satisfaction of certain conditions, not to exceed the amount of \$1,500,000. On December 14, 2006 the Company satisfied the contingent purchase price for a payment of \$1,350,725. After considering the cash received in the transaction,

the acquisition of a building and acquisition costs the net assets acquired totaled approximately \$2,688,000.

All acquisitions have been accounted for using the purchase method of accounting except for U.S. Tag, Blue Ridge, Capitol and Thompson's, which utilized the "pooling-of-interest" method of accounting.

## **BUSINESS**

Champion is engaged in the commercial printing and office products and furniture supply business in regional markets east of the Mississippi River. The Company's sales force sells a full range of printing services, business forms, office products and office furniture. Management views these sales activities as complementary since frequent customer sales calls required for one of its products or services provide opportunities to cross-sell other products and services. The Company believes it benefits from significant customer loyalty and customer referrals because it provides personal service, quality products, convenience and selection with one-stop shopping.

The Company's printing services range from the simplest to the most complex jobs, including business cards, books, tags, brochures, posters, 4- to 6-color process printing and multi-part, continuous and snap-out business forms. The Company's state-of-the-art equipment enables it to provide computerized composition, art design, paste-up, stripping, film assembly and color scanner separations. Included within our print segment are fulfillment services to our customers which encompasses warehousing, distribution, and reporting services. The Company also offers complete bindery and letterpress services. The printing operations contributed \$106.4 million, \$98.5 million and \$95.3 million or 73.3%, 73.0% and 76.6% of the Company's total revenues for the fiscal years ended October 31, 2006, 2005 and 2004.

The Company provides a full range of office products and office furniture primarily in the budget and middle price ranges, and also offers office design services. The Company publishes a catalog of high volume, frequently ordered items purchased directly from manufacturers. These catalog sales account for the bulk of sales volume and afford sales personnel flexibility in product selection and pricing. Medium to large volume customers are offered levels of pricing discounts. In addition, the Company offers a broad line of general office products through major wholesalers' national catalogs. The Company has implemented Internet e-commerce sites, which allow customers to order office products, furniture and forms online. The e-commerce sites include the office products and office furniture catalog, which is customized specifically for each customer requesting Internet e-commerce access. In addition, the Company offers customized on-line forms management solutions through [www.cgcl.com](http://www.cgcl.com). The Company believes that its e-commerce sites will allow customers to access data concerning their company's purchase habits so as to better control expenditures for office products and business forms and eliminate large in-house inventories. The Company is a member of a major office products purchasing organization. Members benefit from volume discounts, which permit them to offer competitive prices and improve margins. The Company's office furniture business focuses on the budget to middle price range lines, although upscale lines are offered as well. Office products, office furniture and office design operations contributed \$38.8 million, \$36.5

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million and \$29.1 million, or 26.7%, 27.0% and 23.4% of the Company's total revenues for the fiscal years ended October 31, 2006, 2005 and 2004.

## ORGANIZATION

Champion's two lines of business are comprised of seventeen operating divisions. The Huntington headquarters provides centralized financial management and administrative services to each of its two business segments.

### Commercial Printing

Eight commercial printing divisions are located in Huntington, Charleston and Parkersburg, West Virginia; Lexington, Kentucky; Baton Rouge, Louisiana; Cincinnati, Ohio; Kingsport, Tennessee; and Asheville, North Carolina. Each has a sales force, a customer service operation and a pre-press department that serve the customers in their respective geographic areas. Although each customer's interface is solely with its local division's personnel, its printing job may be produced in another division using the equipment most suited to the quality and volume requirements of the job. In this way, for example, Champion can effectively compete for high quality process color jobs in Lexington by selling in Lexington, printing in Cincinnati and binding in Huntington. The full range of printing resources is available to customers in the entire market area without Champion having to duplicate equipment in each area.

Interform Corporation, doing business as Interform Solutions and located in Bridgeville, Pennsylvania, manufactures business forms and related products, which it sells through a network of independent distributors concentrated in Eastern Pennsylvania, New Jersey and metropolitan New York.

Consolidated Graphic Communications division in Bridgeville, Pennsylvania operates as a full line printing and printing services distributor. The division offers complete print management, fulfillment services and B2B e-commerce solutions.

Carolina Cut Sheets, Inc., located in Huntington, West Virginia, manufactures single sheet business forms which are sold to other commercial printers and dealers and through the Company's other divisions.

The Huntington, West Virginia division of Chapman Printing Company manufactures single sheet and multi-part, snap-out and continuous business forms for sale through many of the Company's commercial printing divisions.

U.S. Tag, located in Huntington, West Virginia, manufactures and sells tags used in the manufacturing, shipping, postal, airline and cruise industries throughout the United States through dealers and the Company's other divisions.

Chapman Printing in Charleston, West Virginia operates as a full line printing, printing services distributor and office products and office furniture distributor. Chapman Printing Charleston offers complete print management, fulfillment, mail, digital print, office furniture and print and office

products B2B e-commerce solutions. The Syscan operation was consolidated into the Chapman Printing Charleston division effective November 1, 2005. This division also operates a facility in Morgantown, West Virginia providing printing, office products and office furniture, distribution and integration services. In 2007, the Chapman Printing Charleston division spun off its print on demand and mail operations into a new division located in Charleston, West Virginia operating under Champion Output Solutions. Champion Output Solutions is a comprehensive transactional printing and mail center providing statement rendering, check and explanation of benefits variable print, medical billing and postal optimization.

#### Office Products, Office Furniture and Office Design

Stationers, located in Huntington, Clarksburg (doing business as “Champion Clarksburg”), Morgantown (through its Chapman Printing Morgantown division) and Parkersburg, West Virginia (doing business as “Chapman Printing”), provides office products and office furniture primarily to customers in the Company's West Virginia, Ohio and Kentucky market areas. Products are sold by printing division salespeople and delivered in bulk daily to each division, or shipped directly to customers.

Smith & Butterfield, located in Evansville, Indiana and Owensboro, Kentucky, provides office products and office furniture primarily to customers in the Company's Indiana and Kentucky market areas. Products are sold by Smith & Butterfield sales personnel and delivered to customers daily.

Stationers, through its Capitol division, offers office design services throughout West Virginia and eastern Kentucky.

### **PRODUCTS AND SERVICES**

#### Printing Services

Champion's primary business is commercial printing and business forms manufacturing. The Company, unlike most of its regional competitors, offers the full range of printing production processes, enabling the Company to provide customers a one-stop, one-vendor source without the time and service constraints of subcontracting one or more aspects of production. Major production areas include: (i) printing of business cards, letterhead, envelopes, and one, two, or three color brochures; (ii) process color manufacturing of brochures, posters, advertising sheets and catalogues; (iii) die cutting and foil stamping; (iv) bindery services, including trimming, collating, folding and stitching the final product; (v) forms printing, encompassing roll-to-roll computer forms, checks, invoices, purchase orders and similar forms in single-part, multi-part, continuous and snap-out formats; (vi) tag manufacturing; (vii) high volume process color web printing of brochures and catalogs; and (viii) output solutions including print on demand, inserting and mailing services. The capabilities of the Company's various printing divisions are stated below.

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| Division                                      | Sales & Customer Service | Pre-Press | Sheet Printing | Rotary Printing | Full Color | High Volume Full Color | Output Solutions |
|---|--------------------------|-----------|----------------|-----------------|------------|------------------------|------------------|
| Huntington                                    | *                        | *         | *              | *               |            |                        |                  |
| Charleston / Morgantown                       | *                        | *         |                |                 |            |                        |                  |
| Champion Output Solutions                     |                          |           |                |                 |            |                        | *                |
| Parkersburg                                   | *                        | *         | *              |                 | *          |                        |                  |
| Lexington                                     | *                        | *         |                |                 |            |                        |                  |
| Champion Graphic Communications (Baton Rouge) | *                        | *         | *              |                 | *          |                        |                  |
| Champion Graphic Communications (New Orleans) | *                        |           |                |                 |            |                        |                  |
| Carolina Cut Sheets, Inc.                     | *                        |           |                |                 |            |                        |                  |
| U.S. Tag & Ticket Company, Inc.               | *                        | *         |                | *               |            |                        |                  |
| Donihe Graphics, Inc.                         | *                        | *         | *              | *               | *          | *                      |                  |
| The Merten Company                            | *                        | *         | *              |                 | *          |                        |                  |
| Interform Corporation                         | *                        | *         |                | *               | *          |                        | *                |
| Consolidated Graphic Communications           | *                        | *         |                |                 |            |                        |                  |
| Blue Ridge Printing Co., Inc.                 | *                        | *         | *              |                 | *          |                        |                  |

\* - Services Provided

Office Products, Office Furniture and Office Design

Champion provides its customers with a wide range of product offerings in two major categories: supplies, such as file folders, paper products, pens and pencils, computer paper and laser cartridges; and furniture, including budget and middle price range desks, chairs, file cabinets and computer furniture. Office supplies are sold primarily by Company salespeople through the Company's own catalogs. Office furniture is primarily sold from catalogs and supplied from in-house stock. Special orders constitute a small portion of sales. The Capitol division of Stationers provides interior design services to commercial customers. The design services include space planning, purchasing and installation of office furniture, and management of design projects.

**MANUFACTURING AND DISTRIBUTION**

The Company's pre-press facilities have desktop publishing, typesetting, laser imagesetting and scanning/retouching equipment, as well as complete layout, design, stripping and plate processing operations. Sheet printing equipment (for printing onto pre-cut, individual

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sheets) includes single color duplicators, single to six color presses and envelope presses. Rotary equipment (for printing onto continuous rolls of paper) includes multi-color business form web presses, carbon and multi-part collators, and a high-speed 5-color half-web press.

Binding equipment consists of hot-foil, embossing and die cutting equipment, perforators, folders, folder-glueers, scoring machines, collator/stitcher/trimmers for saddle stitching, automatic and manual perfect binders, numbering machines and mailing equipment.

Each of the Company's offices is linked with overnight distribution of products and on-line electronic telecommunications permitting timely transfer of various production work from facility to facility as required. While the Company maintains a fleet of delivery vehicles for intracompany and customer deliveries, it utilizes the most cost effective and expeditious means of delivery, including common carriers.

Requirements for the Company's press runs are determined shortly before the runs are made and, therefore, backlog is not a meaningful measure in connection with the Company's printing business.

The Company's inventory goal is to have approximately 85% of the office product items the Company sells in stock. Another 12% are ordered on a daily basis and received overnight. The remaining 3% are items that come direct from manufacturers and may take one week or more from placement of order to delivery to customer. Office furniture sales for mid-line and budget are made primarily from the Company's in-house stock. However, special orders from manufacturers and project furniture may require 30 to 90 days for delivery.

## **CUSTOMERS**

The Company believes that its reputation for quality, service, convenience and selection allows it to enjoy significant loyalty from its customers. Champion's marketing strategy is to focus on manufacturers, institutions, financial services companies and professional firms. Consistent with customary practice in the commercial printing and office products industries, the Company ordinarily does not have long-term contracts with its customers, although a number of high volume customers issue yearly purchase orders. These purchase orders, which are typically for office products but may include printing services, are for firm prices adjustable for paper price changes. Depending upon customer satisfaction with price and service, these purchase orders may be renewed for another year or up to three years without repeating the full bidding process.

During the fiscal years ended October 31, 2006 and 2005, no single customer accounted for more than 3% of the Company's total revenues. During fiscal year ended October 31, 2004, no single customer accounted for more than 2% of the Company's total revenues. Due to the project-oriented nature of customers' printing requirements, sales to particular customers may vary significantly from year to year depending upon the number and size of their projects.

## **SUPPLIERS**

The Company has not experienced difficulties in obtaining materials in the past and does not consider itself dependent on any particular supplier for supplies. The Company has negotiated company-wide paper purchasing agreements directly with paper manufacturers and is a member of a major office products buying group, which management believes provides the Company with a competitive advantage.

## **COMPETITION**

The markets for the Company's printing services and office products are highly competitive, with success based primarily on price, quality, production capability, capacity for prompt delivery and personal service.

Champion's printing competitors are numerous and range in size from very large national companies with substantially greater resources than the Company to many smaller local companies. In recent years, despite consolidation within the printing industry, there has been a substantial increase in technological advances in new equipment, resulting in excess capacity and highly competitive pricing. The Company has remained competitive by maintaining its printing equipment at state-of-the-art levels and emphasizing personal attention to customers.

Large national and regional mail order discount operations provide significant competition in the office products and office furniture business. The economies afforded by membership in a national purchasing association and by purchasing directly from manufacturers, and the high level of personal services to customers, contribute substantially to the Company's ability to compete in the office supply and office furniture market segments.

## **ENVIRONMENTAL REGULATION**

The Company is subject to the environmental laws and regulations of the United States and the states in which it operates concerning emissions into the air, discharges into waterways and the generation, handling and disposal of waste materials. The Company's past expenditures relating to environmental compliance have not had a material effect on the Company and are included in normal operating expenses. These laws and regulations are constantly evolving, and it is impossible to predict accurately the effect they may have upon the capital expenditures, earnings and competitive position of the Company in the future. Based upon information currently available, management believes that expenditures relating to environmental compliance will not have a material impact on the financial position of the Company.

## **GEOGRAPHIC CONCENTRATION AND ECONOMIC CONDITIONS**

The Company's operations and the majority of its customers are located in the United States of America, east of the Mississippi River. The Company and its profitability may be more susceptible to the effects of unfavorable or adverse local or regional economic factors and conditions than a company with a more geographically diverse customer base.

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On August 29, 2005, Hurricane Katrina made landfall and subsequently caused extensive flooding and destruction along the coastal areas of the Gulf of Mexico, including New Orleans and other communities in Louisiana and Mississippi in which Champion conducts business. Operations in many of the Company's markets were disrupted by both the evacuation of large portions of the population as well as damage and/or lack of access to the Company's operating facility in New Orleans.

The Company filed insurance claims related to both actual and contingent losses. The Company received an advance to claim payment from an insurance company of \$300,000 in February 2006 and final settlement claims of \$278,000 in April and May 2006. The Company recorded the \$300,000 payment as an insurance recovery and related receivable at January 31, 2006. The Company recorded additional charges of approximately \$42,000 in the first quarter of 2006 associated with Hurricane Katrina. The Company received a second advance to claim check in April of 2006 in the amount of \$200,000 and a full settlement of any and all claims check of \$78,000 in May of 2006. The Company recorded the aggregate amount of these checks as an insurance recovery and the \$78,000 as a related receivable at April 30, 2006. The Company incurred additional charges of \$234,000 primarily related to additional inventory valuation reserves and costs associated with relocation in the second quarter of 2006. During the fourth quarter of 2006 the Company successfully negotiated an early lease termination related to its New Orleans location resulting in Katrina related recoveries of approximately \$76,000.

#### **SEASONALITY**

Historically, the Company has experienced a greater portion of its profitability in the second and fourth quarters than in the first and third quarters. The second quarter generally reflects increased orders for printing of corporate annual reports and proxy statements. A post-Labor Day increase in demand for printing services and office products coincides with the Company's fourth quarter.

#### **EMPLOYEES**

On October 31, 2006, the Company had approximately 730 employees.

The Company's subsidiary, Interform Corporation, is party to a collective bargaining agreement with the United Steelworkers of America, AFL-CIO-CLC on behalf of its Local Union 8263 covering all production and maintenance employees (totaling approximately 70 employees at October 31, 2006) at its Bridgeville, Pennsylvania facility. This contract expires May 31, 2010. The Company believes relations with the union and covered employees are good.

**EXECUTIVE OFFICERS OF CHAMPION**

**Position and offices with Champion;**

| Name                 | Age | Principal occupation or employment last five years   |
|----------------------|-----|--|
| Marshall T. Reynolds | 70  | Chief Executive Officer and Chairman of the Board of Directors of the Company from December 1992 to present; President of the Company December 1992 to September 2000; President and General Manager of Harrah and Reynolds, predecessor of the Company from 1964 (and sole shareholder from 1972 to present) to 1993; Chairman of the Board of Directors of River City Associates Inc. (owner of the Pullman Plaza Hotel) since 1989; Chairman of the Board of Directors of Broughton Foods Company from November 1996 to June 1999; Director (from 1983 to November 1993) and Chairman of the Board of Directors (from 1983 to November 1993) of Banc One West Virginia Corporation (formerly Key Centurion Bancshares, Inc.). |
| Toney K. Adkins      | 57  | President and Chief Operating Officer of the Company since January 2005; Vice President-Administration of the Company from November 1995 to January 2005; President, KYOWVA Corrugated Container Company, Inc. from 1991 to 1996.  |
| J. Mac Aldridge      | 65  | Senior Vice President of the Company and Division Manager - Stationers since January 2005; Vice President and Division Manager - Stationers from December 1992 to January 2005; Vice President of Company and Division Manager - Huntington from September 1995 to October 1997; President and General Manager of Stationers since November 1989; Sales Representative of Huntington Division of Harrah and Reynolds from July 1983 to October 1989.   |



|                     |    |   |
|---------------------|----|---|
| R. Douglas McElwain | 59 | Senior Vice President and Division Manager - Consolidated Graphics Division of the Company since January 2005; Vice President and Division Manager - Bourque Printing division of the Company from December 1993 to January 2005; General Manager of Bourque Printing from June 1993 to December 1993; Sales Representative of Charleston Division of Harrah and Reynolds and Company from 1986 until June 1993.                                    |
| Todd R. Fry         | 41 | Senior Vice President and Chief Financial Officer of the Company since January 2005; Vice President and Chief Financial Officer of the Company from November 1999 to January 2005; Treasurer and Chief Financial Officer of Broughton Foods Company from September 1997 to June 1999; Coopers & Lybrand L.L.P. from 1991 to September 1997.   |
| Walter R. Sansom    | 77 | Secretary of the Company since December 1992; Production Coordinator of the Company since December 1992 and of Harrah and Reynolds from August 1968 to December 1992.   |
| James A. Rhodes     | 50 | Senior Vice President of the Company since January 2005; Vice President of the Company from March 1999 to January 2005; President of Interform since October 2004; President of Consolidated Graphic Communications Division of Interform since February 1999; Vice President of Sales of Consolidated Graphic Communications from 1996 to 1999; General Sales Manager - Eastern Division of Consolidated Graphic Communications from 1995 to 1996. |

## ITEM 1A - RISK FACTORS

The Company's business and results of operations are subject to a number of risks, many of which are outside of the Company's control. In addition to the other information in this report, readers should carefully consider that the following important factors, among others, including risks not presently known or currently deemed immaterial by us could materially impact the Company's business and future results of operations.

### **Dependence on Marshall T. Reynolds; Control of the Company.**

The Company's operations and prospects are dependent in large part on the continued efforts of Marshall T. Reynolds. The loss of Mr. Reynolds could have an adverse effect on the Company. In addition, by virtue of Mr. Reynolds' ownership of Company common stock, Mr. Reynolds will continue to significantly influence our operations. As of October 31, 2006, Marshall T. Reynolds and his affiliated entities, including The Harrah and Reynolds Corporation ("Harrah and Reynolds"), held 4,274,127 shares (43.1%) of the common stock of the Company. Sales by Mr. Reynolds of common stock could adversely affect the prevailing market price of the common stock. The Company is unable to estimate the amount of common stock, if any, that may be sold in the future.

### **The Company operates in a highly competitive market that could negatively impact our results of operations.**

In the printing segment, there has been an ongoing consolidation resulting in fewer competitors. This in part has resulted in numerous competitors that are larger with greater geographic diversity and broader product offerings. In addition, the office products and office furniture industries are extremely competitive and fragmented. The Company competes with numerous large and small companies that operate in each industry, some of which have greater financial resources than the Company. The Company competes on the basis of its reputation for quality, production capability, prompt delivery, price and strength of its continuing customer relationships.

Our supply-chain management services are embedded into our printing and office products and office furniture segments. The competitive factors faced by the Company include customer service, price, distribution geography, information technology and the customer's fulfillment and distribution needs.

**The Company may be adversely impacted by the rising costs of critical raw materials such as paper, ink, energy, postage and other raw materials.**

Our primary raw material is paper, therefore, the purchase of paper and other raw materials such as ink, energy, postage and items we distribute such as office products and office furniture and goods and services represent a large portion of our costs. Any increases in the costs of these items will also increase our costs. Depending on the nature of such increases we may not be able to pass these costs on to customers through higher prices. Increases in the costs of these items may also adversely impact our customers' demand for printing and related services as well as for office products and office furniture.

**The Company has substantial investment in the credit worthiness and financial condition of our customers.**

The largest asset on the Company's balance sheet on a net basis is our accounts receivable balances from our customers. We grant credit to substantially all of our customers. A decline in financial condition across a significant component of our customer base could hinder our ability to collect amounts owed by customers. In addition, such a decline could result in lower demand for our services. The potential causes of such a decline include national or local economic downturns, the fact that many of our customers are in highly-competitive industries or markets and the impact of regulatory actions may impact the financial stability of our customers.

**We may have difficulty adjusting our operating models to meet changing or current market conditions.**

Because the markets in which we compete are highly-competitive, we must continue to improve our operating efficiency in order to maintain or improve our profitability. Although we have been able to improve efficiency and reduce costs in the past, there is no assurance that we will continue to do so in the future. In addition, the need to reduce ongoing operating costs may result in significant up-front costs to reduce workforce, close or consolidate facilities, or upgrade equipment and technology.

**We may be unable to grow through acquisitions or to successfully integrate acquired businesses.**

The Company has historically grown through a combination of organic growth and acquisitions. It is critical that the Company achieve the anticipated benefits of acquisitions. The integration of companies that have previously operated independently may result in significant challenges, and we may be unable to accomplish the integration smoothly or successfully. In particular, the coordination of geographically dispersed organizations with differences in corporate cultures and management philosophies may increase the difficulties of integration. The integration of acquired businesses may also require the dedication of significant management resources, which may temporarily shift senior management's attention from the other day-to-day operations of the Company. Our strategy is, in part, predicated on our ability to realize cost savings and to increase revenues through the acquisition of businesses that strategically enhance our capabilities and services.

**We may have difficulty hiring and retaining appropriate employees including senior management.**

Our success depends, in part, on our general ability to attract, develop, motivate and retain highly skilled employees. The loss of a significant number of our employees or the inability to attract, hire, develop, train and retain additional skilled personnel could have a material adverse effect on us. We currently operate in several locations with geographic diversity, individual locations may encounter strong competition from other employers for skilled labor. In addition, many members of our management have significant industry experience and a long track record with us that is important to our continued success. If one or more members of our senior management team leave and we cannot replace them with a suitable candidate quickly, we could experience difficulty in managing our business properly, which could harm our business and results of operations.

**We may be negatively impacted by strikes or other work stoppages by our employees.**

We employ approximately 70 persons who are covered by collective bargaining agreements. If our unionized employees were to engage in a concerted strike or other work stoppage, or if our other employees were to become unionized, we could experience a disruption of operations, higher labor costs or both.

**We may have increased employee benefit costs for health care and other benefits.**

We provide health care and certain other benefits to our employees. In recent years, costs for health care have increased more rapidly than general inflation in the U.S. economy. If this trend in health care costs continues, our cost to provide such benefits could increase, adversely impacting our business and results of operations.

**We may be negatively impacted by declines in general economic conditions or acts of war and terrorism.**

Demand for printing services is highly correlated with general economic conditions. A decline in U.S. economic conditions may, therefore, adversely impact our business and results of operations. Because such outcomes are difficult to predict, the industry may experience excess capacity resulting in declines in prices for our services. The overall business climate may also be impacted by domestic and foreign wars or acts of terrorism. Such acts may have sudden and unpredictable adverse impacts on demand for our services.

**We may face adverse pricing pressures as a result of operating in a highly competitive market.**

The markets for our services are highly fragmented and we have a large number of competitors, resulting in a highly competitive market and increasing the risk of adverse pricing pressures in various circumstances outside of our control, including economic downturns.

**We are dependent on the the markets utilizing printed materials in lieu of alternative media. If this changes we may be adversely affected.**

In addition to traditional non-print based marketing and advertising channels, online distribution and hosting of media content may gain broad acceptance or preferred status relative to printed materials among consumers generally and have an adverse effect on our business. Consumer acceptance of electronic delivery as well as the extent that consumers may have previously replaced traditional reading of print material with online hosted media contents is uncertain. We have no ability to predict the likelihood that this may occur.

**We may be adversely affected by regulatory requirements, tax requirements and The Sarbanes-Oxley Act.**

We are subject to numerous rules and regulations, including, but not limited to, environmental and health and welfare benefit regulations as well as those associated with being a public company as well as numerous federal, state, and local tax rules and regulations. These rules and regulations and associated interpretations may be changed by local, state or federal governments or agencies. Changes in these regulations may result in a significant increase in our compliance costs. Compliance with changes in rules and regulations could require increases to our workforce, increased cost for services, compensation and benefits, or investments in new or upgraded equipment. In addition, audits and examinations of prior years may result in liabilities and additional financial burdens. The Company currently has not been required by the United States Securities and Exchange Commission to report on the effectiveness of its internal controls in accordance with Section 404 of The Sarbanes-Oxley Act. Under current regulations the Company will be required to comply with such requirements in the future. The Company is currently unable to predict the cost or difficulties required to complete such certifications.

**We are highly dependent on information technology. If our systems fail or are unreliable our operations may be adversely impacted.**

The efficient operation of our business depends on our information technology infrastructure and our management information systems. In addition, production technology in the printing industry has continued to evolve specifically related to the pre-press component of production. We rely on our management information systems to effectively manage accounting and financial functions, job entry, tracking and cost accumulation and certain purchasing functions as well as fulfillment and inventory management including e-commerce activities. Our information technology infrastructure includes both third party solutions and applications designed and maintained internally. Since our Company operates on multiple platforms, the failure of our information technology infrastructure and/or our management information systems to perform could severely disrupt our business and adversely affect our results of operation. In addition, our information technology infrastructure and/or our management information systems are vulnerable to damage or interruption from natural or man-made disasters, terrorist attacks, computer viruses or hackers, power loss, or other computer systems, Internet telecommunications or data network failures. Any such interruption could adversely affect our business and results of operations.

**ITEM 2 - PROPERTIES**

The Company conducts its operations primarily from nineteen (19) different physical locations, thirteen (13) of which are leased and six (6) of which are owned in fee simple by Company subsidiaries. The Company also owns two facilities of which the operations have been consolidated into other Champion facilities. The Company also leases other facilities primarily as sales and customer service locations, these operations and locations are not included as core operating facilities. The Company does not anticipate any issues in regards to the renewal of certain leases when the terms expire. The properties leased and certain of the lease terms are set forth below and may be subject to periodic adjustments based on the consumer price index:

| <b>Property</b>   | <b>Division Occupying Property</b> | <b>Square Feet</b> | <b>Annual Rental</b> | <b>Expiration Of Term</b> |
|---|------------------------------------|--------------------|----------------------|---------------------------|
| 2450 1 <sup>st</sup> Avenue<br>Huntington, West Virginia (1)    | Chapman Printing-<br>Huntington    | 85,000             | \$116,400            | 2008                      |
| 1945 5 <sup>th</sup> Avenue<br>Huntington, West Virginia (1)    | Stationers                         | 37,025             | 30,000               | 2007                      |
| 615-619 4 <sup>th</sup> Avenue<br>Huntington, West Virginia (1) | Stationers                         | 59,641             | 21,600               | 2008                      |
| 405 Ann Street<br>Parkersburg, West Virginia (1)                | Chapman Printing -<br>Parkersburg  | 36,614             | 57,600               | 2008                      |
| 890 Russell Cave<br>Road<br>Lexington, Kentucky (1)             | Chapman Printing -<br>Lexington    | 20,135             | 57,600               | 2007                      |
| 2800 Lynch Road<br>Evansville, Indiana (1)                      | Smith & Butterfield                | 42,375             | 121,640              | 2009                      |
| 1901 Mayview Road<br>Bridgeville,<br>Pennsylvania (1)           | Interform Corporation              | 120,000            | 293,503              | 2008                      |
| 736 Carondelet Street<br>New Orleans,<br>Louisiana (3)          | Upton Printing                     | 15,000             | -                    | 2007                      |
| 1515 Central Parkway<br>Cincinnati, Ohio (1)                    | The Merten Company                 | 40,000             | 107,163              | 2011                      |
| 1214 Main Street  | CBI - Wheeling                     | 22,000             | 36,000               | 2009                      |

Wheeling, West  
Virginia

|   |                                |        |         |      |
|---|--------------------------------|--------|---------|------|
| 3000 Washington St.<br>Charleston, West<br>Virginia (2) | Chapman<br>Printing-Charleston | 37,710 | 147,240 | 2009 |
| 951 Point Marion Rd.<br>Morgantown, West<br>Virginia    | Chapman<br>Printing-Charleston | 5,850  | 42,000  | 2010 |
| 120 Hills Plaza<br>Charleston, West<br>Virginia (4)     | Champion Output<br>Solutions   | 22,523 | 115,992 | 2011 |

(1) Lease is “triple net”, whereby the Company pays for all utilities, insurance, taxes, repairs and maintenance and all other costs associated with properties.

(2) Champion has an option to purchase building at end of lease term and Williams Land Corporation has an option to put the building to Champion at end of lease term.

(3) The Upton productions operations were relocated to Baton Rouge in the fourth quarter of 2005 as a result of Hurricane Katrina. However, the sales and customer service staff continues to operate in New Orleans. The annual rent excludes a credit for roof repairs paid by Upton of approximately \$1,478 per month for 57 months. In September 2006, the Company bought out the remaining lease term on this property for a one-time aggregate payment of \$45,000. As a result of this lease buy-out, the Company must vacate the property no later than March 31, 2007.

(4) Lease is gross to the extent it excludes taxes and insurance during the initial lease term. The Company has renewal options through 2019 at various rates and the lease essentially converts to a triple net lease in the renewal period. The Company has entered into a sublease agreement with an anticipated start date of January 2007, through June 30, 2011, at an annual sublease of \$44,370, representing approximately 8,500 square feet.

The Dallas Printing subsidiary owns, and previously operated from, a single-story masonry structure of approximately 19,600 square feet at 321-323 East Hamilton Street, Jackson, Mississippi. This building was vacated during the fourth quarter of 2005. The Company is currently evaluating its options regarding this facility.

The Chapman Printing Charleston operation previously conducted business from a single story masonry building of approximately 21,360 square feet owned by the Company at 1563 Hansford Street, Charleston, West Virginia. This building was vacated during the second quarter of 2005. The Company is currently evaluating its facility needs in Charleston and the future use, if any, of this building. The Company also owns a structure in Charleston, WV that was purchased as a result of the Syscan acquisition. This building is located at 811 Virginia Street West and is a three-story block building.

The Bourque Printing subsidiary owns, and operates from, a single-story building of approximately 42,693 square feet at 10848 Airline Highway, Baton Rouge, Louisiana. The Company also owns a warehouse and storage facility of approximately 18,501 square feet at 13112 South Choctaw Drive, Baton Rouge, Louisiana.

Stationers' Clarksburg operation is conducted from a single-story masonry building of approximately 20,800 square feet owned by the Company at 700 N. Fourth Street, Clarksburg, West Virginia.

Donihe owns, and operates from, a single-story steel building of approximately 38,500 square feet situated on roughly 14.5 acres at 766 Brookside Drive, Kingsport, Tennessee.

Blue Ridge owns, and operates from, a two-story masonry and steel building of approximately 28,000 square feet and a contiguous 1,692 square foot former residential structure at 544 and 560 Haywood Road, Asheville, North Carolina.

The Capitol subsidiary of Stationers owns and operates from a 22,000 square foot building at 711 Indiana Avenue, Charleston, West Virginia.

The Company continually reviews its production facilities and has and continues to consolidate facilities as deemed economically feasible. The Company believes its production facilities are suitable and adequate to meet current production needs.



**ITEM 3 - LEGAL PROCEEDINGS**

The Company is subject to various claims and legal actions that arise in the ordinary course of business. In the opinion of management, after consulting with legal counsel, the Company believes that the ultimate resolution of these claims and legal actions will not have a material effect on the consolidated financial statements of the Company.

**ITEM 4 - SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

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

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**PART II****ITEM 5 - MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

Champion common stock has traded on the National Association of Securities Dealers, Inc. Automated Quotation System ("NASDAQ") National Market System (now Global Market) since the Offering under the symbol "CHMP."

The following table sets forth the high and low closing prices for Champion common stock for the period indicated. The range of high and low closing prices are based on data from NASDAQ and does not include retail mark-up, mark-down or commission.

|                | Fiscal Year 2006 |                | Fiscal Year 2005 |                |
|----------------|------------------|----------------|------------------|----------------|
|                | <b>High</b>      | Low            | <b>High</b>      | Low            |
| First quarter  | <b>\$ 4.50</b>   | <b>\$ 4.25</b> | <b>\$ 3.89</b>   | <b>\$ 3.47</b> |
| Second quarter | <b>6.49</b>      | <b>4.27</b>    | <b>4.38</b>      | <b>3.85</b>    |
| Third quarter  | <b>9.98</b>      | <b>6.05</b>    | <b>4.35</b>      | <b>3.85</b>    |
| Fourth quarter | <b>7.93</b>      | <b>6.30</b>    | <b>4.48</b>      | <b>4.12</b>    |

At the close of business on January 2, 2007, there were 438 shareholders of record of Champion common stock. The shareholders of record are determined by the Company's transfer agent.

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The following table sets forth the quarterly dividends per share declared on Champion common stock.

|                | <b>Fiscal Year<br/>2007</b> | <b>Fiscal Year<br/>2006</b> | <b>Fiscal Year<br/>2005</b> |
|----------------|-----------------------------|-----------------------------|-----------------------------|
| First quarter  | <b>\$0.06</b>               | <b>\$0.05</b>               | <b>\$0.05</b>               |
| Second quarter | -                           | <b>0.05</b>                 | <b>0.05</b>                 |
| Third quarter  | -                           | <b>0.05</b>                 | <b>0.05</b>                 |
| Fourth quarter | -                           | <b>0.05</b>                 | <b>0.05</b>                 |

## **ITEM 6 - SELECTED FINANCIAL DATA**

### **SELECTED CONSOLIDATED FINANCIAL DATA**

The following selected consolidated financial data for each of the five years in the period ended October 31, 2006, have been derived from the Audited Consolidated Financial Statements of the Company. The information set forth below should be read in conjunction with the Audited Consolidated Financial Statements, related notes, and the information contained in Management's Discussion and Analysis of Financial Condition and Results of Operations appearing elsewhere herein.

|  | Year Ended October 31,                          |           |           |           |           |
|--|---|-----------|-----------|-----------|-----------|
|  | 2006 (1)  | 2005 (1)  | 2004      | 2003      | 2002      |
|  | (In thousands, except share and per share data) |           |           |           |           |
| <b>OPERATING STATEMENT</b>                         |   |           |           |           |           |
| <b>DATA:</b>                                       |   |           |           |           |           |
| <b>Revenues:</b>                                   |   |           |           |           |           |
| Printing   | \$ 106,414                                      | \$ 98,458 | \$ 95,325 | \$ 96,537 | \$ 95,194 |
| Office products and office furniture               | 38,774  | 36,467    | 29,077    | 25,646    | 27,690    |
| Total revenues                                     | 145,188   | 134,925   | 124,402   | 122,183   | 122,884   |
| <b>Cost of sales:</b>                              |   |           |           |           |           |
| Printing   | 75,016  | 70,978    | 69,746    | 69,889    | 68,337    |
| Office products and office furniture               | 26,778  | 25,694    | 20,260    | 17,963    | 19,855    |
| Total cost of sales                                | 101,794   | 96,672    | 90,006    | 87,852    | 88,192    |
| <b>Gross profit</b>                                | <b>43,394</b>                                   | 38,253    | 34,396    | 34,331    | 34,692    |
| Selling, general and administrative expense        | 34,018  | 34,797    | 33,058    | 31,175    | 30,619    |
| Hurricane and relocation costs, net of recoveries  | (377)   | 1,021     | -         | -         | -         |
| <b>Income from operations</b>                      | <b>9,753</b>                                    | 2,435     | 1,338     | 3,156     | 4,073     |
| Interest income                                    | 28  | 18        | 7         | 4         | 14        |
| Interest expense                                   | (610)   | (610)     | (301)     | (167)     | (386)     |
| Other income                                       | 32  | 120       | 288       | 10        | 73        |
| <b>Income before income taxes</b>                  | <b>9,203</b>                                    | 1,963     | 1,332     | 3,003     | 3,774     |
| Income tax   | (3,729)   | (846)     | (582)     | (1,235)   | (1,566)   |
| Net income   | \$ 5,474  | \$ 1,117  | \$ 750    | \$ 1,768  | \$ 2,208  |
| <b>Earnings per share:</b>                         |   |           |           |           |           |
| Basic  | \$ 0.56   | \$ 0.11   | \$ 0.08   | \$ 0.18   | \$ 0.23   |
| Diluted  | 0.55  | 0.11      | 0.08      | 0.18      | 0.23      |
| <b>Dividends per share</b>                         | <b>\$ 0.20</b>                                  | \$ 0.20   | \$ 0.20   | \$ 0.20   | \$ 0.20   |
| <b>Weighted average common shares outstanding:</b> |   |           |           |           |           |
| Basic  | 9,818,000                                       | 9,735,000 | 9,729,000 | 9,714,000 | 9,714,000 |
| Diluted  | 9,972,000                                       | 9,809,000 | 9,825,000 | 9,761,000 | 9,726,000 |

(1) During the fourth quarter of 2005, the Company incurred various charges resulting from Hurricane Katrina. As a result of the hurricane, the Company recorded a pre-tax charge of \$1,021,000 or \$581,000 net of tax or \$0.06 per share on a basic and diluted basis. In 2006, the Company recorded recoveries of approximately \$377,000, or \$224,000 net of tax or \$0.02 per share on a basic and diluted basis.



At October 31,

|  | 2006           | 2005     | 2004     | 2003     | 2002     |
|--|----------------|----------|----------|----------|----------|
|  | (In thousands) |          |          |          |          |
| <b>BALANCE SHEET DATA:</b>                             |                |          |          |          |          |
| Cash and cash equivalents                              | \$ 5,487       | \$ 3,662 | \$ 1,745 | \$ 2,172 | \$ 4,507 |
| Working capital  | 25,955         | 26,081   | 26,913   | 26,977   | 26,072   |
| Total assets   | 65,989         | 61,645   | 64,150   | 58,469   | 59,508   |
| Long-term debt (net of current portion) <sup>(1)</sup> | 4,220          | 6,761    | 8,257    | 3,966    | 1,805    |
| Shareholders' equity                                   | 44,777         | 40,752   | 41,551   | 42,691   | 42,866   |

(1) Includes non-current borrowings under the Company's revolving credit facility.

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

### OVERVIEW

The Company is a commercial printer, business forms manufacturer and office products and office furniture supplier in regional markets of the United States of America, east of the Mississippi River. The Company has grown through strategic acquisitions and internal growth. Through such growth, the Company has realized regional economies of scale, operational efficiencies, and exposure of its core products to new markets. The Company has acquired fifteen printing companies, eight office products and office furniture companies, one company with a combined emphasis on both printing and office products and office furniture and a paper distribution division (which was subsequently sold in 2001) since its initial public offering on January 28, 1993.

The Company's net revenues consist primarily of sales of commercial printing, business forms, tags, other printed products, document output solutions including rendering, inserting and mailing, office supplies, office furniture, data products and office design services. The Company recognizes revenues when products are shipped or ownership is transferred and when services are rendered to the customer. The Company's revenues are subject to seasonal fluctuations caused by variations in demand for its products.

The Company's cost of sales primarily consists of raw materials, including paper, ink, pre-press supplies and purchased office supplies, furniture and data products, and manufacturing costs including direct labor, indirect labor and overhead. Significant factors affecting the Company's cost of sales include the costs of paper in both printing and office supplies, the costs of labor and other raw materials.

The Company's operating costs consist of selling, general and administrative expenses. These costs include salaries, commissions and wages for sales, customer service, accounting,



administrative and executive personnel, rent, utilities, legal, audit, information systems equipment costs, software maintenance and depreciation.

### **CRITICAL ACCOUNTING POLICIES INVOLVING SIGNIFICANT ESTIMATES**

The Company's significant accounting policies are described in Note 1 to the consolidated financial statements included in Item 15 of this Form 10-K. The discussion and analysis of the financial statements 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. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosure of contingent assets and liabilities. The following critical accounting policies affect the Company's more significant judgments and estimates used in the preparation of the consolidated financial statements. There can be no assurance that actual results will not differ from those estimates.

*Asset Impairment:* The Company is required to test for asset impairment relating to property and equipment whenever events or changes in circumstances indicate that the carrying value of an asset might not be recoverable. The Company applies Statement of Financial Accounting Standards (SFAS) No. 144, "*Accounting for the Impairment or Disposal of Long-Lived Assets*" (SFAS 144) in order to determine whether or not an asset is impaired. This standard requires an impairment analysis when indicators of impairment are present. If such indicators are present, the standard indicates that if the sum of the future expected cash flows from the Company's asset, undiscounted and without interest charges, is less than the carrying value, an asset impairment must be recognized in the financial statements. The amount of the impairment is the difference between the fair value of the asset and the carrying value of the asset.

The Company believes that the accounting estimate related to an asset impairment is a "critical accounting estimate" because it is highly susceptible to change from period to period because it requires management to make assumptions about future cash flows over future years and that the impact of recognizing an impairment could have a significant effect on operations. Management's assumptions about future cash flows requires significant judgment because actual operating levels have fluctuated in the past and are expected to continue to do so in the future. Management has discussed the development and selection of this critical accounting estimate with the audit committee of our board of directors and the audit committee has reviewed the Company's disclosure relating to it in the MD&A.

Beginning in fiscal year 2002, goodwill and other intangibles are required to be evaluated annually for impairment, according to SFAS No. 142, "*Goodwill and Other Intangible Assets*." (SFAS 142). The standard requires a two-step process be performed to analyze whether or not goodwill has been impaired. Step one is to test for potential impairment and requires that the fair value of the reporting unit be compared to its book value including goodwill and other intangibles. If the fair value is higher than the book value, no impairment is recognized. If the fair value is lower than the book value, a second step must be performed. The second step is to measure the amount of impairment loss, if any, and requires that a hypothetical purchase price allocation be done to determine the implied fair value



of goodwill and other intangibles. This fair value is then compared to the carrying value of goodwill and other intangibles. If the implied fair value is lower than the carrying value, an impairment must be recorded.

As discussed in the notes to the financial statements, goodwill and other intangibles are recorded at the adjusted book value and were analyzed for impairment with the implementation of SFAS 142. The fair value of the Company's goodwill and other intangibles was estimated using discounted cash flow methodologies. Based on the analysis, the Company determined that fair value relating to goodwill and other intangibles resulted in an implied fair value greater than the book value recorded for the corresponding goodwill and other intangibles, and therefore, no impairment was recognized in any period subsequent to the adoption of this statement.

The Company believes that the accounting estimate related to the goodwill and other intangibles impairment is a "critical accounting estimate" because the underlying assumptions used for the discounted cash flow can change from period to period and could potentially cause a material impact to the income statement. Management's assumptions about discount rates, inflation rates and other internal and external economic conditions, such as earnings growth rate, require significant judgment based on fluctuating rates and expected revenues. Additionally, SFAS 142 requires that the goodwill and other intangibles be analyzed for impairment on an annual basis using the assumptions that apply at the time the analysis is updated. Management has discussed the development of these estimates with the audit committee of the board of directors. Additionally, the board of directors has reviewed this disclosure and its relation to MD&A.

*Allowance for Doubtful Accounts:* The Company encounters risks associated with sales and the collection of the associated accounts receivable. As such, the Company records a monthly provision for accounts receivable that are considered to be uncollectible. In order to calculate the appropriate monthly provision, the Company primarily utilizes a historical rate of accounts receivables written off as a percentage of total revenue. This historical rate is applied to the current revenues on a monthly basis. The historical rate is updated periodically based on events that may change the rate such as a significant increase or decrease in collection performance and timing of payments as well as the calculated total exposure in relation to the allowance. Periodically, the Company compares the identified credit risks with the allowance that has been established using historical experience and adjusts the allowance accordingly.

The Company believes that the accounting estimate related to the allowance for doubtful accounts is a "critical accounting estimate" because the underlying assumptions used for the allowance can change from period to period and could potentially cause a material impact to the income statement and working capital. Management has discussed the development and selection of this estimate with the audit committee of the board of directors, and the board has, in turn, reviewed the disclosure and its relation to MD&A.

During 2006, 2005 and 2004, \$979,000, \$421,000 and \$488,000 of bad debt expense was incurred and the allowance for doubtful accounts was \$1,558,000, \$1,410,000 and \$1,422,000 as

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of October 31, 2006, 2005 and 2004. The actual write-offs for the periods were \$832,000, \$407,000 and \$464,000 during 2006, 2005 and 2004. General economic conditions and specific geographic and customer concerns are major factors that may affect the adequacy of the allowance and may result in a change in the annual bad debt expense.

The following discussion and analysis presents the significant changes in the financial position and results of operations of the Company and should be read in conjunction with the Audited Consolidated Financial Statements and notes thereto included elsewhere herein.

## RESULTS OF OPERATIONS

The following table sets forth for the periods indicated information derived from the Company's Consolidated Statements of Operations, including certain information presented as a percentage of total revenues.

|   | Year Ended October 31, |               |                 |               |                |               |
|---|------------------------|---------------|-----------------|---------------|----------------|---------------|
|   | 2006                   |               | 2005            |               | 2004           |               |
|   | (\$ In thousands)      |               |                 |               |                |               |
| <b>Revenues:</b>                                  |                        |               |                 |               |                |               |
| Printing  | \$ 106,414             | 73.3%         | \$ 98,458       | 73.0%         | \$ 95,325      | 76.6%         |
| Office products and office furniture              | 38,774                 | 26.7%         | 36,467          | 27.0%         | 29,077         | 23.4%         |
| <b>Total revenues</b>                             | <b>145,188</b>         | <b>100.0%</b> | <b>134,925</b>  | <b>100.0%</b> | <b>124,402</b> | <b>100.0%</b> |
| <b>Cost of sales:</b>                             |                        |               |                 |               |                |               |
| Printing  | 75,016                 | 51.7%         | 70,978          | 52.6%         | 69,746         | 56.1%         |
| Office products and office furniture              | 26,778                 | 18.4%         | 25,694          | 19.0%         | 20,260         | 16.2%         |
| <b>Total cost of sales</b>                        | <b>101,794</b>         | <b>70.1%</b>  | <b>96,672</b>   | <b>71.6%</b>  | <b>90,006</b>  | <b>72.3%</b>  |
| <b>Gross profit</b>                               | <b>43,394</b>          | <b>29.9%</b>  | <b>38,253</b>   | <b>28.4%</b>  | <b>34,396</b>  | <b>27.7%</b>  |
| Selling, general and administrative expenses      | 34,018                 | 23.5%         | 34,797          | 25.8%         | 33,058         | 26.6%         |
| Hurricane and relocation costs, net of recoveries | (377)                  | -0.3%         | 1,021           | 0.8%          | -              | 0.0%          |
| <b>Income from operations</b>                     | <b>9,753</b>           | <b>6.7%</b>   | <b>2,435</b>    | <b>1.8%</b>   | <b>1,338</b>   | <b>1.1%</b>   |
| <b>Other income (expense):</b>                    |                        |               |                 |               |                |               |
| Interest income                                   | 28                     | 0.0%          | 18              | 0.0%          | 7              | 0.0%          |
| Interest expense                                  | (610)                  | -0.4%         | (610)           | -0.4%         | (301)          | -0.2%         |
| Other income                                      | 32                     | 0.0%          | 120             | 0.1%          | 288            | 0.2%          |
| <b>Income before income taxes</b>                 | <b>9,203</b>           | <b>6.3%</b>   | <b>1,963</b>    | <b>1.5%</b>   | <b>1,332</b>   | <b>1.1%</b>   |
| <b>Income tax expense</b>                         | <b>(3,729)</b>         | <b>-2.5%</b>  | <b>(846)</b>    | <b>-0.7%</b>  | <b>(582)</b>   | <b>-0.5%</b>  |
| <b>Net income</b>                                 | <b>\$ 5,474</b>        | <b>3.8%</b>   | <b>\$ 1,117</b> | <b>0.8%</b>   | <b>\$ 750</b>  | <b>0.6%</b>   |

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The following table is a reconciliation of net income as reported to core net income, which is defined as generally accepted accounting principles (GAAP) net income adjusted for recoveries, net of expenses (Hurricane and relocation expenses), net of tax associated with Hurricane Katrina. The Company believes that events associated with Hurricane Katrina require additional disclosure and therefore, the Company has disclosed additional non-GAAP financial measures in an effort to make the quarterly and annual financial statements more useful to investors.

|  | <b>Three Months Ended October</b> |              | <b>Year Ended October 31,</b> |              |
|--|-----------------------------------|--------------|-------------------------------|--------------|
|  | <b>2006</b>                       | <b>2005</b>  | <b>2006</b>                   | <b>2005</b>  |
| Net income   | \$ 1,973,000                      | \$ 569,000   | \$ 5,474,000                  | \$ 1,117,000 |
| Recoveries, net of<br>expenses (Hurricane and relocation<br>expenses),<br>net of tax | 46,000                            | (581,000)    | 224,000                       | (581,000)    |
| Core net income  | \$ 1,927,000                      | \$ 1,150,000 | \$ 5,250,000                  | \$ 1,698,000 |

**Year Ended October 31, 2006 Compared to Year Ended October 31, 2005**

Revenues

Consolidated net revenues were \$145.2 million for the year ended October 31, 2006 compared to \$134.9 million in the prior fiscal year. This change represents an increase in revenues of approximately \$10.3 million, or 7.6%. Printing revenues increased by \$8.0 million or 8.1% from \$98.5 million in 2005 to \$106.4 million in 2006. The increase in printing sales was primarily due to organic growth since there were no new acquisitions since the fourth quarter of 2004. Office products and office furniture revenue increased \$2.3 million or 6.3% from \$36.5 million in 2005 to \$38.8 million in 2006. The increase in revenues for the office products and office furniture segment was primarily attributable to robust office furniture sales in 2006 compared to 2005.

Cost of Sales

Total cost of sales for the year ended October 31, 2006 totaled \$101.8 million compared to \$96.7 million in the previous year. This change represented an increase of \$5.1 million or 5.3% in cost of sales. Printing cost of sales increased \$4.0 million, or 5.7% to \$75.0 million in 2006 compared to \$71.0 million in 2005. Printing cost of sales was higher due to an overall increase in printing sales. This increase was partially offset with an improved gross margin percentage due to lower material and outside purchase costs as a percentage of sales coupled with improved labor and overhead absorption. Office products and office furniture cost of sales increased \$1.1 million to \$26.8 million in 2006 from \$25.7 million in 2005. The increase in office products and office furniture cost of sales is attributable to an increase in office products and office furniture sales. The decrease in office products and office furniture cost of sales as a percent of office products and office furniture sales is primarily reflective of lower furniture costs as a percent of furniture sales and improvements in wholesale pricing factors at Syscan for office supplies.

Operating Expenses and Income

Selling, general and administrative (S,G&A) expenses decreased \$779,000 to \$34.0 million in 2006 from \$34.8 million in 2005. S,G&A as a percentage of net sales represented 23.5% of net sales in 2006 compared with 25.8% of net sales in 2005. This decrease is primarily related to approximately \$800,000 in legal related costs associated with various legal settlement accruals and expenses, including a \$440,000 settlement related to a Mississippi lawsuit that was present in 2005. The decrease in selling, general and administrative expenses as a percent of sales is primarily a result of higher overall sales coupled with associated cost savings related to personnel adjustments and facility consolidations, as well as the aforementioned legal related costs in 2005 that were not present in 2006.

On August 29, 2005, Hurricane Katrina made landfall and subsequently caused extensive flooding and destruction along the coastal areas of the Gulf of Mexico, including New Orleans and other communities in Louisiana and Mississippi in which Champion conducts business. Operations in many of the Company's markets were disrupted by both the evacuation of large portions of the population as well as damage and/or lack of access to the Company's operating facility in New Orleans.

The Company filed insurance claims related to both actual and contingent losses. The Company received an advance to claim payment from an insurance company of \$300,000 in February 2006 and final settlement claims of \$278,000 in April and May 2006. The Company recorded the \$300,000 payment as an insurance recovery and related receivable at January 31, 2006. The Company recorded additional charges of approximately \$42,000 in the first quarter of 2006 associated with Hurricane Katrina. The Company received a second advance to claim check in April 2006 in the amount of \$200,000 and a full settlement of any and all claims check of \$78,000 in May 2006. The Company recorded the aggregate amount of these checks as an insurance recovery and the \$78,000 as a related receivable at April 30, 2006. The Company incurred additional charges of \$234,000 primarily related to additional inventory valuation reserves and costs associated with relocation in the second quarter of 2006. During the fourth quarter of 2006, the Company successfully negotiated an early lease termination related to its New Orleans location resulting in Katrina related recoveries of approximately \$76,000.

#### Other Income (Expense)

Other expense increased approximately \$78,000 from (\$472,000) in 2005 to (\$550,000) in 2006 due to a reduction in other income of \$89,000. The interest expense was flat on a year to year basis.

#### Income Taxes

Income taxes as a percentage of income before taxes were 40.5% in 2006 compared with 43.1% in 2005. The decrease in income taxes as a percentage of income before taxes is primarily related to improved absorption regarding the nondeductibility of certain selling related expenses.

The effective income tax rate in 2006 and 2005 approximates the combined federal and state, net of federal benefit, statutory income tax rate.

#### Net Income

For reasons set forth above, net income for 2006 increased approximately \$4.4 million to \$5.5 million, or \$0.56 per share on a basic and \$0.55 per share on a diluted basis, from net income of \$1.1 million for 2005, or \$0.11 per share on a basic and diluted basis.

### **Year Ended October 31, 2005 Compared to Year Ended October 31, 2004**

#### Revenues

Consolidated net revenues were \$134.9 million for the year ended October 31, 2005 compared to \$124.4 million in the prior fiscal year. This change represents an increase in revenues of approximately \$10.5 million, or 8.5%. Printing revenues increased by \$3.1 million or 3.3% from \$95.3 million in 2004 to \$98.5 million in 2005.

The increase in printing sales was primarily due to the acquisition of Syscan, of which a full years results were reflected in 2005 compared with two months of sales from the Syscan acquisition in 2004. Office products and office furniture revenue increased \$7.4 million or 25.4% from \$29.1 million in 2004 to \$36.5 million in 2005. The increase in revenues for the office products and office furniture segment was primarily attributable to a full years sales in 2005 for Syscan compared with two months of sales from the Syscan acquisition in 2004.

### Cost of Sales

Total cost of sales for the year ended October 31, 2005 totaled \$96.7 million compared to \$90.0 million in the previous year. This change represented an increase of \$6.7 million or 7.4% in cost of sales. Printing cost of sales increased \$1.2 million, or 1.8% to \$71.0 million in 2005 compared to \$69.7 million in 2004. Printing cost of sales were higher due to an overall increase in printing sales. This increase was partially offset with an improved gross margin percent due to lower material and outside purchase costs as a percentage of sales coupled with improved labor and overhead absorption. Office products and office furniture cost of sales increased \$5.4 million to \$25.7 million in 2005 from \$20.3 million in 2004. The increase in office products and office furniture cost of sales is attributable to an increase in office products and office furniture sales. The increase in office products and office furniture cost of sales as a percent of sales is also reflective of higher furniture costs as a percent of furniture sales and wholesale pricing factors at Syscan for office supplies.

### Operating Expenses and Income

Selling, general and administrative (S,G&A) expenses increased \$1.7 million to \$34.8 million in 2005 from \$33.1 million in 2004. S,G&A as a percentage of net sales represented 25.8% of net sales in 2005 compared with 26.6% of net sales in 2004. This increase is primarily related to the Syscan acquisition reflecting a full year of expenses in 2005 compared with two months of expenses in 2004 and approximately \$800,000 in legal related costs associated with various legal settlement accruals and expenses, including a \$440,000 settlement related to a Mississippi lawsuit. The decrease in selling, general and administrative expenses as a percent of sales is a result of personnel reductions at several divisions resulting in lower personnel costs as a percent of sales.

On August 29, 2005, Hurricane Katrina made landfall and subsequently caused extensive flooding and destruction along the coastal areas of the Gulf of Mexico, including New Orleans and other communities in Louisiana and Mississippi in which Champion conducts business. Operations in many of the Company's markets were disrupted by both the evacuation of large portions of the population as well as damage and/or lack of access to the Company's operating facility in New Orleans. The Company's production operations were relocated from the New Orleans facility to the Baton Rouge facility in the fourth quarter of 2005.

The Company has filed insurance claims related to both actual and contingent losses. However, the Company to date has received no insurance funds or any indication of the amount the insurance companies are willing to pay related to such claims. Therefore, the Company has recorded no insurance related receivables.

As a result of Hurricane Katrina, the Company incurred charges of approximately \$1.0 million during the fourth quarter of 2005. These charges were primarily a result of facilities related costs, equipment costs, operational costs from lost business and uncollectible receivables, personnel costs, inventory related costs and relocation related costs as a result of the Hurricane.

The Company is currently unable to accurately assess the long term effects of Hurricane Katrina on its business and on the macro operating environment in the Gulf States in which the Company operates. (See Management's Discussion and Analysis of Financial Condition and Results of Operations for the Year Ended October 31, 2006 Compared to Year Ended October 31, 2005 for an update regarding Hurricane Katrina.)

Other Income (Expense)

Other expense increased approximately \$466,000 from (\$6,000) in 2004 to (\$472,000) in 2005, due to lower other income primarily related to the gains on the sale of two buildings during 2004 and a casualty gain resulting from a roof collapse at one division in 2004. Interest expense increased \$310,000 primarily as a result of an increase in interest rates and higher outstanding borrowings.

Income Taxes

Income taxes as a percentage of income before taxes were 43.1% in 2005 compared with 43.7% in 2004. The decrease in income taxes as a percentage of income before taxes is primarily related to lower nondeductible selling related expenses as a percentage of pre-tax income.

The effective income tax rate in 2005 and 2004 approximates the combined federal and state, net of federal benefit, statutory income tax rate.

Net Income

For reasons set forth above, net income for 2005 increased approximately \$400,000 to \$1.1 million, or \$0.11 per share on a basic and diluted basis, from net income of \$750,000 for 2004, or \$0.08 per share on a basic and diluted basis.

**LIQUIDITY AND CAPITAL RESOURCES**

As of October 31, 2006, the Company had \$5.5 million of cash and cash equivalents, an increase of \$1.8 million from the prior year. Working capital as of October 31, 2006 was \$26.0 million, a 0.5% decrease from \$26.1 million at October 31, 2005.

The Company has historically used cash generated from operating activities and debt to finance capital expenditures and the cash portion of the purchase price of acquisitions. Management plans to continue making significant investments in equipment and to seek appropriate acquisition candidates. However, to fund the Company's continued expansion of operations, additional financing may be necessary. The Company has two available lines of credit totaling \$11.0 million (See Note 3 of the Consolidated Financial Statements). For the foreseeable future including through Fiscal 2007, management believes it can fund operations, meet debt service requirements and make the planned capital expenditures based on the available cash and cash equivalents, cash flow from operations and lines of credit.

Additionally, the Company has minimal amounts of future contracted obligations (See Note 3 and Note 6 of the Consolidated Financial Statements). The Company is not a guarantor of indebtedness of others. The Company's off balance sheet arrangements at October 31, 2006 relate to the Syscan acquisition and are associated with a put option from Williams Land Corporation to sell a building to the Company for \$1.5 million. This option may be exercised no later than 60 days prior to the end of the lease and closing of said purchase cannot exceed 45 days from the end of the lease.

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As of October 31, 2006, the Company had contractual obligations in the form of leases, debt, contingent acquisition payment and equipment purchase obligations as follows:

| Contractual Obligations               | Payments Due by Fiscal Year |              |              |              |            | Total         |
|---------------------------------------|-----------------------------|--------------|--------------|--------------|------------|---------------|
|                                       | 2007                        | 2008         | 2009         | 2010         | 2011       |               |
| Non-cancelable operating leases       | \$ 1,124,779                | \$ 890,647   | \$ 517,666   | \$ 255,056   | \$ 157,042 | \$ 2,945,190  |
| Term debt                             | 1,614,861                   | 1,091,699    | 971,460      | 1,733,354    | 423,211    | 5,834,585     |
| Equipment purchase obligations        | 1,565,000                   | -            | -            | -            | -          | 1,565,000     |
| Contingent purchase price acquisition | 1,350,725                   | -            | -            | -            | -          | 1,350,725     |
|                                       | \$ 5,655,365                | \$ 1,982,346 | \$ 1,489,126 | \$ 1,988,410 | \$ 580,253 | \$ 11,695,500 |

The Company entered into a purchase commitment for a printing press with a manufacturer for \$1,850,000. As a result of this commitment, the Company paid this manufacturer a deposit of \$185,000 and received an associated trade-in allowance of \$100,000 as of October 31, 2006.

Cash Flows from Operating Activities

Cash flows from operating activities for the years ended October 31, 2006, 2005 and 2004 were \$10.2 million, \$8.3 million and \$4.8 million. The increase in cash flows from operating activities for the fiscal year 2006 compared to 2005 was primarily reflective of additional cash generated in 2006 from higher net income. The cash flow increase from operating activities for the fiscal year 2005 compared to 2004 was reflective of additional cash generated in 2005 from changes in assets and liabilities, increased depreciation and amortization expense and higher net income.

Cash Flows from Investing Activities

Cash used in investing activities was (\$3.0) million, (\$2.7) million and (\$7.5) million for the years ended October 31, 2006, 2005 and 2004. Cash flows used in investing activities increased slightly in 2006 compared to 2005 due to higher capital expenditures. Cash flows used in investing activities decreased in 2005 compared to 2004 due to lower capital expenditures and no acquisitions in 2005.

Cash Flows from Financing Activities

Net cash flows (used in) and provided by financing activities for the years ended October 31, 2006, 2005 and 2004 were (\$5.4) million, (\$3.7) million and \$2.2 million. During 2006, the Company reduced net borrowings by approximately \$2.6 million and, after adjusting for non-cash investing and financing activities, reduced net borrowings by \$3.9 million. This coupled with dividend payments of \$2.0 million, partially offset by stock option proceeds, was reflective of net cash used in financing activities during 2006. During 2005, the Company reduced net borrowings by approximately \$1.5 million thus coupled with dividend payments of \$1.9 million was reflective of net cash used in financing activities during 2005. During 2004, net borrowings exceeded cash payments thus generating



cash flow from financing activities. Dividends paid in 2006 were \$2.0 million and \$1.9 million per year in 2005 and 2004.

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## **INFLATION AND ECONOMIC CONDITIONS**

Management believes that the effect of inflation on the Company's operations has not been material and will continue to be immaterial for the foreseeable future. The Company does not have long-term contracts; therefore, to the extent permitted by competition, it has the ability to pass through to its customers most cost increases resulting from inflation, if any. In addition, the Company is not particularly energy dependent; therefore, an increase in energy costs should not have a significant impact on the Company.

## **SEASONALITY**

Historically, the Company has experienced a greater portion of its profitability in the second and fourth quarters than in the first and third quarters. The second quarter generally reflects increased orders for printing of corporate annual reports and proxy statements. A post-Labor Day increase in demand for printing services and office products coincides with the Company's fourth quarter.

## **NEWLY ISSUED ACCOUNTING STANDARDS**

### **SAB 108**

In September 2006, the SEC Staff issued Staff Accounting Bulletin (SAB) No. 108, *“Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements”* (SAB 108). SAB 108 was issued in order to eliminate the diversity of practice surrounding how public companies quantify financial statement misstatements.

Traditionally, there have been two widely-recognized methods for quantifying the effects of financial statement misstatements: the “rollover” method and the “iron curtain” method. The rollover method focuses primarily on the impact of a misstatement on the income statement-including the reversing effect of prior year misstatements- but its use can lead to the accumulation of misstatements in the balance sheet. The iron curtain method, on the other hand, focuses primarily on the effect of correcting the period-end balance sheet with less emphasis on the reversing effects of prior year errors on the income statement. We currently use the rollover method for quantifying identified financial statement misstatements.

In SAB 108, the SEC Staff established an approach that requires quantification of financial statement misstatements based on the effects of the misstatements on each of the Company's financial statements and the related financial statement disclosures. This model is commonly referred to as a “dual approach” because it requires quantification of errors under both the iron curtain and the rollover methods.

SAB 108 permits existing public companies to initially apply its provisions by (i) restating prior financial statements as if the “dual approach” had always been used or (ii) recording the cumulative effect of initially applying the “dual approach” as adjustments to the carrying value of assets and liabilities as of November 1, 2006 with an offsetting adjustment recorded to the opening balance of retained earnings. Use of the “cumulative effect” transition method requires detailed disclosure of the nature and amount of each individual error being corrected through the cumulative adjustment and how and when it arose.

We will initially apply the provisions of SAB 108 using the cumulative effect transition method in connection with the preparation of our annual financial statements for the year ending October 31, 2007. When we initially apply the provisions of SAB 108, we currently anticipate an increase in fixed assets of approximately \$95,000, an increase in accounts receivable of approximately \$101,000, a decrease in accrued payroll of approximately \$215,000, a decrease in accrued professional fees of approximately \$83,000 and an increase in retained earnings of approximately \$294,000, net of tax, as of November 1, 2006 . The accompanying financial statements do not reflect these

adjustments.

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**FIN 48**

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48 (FIN 48), this interpretation clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109, *"Accounting for Income Taxes"* (SFAS 109). This interpretation is effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the impact of this standard on the financial statements.

**EITF 06-3**

In June 2006, the FASB Emerging Issues Tax Force (EITF) issued EITF 06-3 *"How Sales Taxes Collected from Customers and Remitted to Governmental Authorities Should be Presented in the Income Statement"* (That is, Gross Versus Net Presentation) to clarify diversity in practice on the presentation of different types of taxes in the financial statements. The task force concluded that, for taxes within the scope of the issue, a company may adopt a policy of presenting taxes either gross within revenue or net. That is, it may include charges to customers for taxes within revenues and the charges for the taxes from the taxing authority within cost of sales, or alternatively, it may net the charge to the customer and the charge from the taxing authority. If taxes subject to EITF 06-3 are significant, a company is required to disclose its accounting policy for presenting taxes and the amounts of such taxes that are recognized on a gross basis. The guidance in this consensus is effective for the first interim reporting period beginning after December 15, 2006 (the second quarter of our fiscal year 2007). We do not expect the adoption of EITF 06-3 to have a material impact on our results of operations, financial position or cash flows.

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**ITEM 7A - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The Company does not have any significant exposure relating to market risk.

**ITEM 8 - FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

The financial statements and other information required by this Item are contained in the financial statements and footnotes thereto included in Item 15 and listed in the index on page F-1 of this report.

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

There were none.

**ITEM 9A - CONTROLS AND PROCEDURES**

Company management, including the Chief Executive Officer, Chief Operating Officer and Chief Financial Officer, has conducted an evaluation of the effectiveness of disclosure controls and procedures pursuant to Exchange Act Rule 13a-15c as of the end of the period covered by this annual report. Based on that evaluation, the Chief Executive Officer, Chief Operating Officer and Chief Financial Officer concluded that the disclosure controls and procedures are effective in ensuring that all material information required to be filed in this annual report has been made known to them in a timely fashion. There were no changes in internal controls over financial reporting during the fourth fiscal quarter that have materially affected or are reasonably likely to materially affect the Company's internal controls over financial reporting.

## **PART III**

### **ITEM 10 - DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT**

Information relating to the directors of the Company is contained under the captions “Elections of Directors”, “Director Meetings, Committees and Attendance”, “Section 16a Beneficial Ownership Reporting Compliance” and “Code of Ethics” in the Company’s definitive Proxy Statement, expected to be dated February 19, 2007, with respect to the Annual Meeting of Shareholders to be held on March 19, 2007, which will be filed pursuant to regulation 14(a) of the Securities Exchange Act of 1934 and which is incorporated herein by reference. Certain information concerning executive officers of the Company appear in “EXECUTIVE OFFICERS OF CHAMPION” at Part I of this report.

### **ITEM 11 - EXECUTIVE COMPENSATION**

The information called for by this Item is contained under the captions “Compensation of Directors and Officers”, “Compensation Committee Report on Executive Compensation” and “Stock Performance Graph” in the Company’s definitive Proxy Statement, expected to be dated February 19, 2007, with respect to the Annual Meeting of Shareholders to be held on March 19, 2007, which will be filed pursuant to regulation 14(a) of the Securities Exchange Act of 1934 and which is incorporated herein by reference.

### **ITEM 12 - SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

The information called for by this Item is contained under the captions “Equity Compensation Plan Information” and “Ownership of Shares” in the Company’s definitive Proxy Statement, expected to be dated February 19, 2007, with respect to the Annual Meeting of Shareholders to be held on March 19, 2007, which will be filed pursuant to regulation 14(a) of the Securities Exchange Act of 1934 and which is incorporated herein by reference.

### **ITEM 13 - CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS**

The information called for by this Item is contained under the caption “Transactions with Directors, Officers and Principal Shareholders” in the Company’s definitive Proxy Statement, expected to be dated February 19, 2007, with respect to the Annual Meeting of Shareholders to be held on March 19, 2007, which will be filed pursuant to regulation 14(a) of the Securities Exchange Act of 1934 and which is incorporated herein by reference.

### **ITEM 14 - PRINCIPAL ACCOUNTANT FEES AND SERVICES**

The information called for by this Item is contained under the caption “Independent Accountants” in the Company’s definitive Proxy Statement, expected to be dated February 19, 2007, with respect to the Annual Meeting of Shareholders to be held on March 19, 2007, which will be filed pursuant to regulation 14(a) of the Securities Exchange Act of 1934 and which is incorporated herein by reference.

**PART IV**

**ITEM 15 - EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K**

(a) (1) and (2)

The Consolidated Financial Statements and Schedule, required by Item 8, are listed on the index on page F-1 and included as part of Item 15.

All other Schedules for which provision is made in the applicable accounting regulation of the Securities and Exchange Commission are not required under the related instructions or are inapplicable and therefore have been omitted.

**3. EXHIBITS**

- (2) Plan of Acquisition Stock Purchase Agreement between Company and William G. Williams, Jr., sole shareholder of Syscan Corporation, dated September 7, 2004 filed as Exhibit 2.1 to Form 8-K dated September 7, 2004, filed September 10, 2004, is incorporated herein by reference.
- (3) 3.1 Articles of Incorporation Filed as Exhibit 3.1 to Form 10-Q dated June 16, 1997, filed on June 16, 1997, incorporated herein by reference.
- 3.2 Bylaws Filed as Exhibit 3.2 to Registration Statement on Form S-1, File No. 33-54454, filed on November 10, 1992, incorporated herein by reference.
- (4) Instruments defining the rights of security holders, including debentures. See Exhibit 3.1 above.
- (10) Material Contracts Realty Lease dated January 28, 1993 between ADJ Corp. and Company regarding 2450 1st Avenue, Huntington, West Virginia, filed as Exhibit 10.1 to Form 10-K dated January 27, 1994, filed January 31, 1994, is incorporated herein by reference.

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Realty Lease dated January 28, 1993  
between The Harrah and Reynolds  
Corporation and Company regarding 615  
4th Avenue, Huntington, West Virginia,  
filed as Exhibit 10.2 to Form 10-K dated  
January 27, 1994, filed January 31, 1994,  
is incorporated herein by reference.

Realty Lease dated January 28, 1993  
between ADJ Corp. and Company  
regarding 617-619 4th Avenue,  
Huntington, West Virginia, filed as  
Exhibit 10.3 to Form 10-K dated January  
27, 1994, filed January 31, 1994, is  
incorporated herein by reference.

Realty Lease dated January 28, 1993  
between The Harrah and Reynolds  
Corporation and Company regarding 1945  
5th Avenue, Huntington, West Virginia,  
filed as Exhibit 10.4 to Form 10-K dated  
January 27, 1994, filed January 31, 1994,  
is incorporated herein by reference.

Realty Lease dated January 28, 1993  
between Printing Property Corp. and  
Company regarding 405 Ann Street,  
Parkersburg, West Virginia, filed as  
Exhibit 10.5 to Form 10-K dated January  
27, 1994, filed January 31, 1994, is  
incorporated herein by reference.

Realty Lease dated January 28, 1993  
between Printing Property Corp. and  
Company regarding 890 Russell Cave  
Road, Lexington, filed as Exhibit 10.6 to  
Form 10-K dated January 27, 1994, filed  
January 31, 1994, is incorporated herein  
by reference.

Lease dated April 11, 1994 between Terry  
and Anis Wyatt and Stationers Inc.  
regarding 214 Stone Road, Belpre, Ohio,  
filed as Exhibit 10.1 to Form 10-K dated  
January 26, 1995, filed January 27, 1995,  
is incorporated herein by reference.

Form of Indemnification Agreement  
between Company and all directors and  
executive officers, filed as Exhibit 10.4 to  
Registration Statement on Form S-1, File



No. 33-54454, filed on November 10,  
1992, is incorporated herein by reference.

Executive Compensation Plans and Arrangements      Company's 1993 Stock Option Plan, effective March 22, 1994, filed as Exhibit 10.14 to Form 10-K dated January 27, 1994, filed January 31, 1994, is incorporated herein by reference.

Company's 2003 Stock Option Plan, filed as Exhibit A to proxy statement dated February 12, 2004, filed February 13, 2004, is incorporated herein by reference.

Form of Stock Option Agreement pursuant to Company's 2003 Stock Option Plan filed as Exhibit 10.2 to form 10-Q dated September 10, 2004 filed September 13, 2004, is incorporated herein by reference.

Employment Agreement dated September 7, 2004 among William G. Williams, Jr., Syscan Corporation and the Company, filed as Exhibit 10.1 to Form 8-K dated September 7, 2004, filed September 10, 2004, is incorporated herein by reference.

Confidentiality and Non-Competition Agreement dated September 7, 2004 among William G. Williams, Jr., Syscan Corporation and the Company, filed as Exhibit 10.2 to Form 8-K dated September 7, 2004, filed September 10, 2004, is incorporated herein by reference.

\$10,000,000 revolving credit agreement by and among the Company and its subsidiaries and National City Bank dated as of April 1, 1999, filed as Exhibit 10.2 to Form 10-K dated January 25, 2000, filed January 28, 2000, is incorporated herein by reference.

Lease Agreement dated November 1, 1999 between Randall M. Schulz, successor trustee of The Butterfield Family Trust No. 2 and Smith & Butterfield Co., Inc. regarding 2800 Lynch Road, Evansville, Indiana, filed as Exhibit 10.3 to Form 10-K dated January 25, 2000, filed January 28, 2000, is incorporated herein by reference.



Agreement of Lease dated September 25, 1998 between Ronald H. Scott and Frank J. Scott dba St. Clair Leasing Co. and Interform Corporation, regarding 1901 Mayview Road, Bridgeville, Pennsylvania, filed as Exhibit 10.4 to Form 10-K dated January 25, 2000, filed January 28, 2000, is incorporated herein by reference.

First Amendment of Real Estate Lease Agreement dated May 6, 2003 by and between Ronald H. Scott and Frank J. Scott dba St. Clair Leasing Company and Interform Corporation, filed as Exhibit 10.1 to Form 8-K filed October 4, 2004, is incorporated herein by reference.

\$2,690,938 Business Loan agreement by and among the Company and One Valley Bank National Association (BB&T), dated as of May 6, 1999, together with Promissory Note and Commercial Security Agreement, filed as Exhibit 10.4 to form 10-K dated January 22, 2001, filed January 26, 2001 is incorporated herein by reference.

\$618,720 Promissory Note by and among the Company and Bank One, West Virginia, N.A. dated as of June 6, 2000 together with commercial security agreement, filed as Exhibit 10.5 to form 10-K dated January 22, 2001, filed January 26, 2001, is incorporated herein by reference.

\$550,000 Promissory Note by and among the Company and Bank One, West Virginia, N.A. dated as of August 4, 2000 together with Commercial Security Agreement and Letter of Understanding, filed as Exhibit 10.6 to form 10-K dated January 22, 2001, filed January 26, 2001, is incorporated herein by reference.

Agreement of Lease dated September 1, 2002 between Marion B. and Harold A. Merten, Jr. and The Merten Company regarding 1515 Central Parkway, Cincinnati, Ohio, filed as Exhibit (10.1) to

form 10-K dated January 21, 2002, Filed  
January 25, 2002 is incorporated herein by  
reference.

\$415,000 Commercial Lease Agreement by and among the company and Firststar Equipment Finance dated as of January 12, 2001, Filed as Exhibit (10.2) to form 10-K dated January 21, 2002, filed January 25, 2002 is incorporated herein by reference.

\$450,000 Commercial Lease Agreement by and among the Company and Leasing One Corporation dated as of April 19, 2001, Filed as Exhibit (10.3) to form 10-K dated January 21, 2002, filed January 25, 2002 is incorporated herein by reference.

\$315,665 Promissory Note by and among the Company and Community Trust Bank, N.A. as of April 27, 2001, Filed as Exhibit (10.4) to form 10-K dated January 21, 2002, filed January 25, 2002 is incorporated herein by reference.

Lease Agreement dated February 27, 1991 between the Alfred J. Moran Trust and Docutec of Louisiana, Inc. regarding 7868 Anselmo Lane, Baton Rouge, Louisiana, filed as Exhibit (10.6) to form 10-K dated January 21, 2002, Filed January 25, 2002 is incorporated herein by reference.

Amendment No. 2 to Credit Agreement by and among the Company and its subsidiaries and National City Bank dated as of April 1, 2002 along with Amended and Restated Subsidiaries Guaranty. Filed as Exhibit (10.1) to form 10-K dated January 20, 2003, filed January 24, 2003 is incorporated herein by reference.

Agreement Amending and Extending term of lease dated May 24, 2002 between Earl H. and Elaine D. Seibert and Smith and Butterfield Co., Inc. Filed as Exhibit (10.2) to form 10-K dated January 20, 2003, Filed January 24, 2003 is incorporated herein by reference.

Business Loan Agreement, \$1,440,000 commercial loan between Bourque Printing Company and Hibernia National Bank together with promissory note dated

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as of March 19, 2003, filed as Exhibit 10.1  
to form 10-K dated January 19, 2004 filed  
January 26, 2004, is

incorporated herein by reference.

Commercial Security Agreement, \$450,050 commercial loan between Champion Industries, Inc. and First Century Bank dated as of March 2, 2003, filed as Exhibit 10.2 to form 10-K dated January 19, 2004 filed January 26, 2004, is incorporated herein by reference.

Business Loan Agreement, \$351,000 commercial loan between Champion Industries, Inc. and City National Bank together with promissory note dated as of August 14, 2003, filed as Exhibit 10.3 to form 10-K dated January 19, 2004 filed January 26, 2004, is incorporated herein by reference.

Revolving Credit Agreement, \$10,000,000 revolving line of credit between Champion Industries, Inc. and United Bank, Inc. dated as of August 1, 2003, filed as Exhibit 10.4 to form 10-K dated January 19, 2004 filed January 26, 2004, is incorporated herein by reference.

Agreement Amending and Extending term of lease dated May 9, 2003 between Champion Industries, Inc. DBA, Upton Printing and AMB Property, L.P, filed as Exhibit 10.5 to form 10-K dated January 19, 2004 filed January 26, 2004, is incorporated herein by reference.

Agreement Amending and Extending term of lease dated October 1, 2003 between Bourque Printing DBA, Upton Printing and M. Field Gomila Et. Al. , filed as Exhibit 10.6 to form 10-K dated January 19, 2004 filed January 26, 2004, is incorporated herein by reference.

Promissory Note, \$122,500 between Champion Industries, Inc. and Community Trust Bank dated as of January 9, 2003, filed as Exhibit 10.7 to form 10-K dated January 19, 2004 filed January 26, 2004, is incorporated herein by reference.





Agreement of Lease dated as of September 1, 2004, between Williams Land Corporation and Syscan Corporation regarding North Hills Drive and Washington Street, Charleston, West Virginia, filed as Exhibit 10.3 to Form 8-K dated September 7, 2004, filed September 10, 2004, is incorporated herein by reference.

Agreement of Lease dated as of September 1, 2004, between Williams Land Corporation and Syscan Corporation regarding 2800 Seventh Avenue, Charleston, West Virginia, filed as Exhibit 10.4 to Form 8-K dated September 7, 2004, filed September 10, 2004, is incorporated herein by reference.

Agreement of Purchase and Sale dated September 7, 2004, between Syscan Corporation and Williams Properties, LLC regarding 811 Virginia Street, East, Charleston, West Virginia, filed as Exhibit 10.5 to Form 8-K dated September 7, 2004, filed September 10, 2004, is incorporated herein by reference.

Exercise of Lease renewal option for 2800 Lynch Road Evansville, Indiana dated as of September 22, 2003, filed as Exhibit 10.1 to form 10-K dated January 17, 2005 filed January 31, 2005, is incorporated herein by reference.

\$1,000,000 Business Loan Agreement and promissory note by and between the Company and Community Trust Bank, N.A. as of March 19, 2004, filed as Exhibit 10.2 to form 10-K dated January 17, 2005 filed January 31, 2005, is incorporated herein by reference.

\$1,000,000 revolving line of credit between Stationers, Inc. and First Sentry Bank dated as of April 7, 2004, filed as Exhibit 10.3 to form 10-K dated January 17, 2005 filed January 31, 2005, is incorporated herein by reference.

\$600,075 term note between Bourque  
Printing, Inc. and First Century Bank  
dated as of September 9, 2004, filed as  
Exhibit 10.4 to form 10-K dated January  
17, 2005 filed January 31, 2005, is

incorporated herein by reference.

\$3,920,000 promissory note and security agreement between Champion Industries, Inc. and United Bank, Inc. dated as of October 26, 2004, filed as Exhibit 10.5 to form 10-K dated January 17, 2005 filed January 31, 2005, is incorporated herein by reference.

Modification letter to promissory note between Bourque Printing and Hibernia National Bank, Inc. dated December 28, 2004, filed as Exhibit 10.6 to form 10-K dated January 17, 2005 filed January 31, 2005, is incorporated herein by reference.

First Amendment to Revolving Credit Agreement between Champion Industries, Inc. and United Bank, Inc. Filed as Exhibit 10.1 to form 8-K dated February 15, 2005, filed February 16, 2005, is incorporated herein by reference.

Release of Claims and Settlement Agreement between Defendants Champion Industries, Inc., Timothy V. Ross and Todd Ross and Plaintiff National Forms and Systems Group, Inc. dated May 6, 2005 filed as Exhibit 10.1 to form 8-K dated May 11, 2005, filed May 11, 2005, is incorporated herein by reference.

Second Amendment to Revolving Credit Agreement between Champion Industries, Inc. and United Bank, Inc. Filed as Exhibit 10.1 to form 8-K dated July 11, 2005, filed July 11, 2005, is incorporated herein by reference.

\$605,095 term note between Champion Industries, Inc. and First Century Bank dated as of July 27, 2005. Filed as Exhibit 10.1 to form 10-Q dated September 9, 2005, filed September 9, 2005, is incorporated herein by reference.

\$1,000,000 revolving line of credit between Stationers, Inc. and First Sentry Bank dated as of October 7, 2005, files as exhibit 10.1 to Form 10-K dated January

16, 2006 filed January 27, 2006, is incorporated herein by reference.

Lease Agreement dated October 31, 2005, between SANS LLC and Champion Industries, Inc. DBA Chapman Printing Company regarding 951 Point Marion Road Morgantown, West Virginia, filed as Exhibit 10.2 to Form 10-K dated January 16, 2006, filed January 27, 2006, is incorporated herein by reference.

Lease Agreement dated June 28, 2006, between White Properties No. II, LLC and Champion Industries, Inc. regarding 120 Hills Plaza Charleston, West Virginia, filed as Exhibit 10.1 to Form 8-K dated July 3, 2006, filed July 3, 2006 is incorporated herein by reference.

- (10.1) \$1,200,000 term note between Champion Industries, Inc. and Community Trust Bank, Inc. dated as of July 28, 2006  
Page Exhibit (10.1)-p1
- (10.2) \$642,831.68 term note between Champion Industries, Inc. and First Bank of Charleston, Inc. dated as of August 30, 2006  
Page Exhibit (10.2)-p1
- (14) Code of Ethics Code of Ethics for the Chief Executive Officer, Chief Operating Officer and Chief Accounting Officer, filed as Exhibit 14 to form 10-K dated January 19, 2004 filed January 26, 2004, is incorporated herein by reference.  
  
Code of Business Conduct and Ethics, filed as Exhibit 14.2 to Form 10-K dated January 19, 2004 filed January 26, 2004, is incorporated herein by reference.
- (16) Letter of Ernst & Young dated February 6, 2004, filed as Exhibit 16 to Form 8-K dated February 9, 2004, filed February 9, 2004, is incorporated herein by reference.
- (21) Subsidiaries of the Registrant Exhibit 21 Page Exhibit 21-p1
- (23.1) Consent of BKD, LLP Exhibit 23.1 Page Exhibit 23.1-p1
- (31.1) Principal Executive Officer Certification Pursuant to Section 302 of the Sarbanes-Oxley act of 2002 - Marshall T. Reynolds Exhibit 31.1 Page Exhibit 31.1-p1
- (31.2) Principal Financial Officer Certification Pursuant to Section 302 of the Sarbanes-Oxley act of 2002 - Todd R. Fry Exhibit 31.2 Page Exhibit 31.2-p1

- |        |   |              |                      |
|--------|---|--------------|----------------------|
| (31.3) | Principal Operating Officer Certification Pursuant to Section 302 of the Sarbanes-Oxley act of 2002 - Toney K. Adkins   | Exhibit 31.3 | Page Exhibit 31.3-p1 |
| (32)   | Marshall T. Reynolds, Todd R. Fry and Toney K. Adkins Certification Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley act of 2002 | Exhibit 32   | Page Exhibit 32-p1   |

(b) Exhibits - Exhibits are filed as a separate section of this report.

(c) Financial Statement Schedules - Filed as separate section on page F-34.

**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.

**Champion Industries, Inc.**

By /s/ Marshall T.  
Reynolds  
Marshall T. Reynolds  
Chief Executive Officer

By /s/ Toney K. Adkins

Toney K. Adkins  
President and Chief Operating  
Officer

By /s/ Todd R. Fry

Todd R. Fry  
Senior Vice President and Chief  
Financial Officer

Date: January 15, 2007



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

| SIGNATURE AND TITLE  | DATE             |
|--|------------------|
| /s/ Lou J. Akers<br>Lou J. Akers, Director                         | January 15, 2007 |
| /s/ Philip E.<br>Cline<br>Philip E. Cline, Director                | January 15, 2007 |
| /s/ Harley F. Mooney,<br>Jr.<br>Harley F. Mooney, Jr.,<br>Director | January 15, 2007 |
| /s/ A. Michael<br>Perry<br>A. Michael Perry, Director              | January 15, 2007 |
| /s/ Marshall T.<br>Reynolds<br>Marshall T. Reynolds,<br>Director   | January 15, 2007 |
| /s/ Neal W.<br>Scaggs<br>Neal W. Scaggs, Director                  | January 15, 2007 |
| /s/ Glenn W. Wilcox,<br>Sr.<br>Glenn W. Wilcox, Sr.,<br>Director   | January 15, 2007 |

**Champion Industries, Inc.**

Audited Consolidated Financial Statements and Schedule

October 31, 2006

**Contents**

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**Report of Independent Registered Public Accounting Firm**

Audit Committee, Board of Directors and Shareholders  
Champion Industries, Inc.  
Huntington, West Virginia

We have audited the accompanying consolidated balance sheets of Champion Industries, Inc. and Subsidiaries (the "Company") as of October 31, 2006 and 2005, and the related consolidated statements of operations, shareholders' equity and cash flows for each of the three years in the period ended October 31, 2006. Our audits also included the financial statement schedule listed in the index at Item 15(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based upon our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain 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 the Company at October 31, 2006 and 2005, and the results of its operations and its cash flows for each of the three years in the period ended October 31, 2006, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ BKD, LLP

Evansville, Indiana  
December 15, 2006

**Champion Industries, Inc. and Subsidiaries**

Consolidated Balance Sheets

|  | <b>October 31,</b>   |               |
|--|----------------------|---------------|
|  | <b>2006</b>          | <b>2005</b>   |
| <b>Assets</b>  |                      |               |
| Current assets:  |                      |               |
| Cash and cash equivalents  | \$ 5,486,577         | \$ 3,661,622  |
| Accounts receivable, net of allowance of \$1,558,000 and \$1,410,000 | 20,638,823           | 19,300,453    |
| Inventories  | <b>10,986,590</b>    | 11,079,726    |
| Other current assets   | <b>618,549</b>       | 629,381       |
| Deferred income tax assets   | <b>1,200,037</b>     | 1,168,526     |
| Total current assets   | <b>38,930,576</b>    | 35,839,708    |
| Property and equipment, at cost:                                     |                      |               |
| Land   | <b>2,023,375</b>     | 2,006,375     |
| Buildings and improvements   | <b>8,731,280</b>     | 8,368,720     |
| Machinery and equipment  | <b>46,757,859</b>    | 43,668,900    |
| Equipment under capital leases                                       | -                    | 426,732       |
| Furniture and fixtures   | <b>3,620,783</b>     | 3,492,535     |
| Vehicles   | <b>3,453,415</b>     | 3,629,268     |
|  | <b>64,586,712</b>    | 61,592,530    |
| Less accumulated depreciation  | <b>(45,541,027)</b>  | (42,894,910)  |
|  | <b>19,045,685</b>    | 18,697,620    |
| Cash surrender value of officers' life insurance                     | <b>1,202,696</b>     | 1,117,484     |
| Goodwill   | <b>3,411,511</b>     | 2,060,786     |
| Other intangibles, net of accumulated amortization                   | <b>3,125,691</b>     | 3,697,368     |
| Other assets   | <b>272,567</b>       | 232,204       |
|  | <b>8,012,465</b>     | 7,107,842     |
| Total assets   | <b>\$ 65,988,726</b> | \$ 61,645,170 |

*See notes to consolidated financial statements.*

**Champion Industries, Inc. and Subsidiaries**

## Consolidated Balance Sheets (continued)

|  | <b>October 31,</b> |               |
|--|--------------------|---------------|
|  | <b>2006</b>        | <b>2005</b>   |
| <b>Liabilities and shareholders' equity</b>  |                    |               |
| Current liabilities:   |                    |               |
| Accounts payable   | \$ 5,763,928       | \$ 3,584,323  |
| Accrued payroll and commissions  | 2,169,878          | 1,714,078     |
| Taxes accrued and withheld   | 1,394,345          | 1,106,910     |
| Accrued income taxes   | 1,107,837          | 681,763       |
| Accrued expenses   | 925,070            | 987,228       |
| Current portion of long-term debt:   |                    |               |
| Notes payable  | 1,614,861          | 1,667,797     |
| Capital lease obligations  | -                  | 16,483        |
| Total current liabilities  | 12,975,919         | 9,758,582     |
| Long-term debt, net of current portion:  |                    |               |
| Line of credit   | -                  | 1,612,000     |
| Notes payable  | 4,219,724          | 5,148,503     |
| Deferred income tax liabilities  | 3,628,014          | 3,984,934     |
| Other liabilities  | 388,384            | 388,930       |
| Total liabilities  | 21,212,041         | 20,892,949    |
| Commitments and contingencies  |                    |               |
| Shareholders' equity:  |                    |               |
| Common stock, \$1 par value, 20,000,000 shares authorized;<br>9,922,913 and 9,745,913 shares issued<br>and outstanding |                    |               |
|  | 9,922,913          | 9,745,913     |
| Additional paid-in capital   | 22,636,620         | 22,297,670    |
| Retained earnings  | 12,217,152         | 8,708,638     |
| Total shareholders' equity   | 44,776,685         | 40,752,221    |
| Total liabilities and shareholders' equity   | \$ 65,988,726      | \$ 61,645,170 |

See notes to consolidated financial statements.

## Champion Industries, Inc. and Subsidiaries

## Consolidated Statements of Operations

|   | Year Ended October 31, |               |               |
|---|------------------------|---------------|---------------|
|   | 2006                   | 2005          | 2004          |
| Revenues:   |                        |               |               |
| Printing  | \$ 106,413,663         | \$ 98,458,017 | \$ 95,324,314 |
| Office products and office furniture              | 38,774,213             | 36,467,219    | 29,077,258    |
| Total revenues                                    | 145,187,876            | 134,925,236   | 124,401,572   |
| Cost of sales:                                    |                        |               |               |
| Printing  | 75,015,978             | 70,978,621    | 69,746,212    |
| Office products and office furniture              | 26,777,539             | 25,693,958    | 20,259,542    |
| Total cost of sales                               | 101,793,517            | 96,672,579    | 90,005,754    |
| Gross profit                                      | 43,394,359             | 38,252,657    | 34,395,818    |
| Selling, general and administrative expenses      |                        |               |               |
|   | 34,018,288             | 34,796,990    | 33,057,699    |
| Hurricane and relocation costs, net of recoveries | (377,276)              | 1,020,999     | -             |
| Income from operations                            | 9,753,347              | 2,434,668     | 1,338,119     |
| Other income (expense):                           |                        |               |               |
| Interest income                                   | 28,251                 | 18,472        | 6,663         |
| Interest expense                                  | (609,881)              | (610,787)     | (300,742)     |
| Other   | 31,694                 | 120,436       | 287,750       |
|   | (549,936)              | (471,879)     | (6,329)       |
| Income before income taxes                        | 9,203,411              | 1,962,789     | 1,331,790     |
| Income tax expense                                | (3,729,563)            | (846,155)     | (582,092)     |
| Net income  | \$ 5,473,848           | \$ 1,116,634  | \$ 749,698    |
| Earnings per share:                               |                        |               |               |
| Basic   | \$ 0.56                | \$ 0.11       | \$ 0.08       |
| Diluted   | 0.55                   | 0.11          | 0.08          |
| Dividends paid per share                          |                        |               |               |
|   | 0.20                   | 0.20          | 0.20          |
| Weighted average shares outstanding:              |                        |               |               |
| Basic   | 9,818,000              | 9,735,000     | 9,729,000     |
| Diluted   | 9,972,000              | 9,809,000     | 9,825,000     |

See notes to consolidated financial statements.



**Champion Industries, Inc. and Subsidiaries**

## Consolidated Statements of Shareholders' Equity

|  | <b>Common Stock<br/>Shares</b> | <b>Common Stock<br/>Amount</b> | <b>Additional<br/>Paid-In<br/>Capital</b> | <b>Retained<br/>Earnings</b> | <b>Total</b>         |
|--|--------------------------------|--------------------------------|---|------------------------------|----------------------|
| Balance, October<br>31, 2003             | 9,713,913                      | \$ 9,713,913                   | \$ 22,242,047                             | \$ 10,734,874                | \$ 42,690,834        |
| Net income for<br>2004                   | -                              | -                              | -   | 749,698                      | 749,698              |
| Dividends (\$0.20<br>per share)          | -                              | -                              | -   | (1,945,783)                  | (1,945,783)          |
| Stock options<br>exercised               | 20,000                         | 20,000                         | 36,063                                    | -                            | 56,063               |
| Balance, October<br>31, 2004             | 9,733,913                      | 9,733,913                      | 22,278,110                                | 9,538,789                    | 41,550,812           |
| Net income for<br>2005                   | -                              | -                              | -   | 1,116,634                    | 1,116,634            |
| Dividends (\$0.20<br>per share)          | -                              | -                              | -   | (1,946,785)                  | (1,946,785)          |
| Stock options<br>exercised               | 12,000                         | 12,000                         | 19,560                                    | -                            | 31,560               |
| Balance, October<br>31, 2005             | 9,745,913                      | 9,745,913                      | 22,297,670                                | 8,708,638                    | 40,752,221           |
| <b>Net income for<br/>2006</b>           | -                              | -                              | -   | <b>5,473,848</b>             | <b>5,473,848</b>     |
| <b>Dividends (\$0.20<br/>per share)</b>  | -                              | -                              | -   | <b>(1,965,334)</b>           | <b>(1,965,334)</b>   |
| <b>Stock options<br/>exercised</b>       | <b>177,000</b>                 | <b>177,000</b>                 | <b>338,950</b>                            | -                            | <b>515,950</b>       |
| <b>Balance,<br/>October 31,<br/>2006</b> | <b>9,922,913</b>               | <b>\$ 9,922,913</b>            | <b>\$ 22,636,620</b>                      | <b>\$ 12,217,152</b>         | <b>\$ 44,776,685</b> |

See notes to consolidated financial statements.



**Champion Industries, Inc. and Subsidiaries**

## Consolidated Statements of Cash Flows

Year Ended October 31,

|   | 2006         | 2005         | 2004         |
|---|--------------|--------------|--------------|
| <b>Cash flows from operating activities:</b>                                  |              |              |              |
| Net income  | \$ 5,473,848 | \$ 1,116,634 | \$ 749,698   |
| Adjustments to reconcile net income to cash provided by operating activities: |              |              |              |
| Depreciation and amortization   | 4,158,748    | 4,696,105    | 4,389,758    |
| Loss (gain) on sale of assets   | 4,409        | (36,516)     | (91,420)     |
| Deferred income taxes   | (388,431)    | (461,308)    | (35,866)     |
| Deferred compensation   | 3,574        | 7,149        | 10,723       |
| Bad debt expense  | 979,089      | 420,673      | 487,550      |
| Hurricane and relocation (recoveries) costs                                   | (377,276)    | 1,020,999    | -            |
| Changes in assets and liabilities:  |              |              |              |
| Accounts receivable   | (2,239,782)  | 1,413,579    | (268,690)    |
| Inventories   | (101,037)    | 135,596      | 473,586      |
| Other current assets  | 10,832       | 344,451      | (4,052)      |
| Accounts payable  | 1,533,189    | (558,876)    | (616,230)    |
| Accrued payroll and commissions   | 455,799      | (64,658)     | 148,799      |
| Taxes accrued and withheld  | 287,435      | (182,614)    | (88,742)     |
| Accrued income taxes  | 426,074      | 546,207      | (501,213)    |
| Accrued expenses  | (62,158)     | (41,018)     | 166,236      |
| Other liabilities   | (4,120)      | (46,585)     | (6,590)      |
| Net cash provided by operating activities                                     | 10,160,193   | 8,309,818    | 4,813,547    |
| <b>Cash flows from investing activities:</b>                                  |              |              |              |
| Purchase of property and equipment  | (2,951,610)  | (2,736,561)  | (4,973,834)  |
| Proceeds from sale of fixed assets  | 135,846      | 301,559      | 850,287      |
| Businesses acquired, net of cash received                                     | -            | -            | (3,034,886)  |
| Goodwill and other intangible additions                                       | -            | (359,648)    | (227,161)    |
| Change in other assets  | (52,362)     | 171,670      | (76,437)     |
| Increase in cash surrender value  | (85,212)     | (77,970)     | (18,719)     |
| Net cash used in investing activities   | (2,953,338)  | (2,700,950)  | (7,480,750)  |
| <b>Cash flows from financing activities:</b>                                  |              |              |              |
| Borrowings on line of credit  | 10,884,000   | 7,719,000    | 8,294,591    |
| Payments on line of credit  | (12,496,000) | (8,407,000)  | (7,581,259)  |
| Proceeds from long-term debt  | 1,091,843    | 605,000      | 5,520,000    |
| Principal payments on long-term debt  | (3,412,359)  | (1,694,478)  | (2,102,665)  |
| Proceeds from exercise of stock options                                       | 515,950      | 31,560       | 56,063       |
| Dividends paid  | (1,965,334)  | (1,946,785)  | (1,945,783)  |
| Net cash (used in) provided by financing activities                           | (5,381,900)  | (3,692,703)  | 2,240,947    |
| Net increase (decrease) in cash and cash equivalents                          | 1,824,955    | 1,916,165    | (426,256)    |
| Cash and cash equivalents at beginning of year                                | 3,661,622    | 1,745,457    | 2,171,713    |
| Cash and cash equivalents at end of year                                      | \$ 5,486,577 | \$ 3,661,622 | \$ 1,745,457 |

See notes to consolidated financial statements.

**Champion Industries, Inc. and Subsidiaries**

Notes to Consolidated Financial Statements

**1. Summary of Significant Accounting Policies**

Champion is a commercial printer, business forms manufacturer and office products and office furniture supplier in regional markets in the United States of America, east of the Mississippi.

The accounting and reporting policies of Champion conform to accounting principles generally accepted in the United States. The preparation of the financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from these estimates. The following is a summary of the more significant accounting and reporting policies.

**Principles of Consolidation**

The accompanying consolidated financial statements of Champion Industries, Inc. and Subsidiaries (the "Company") include the accounts of The Chapman Printing Company, Inc., Bourque Printing, Inc., Dallas Printing Company, Inc., Stationers, Inc., Carolina Cut Sheets, Inc., U.S. Tag & Ticket Company, Inc., Donihe Graphics, Inc., Smith and Butterfield Co., Inc., The Merten Company, Interform Corporation, Blue Ridge Printing Co., Inc., CHMP Leasing, Inc., Rose City Press, Capitol Business Equipment, Inc., Thompson's of Morgantown, Inc., Independent Printing Service, Inc., Diez Business Machines, Transdata Systems, Inc. and Syscan Corporation.

Significant intercompany transactions have been eliminated in consolidation.

**Cash and Cash Equivalents**

Cash and cash equivalents consist principally of cash on deposit with banks, repurchase agreements for government securities and a money market account, all highly liquid investments with an original maturity of three months or less. At October 31, 2006, the Company held overnight repurchase agreements for \$1,487,000 of government securities with stated interest rates of 4.88%. The Company did not have any overnight repurchase agreements at October 31, 2005.

**Accounts Receivable**

Accounts receivable are stated at the amount billed to customers. Accounts receivable are ordinarily due 30 days from the invoice date.

The Company encounters risks associated with sales and the collection of the associated accounts receivable. As such, the Company records a monthly provision for accounts receivable that are considered to be uncollectible. In order to calculate the appropriate monthly provision, the Company primarily utilizes a historical rate of accounts receivable written off as a percentage of total revenue. This historical rate is applied to the current revenues on a monthly basis. The historical rate is updated periodically based on events that may change the rate such as a significant increase or decrease in collection performance and timing of payments as well as the calculated total exposure in relation to the allowance. Periodically, the Company compares

**Champion Industries, Inc. and Subsidiaries**

Notes to Consolidated Financial Statements (continued)

the identified credit risks with the allowance that has been established using historical experience and adjusts the allowance accordingly.

During 2006, 2005 and 2004, \$979,000, \$421,000 and \$488,000 of bad debt expense was incurred and the allowance for doubtful accounts was \$1,558,000, \$1,410,000 and \$1,422,000 as of October 31, 2006, 2005 and 2004. The actual write-offs for the periods were \$832,000, \$407,000 and \$464,000 during 2006, 2005 and 2004. The actual write-offs occur when it is determined an account will not be collected. General economic conditions and specific geographic and customer concerns are major factors that may affect the adequacy of the allowance and may result in a change in the annual bad debt expense.

No individual customer represented greater than 5.00% and 4.00% of the gross outstanding accounts receivable at October 31, 2006 and 2005. The Company's ten largest accounts receivable balances represented 19.85% and 13.64% of gross outstanding accounts receivable at October 31, 2006 and 2005.

**Inventories**

Inventories are principally stated at the lower of first-in, first-out, cost or market. Manufactured finished goods and work-in-process inventories include material, direct labor and overhead based on standard costs, which approximate actual costs.

In November 2004, the FASB issued SFAS No. 151 "*Inventory Costs*" (SFAS 151), an amendment of ARB No. 43, chapter 4. SFAS 151 clarifies the accounting for abnormal amounts of idle facility expense, freight, handling cost and wasted material. SFAS 151 was effective for inventory costs incurred during fiscal years beginning after June 15, 2005. The adoption of this standard did not have a material effect on the Company's financial statements.

**Property and Equipment**

Depreciation of property and equipment and amortization of leasehold improvements and equipment under capital leases are recognized primarily on the straight-line and declining-balance methods in amounts adequate to amortize costs over the estimated useful lives of the assets as follows:

|                            |              |
|----------------------------|--------------|
| Buildings and improvements | 5 - 40 years |
| Machinery and equipment    | 3 - 10 years |
| Furniture and fixtures     | 5 - 10 years |
| Vehicles                   | 3 - 5 years  |

The Company leases certain equipment under financing agreements that are classified as capital leases. These leases are for a term of five years and contain purchase options at the end of the original lease term. Amortization of assets recorded under capital lease agreements is included in depreciation expense.

Major renewals, betterments and replacements are capitalized while maintenance and repair costs are charged to operations as incurred. Upon the sale or disposition of assets, the

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cost and related accumulated depreciation are removed from the accounts with the resulting gains or losses reflected in income. Depreciation expense approximated \$3,786,000, \$4,292,000 and \$4,100,000 for the years ended October 31, 2006, 2005 and 2004.

Long-lived property and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. This evaluation includes the review of operating performance and estimated future undiscounted cash flows of the underlying assets or businesses.

### **Goodwill and Other Intangibles**

The excess cost over fair value of net assets of acquired businesses, goodwill, was in years prior to 2002 being amortized by the straight-line method over periods ranging from 15 to 25 years. The other intangible assets are being amortized over 5 to 20 years representing the future benefit of the intangible.

In June 2001, the FASB issued SFAS No. 141, "*Business Combinations*" (SFAS 141), and SFAS No. 142, "*Goodwill and Other Intangible Assets*" (SFAS 142). The Company adopted these standards with its fiscal year beginning November 1, 2001. Under the new rules, goodwill (and intangible assets deemed to have indefinite lives) is no longer amortized but is subject to annual impairment tests in accordance with SFAS 142 except in the year of adoption where companies were required to evaluate impairment at the beginning of the year and again at a recurring annual date. The first step in the impairment analysis is a screen for potential impairment and was required to be completed within six months of adopting SFAS 142. The second step if required, measures the amount of impairment. The Company completed step one of the initial impairment analysis and the subsequent annual analysis during the second and fourth quarters of 2002. Additionally, this analysis was performed in the fourth quarter of each year thereafter. The application of the requirements of this standard did not result in an impairment charge.

### **Advertising Costs**

Advertising costs are expensed as incurred. Advertising expense for the years ended October 31, 2006, 2005 and 2004 approximated \$647,000, \$617,000, and \$641,000.

### **Income Taxes**

Provisions for income taxes currently payable and deferred income taxes are based on the liability method. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax basis of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. A valuation allowance is established to reduce deferred tax assets if it is more likely than not that a deferred tax asset will not be realized.

**Champion Industries, Inc. and Subsidiaries**

Notes to Consolidated Financial Statements (continued)

**Earnings Per Share**

Basic earnings per share is computed by dividing net income by the weighted average shares of common stock outstanding for the period and excludes any dilutive effects of stock options. Diluted earnings per share is computed by dividing net income by the weighted average shares of common stock outstanding for the period plus the shares that would be outstanding assuming the exercise of dilutive stock options using the treasury stock method. The effect of dilutive stock options increased weighted average shares outstanding by 154,000, 74,000 and 96,000 for the years ended October 31, 2006, 2005 and 2004.

**Segment Information**

The Company designates the internal organization that is used by management for making operating decisions and assessing performance as the source of the Company's reportable segments. The Company's operating segments are more fully described in Note 9.

**Accounting for Web Site Development Costs**

Certain external costs and internal payroll and payroll-related costs have been capitalized during the application, development and implementation stages of the Company's web site. The costs regarding the ongoing operation and maintenance are expensed in the period incurred. The Company's internet sales are based on a cooperative effort with the Company's direct sales force as an optional ordering alternative.

**Revenue Recognition**

Revenues are recognized when products are shipped or ownership is transferred and when services are rendered to customers. The Company acts as a principal party in sales transactions, assumes title to products and assumes the risks and rewards of ownership including risk of loss for collection, delivery or returns. The Company typically recognizes revenue for the majority of its products upon shipment to the customer and transfer of title. Under agreements with certain customers, custom forms may be stored by the Company for future delivery. In these situations, the Company may receive a logistics and warehouse management fee for the services provided. In these cases, delivery and bill schedules are outlined with the customer and product revenue is recognized when manufacturing is complete and the product is received into the warehouse, title transfers to the customer, the order is invoiced and there is reasonable assurance of collectibility. Since the majority of products are customized, product returns are not significant. Therefore, the Company records sales on a gross basis. Shipping and handling costs are recorded as a component of cost of sales.

**Accounting for Costs Associated with Exit or Disposal Activities**

In July 2002, the FASB issued SFAS No. 146 "*Accounting for Costs Associated with Exit or Disposal Activities*" (SFAS 146), which supersedes EITF No. 94-3, "*Liability Recognition for Certain Employment Termination Benefits and Other Costs to Exit an Activity.*" SFAS 146 requires companies to record liabilities for costs associated

**Champion Industries, Inc. and Subsidiaries**

Notes to Consolidated Financial Statements (continued)

with exit or disposal activities to be recognized only when the liability is incurred instead of at the date of commitment to an exit or disposal activity. Adoption of this standard was effective for exit or disposal activities that were initiated after December 31, 2002. During the second quarter of 2004, the Company recognized costs associated with facility consolidations of approximately \$150,000 and personnel severance related costs of approximately \$37,000. During the fourth quarter of 2005, the Company recognized costs associated with facility related costs, equipment costs, operational costs from lost business and uncollectible receivables, personnel costs, inventory related costs and relocation costs aggregating approximately \$1.0 million associated with Hurricane Katrina. In 2006, the Company recognized recoveries, net of expenses associated with Hurricane Katrina of approximately \$377,000.

**Accounting for Stock-Based Compensation**

In December 2004, the FASB issued SFAS No. 123R (revised 2004), "*Share-Based Payment*" (SFAS 123R). This statement revises SFAS No. 123, "*Accounting for Stock-Based Compensation*," (SFAS 123) and requires companies to expense the value of employee stock options and similar awards. The effective date of this standard was interim and annual periods beginning after June 15, 2005. On April 14, 2005, the United States Securities and Exchange Commission amended the effective date of this standard to the beginning of a company's fiscal year that begins after June 15, 2005. Therefore, the effective date of this standard for the Company was November 1, 2005. Since the Company's employee stock options vest immediately in the year granted, the initial adoption of this standard did not have any affect on the Company's financial statements. However, the Company will be required to expense the value of the employee stock options when future options are granted. There were no stock option grants in 2006.

Before the adoption of SFAS 123R, the Company has elected to followed the intrinsic value method in accounting for its employee stock options. Accordingly, because the exercise price of the Company's employee stock options equals the market price of the underlying stock on the date of grant, no compensation expense was recognized.

The fair value of these options was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted-average assumptions for 2005 and 2004 respectively: risk-free interest rates of 4.34% and 4.03%; dividend yields of 4.72% and 4.21%; volatility factors of the expected market price of the Company's common stock of 45.1% and 54.0%; and a weighted-average expected life of the option of 4 years.

**Champion Industries, Inc. and Subsidiaries**

## Notes to Consolidated Financial Statements (continued)

The following pro forma information has been determined as if the Company had accounted for its employee stock options under the fair value method. For purposes of pro forma disclosures, the estimated fair value of the options was expensed in the year granted since the options vested immediately. The Company's pro forma information for the years ended October 31 are as follows:

|   | <b>Year Ended October 31,</b> |              |             |
|---|-------------------------------|--------------|-------------|
|   | <b>2006 (1)</b>               | <b>2005</b>  | <b>2004</b> |
| Net income as reported  | \$ 5,473,848                  | \$ 1,116,634 | \$ 749,698  |
| Deduct: Total stock-based employee compensation expense determined under the fair value method for all awards, net of related tax effects | -                             | 296,400      | 183,270     |
| Pro forma net income  | \$ 5,473,848                  | \$ 820,234   | \$ 566,428  |
| Earnings per share:   |                               |              |             |
| Basic, as reported  | \$ 0.56                       | \$ 0.11      | \$ 0.08     |
| Basic, pro forma  | \$ 0.56                       | \$ 0.08      | \$ 0.06     |
| Diluted, as reported  | \$ 0.55                       | \$ 0.11      | \$ 0.08     |
| Diluted, pro forma  | \$ 0.55                       | \$ 0.08      | \$ 0.06     |

(1) Not applicable, since the Company adopted SFAS 123R on November 1, 2005 and there were no stock options granted during 2006.

**SAB 108**

In September 2006, the SEC Staff issued SAB No. 108, *“Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements”* (SAB 108). SAB 108 was issued in order to eliminate the diversity of practice surrounding how public companies quantify financial statement misstatements.

Traditionally, there have been two widely-recognized methods for quantifying the effects of financial statement misstatements: the “rollover” method and the “iron curtain” method. The rollover method focuses primarily on the impact of a misstatement on the income statement-including the reversing effect of prior year misstatements- but its use can lead to the accumulation of misstatements in the balance sheet. The iron curtain method, on the other hand, focuses primarily on the effect of correcting the period-end balance sheet with less emphasis on the reversing effects of prior year errors on the income statement. We currently use the rollover method for quantifying identified financial statement misstatements.

In SAB 108, the SEC Staff established an approach that requires quantification of financial statement misstatements based on the effects of the misstatements on each of the company’s financial statements and the related financial statement disclosures. This model is commonly referred to as a “dual approach” because it requires quantification of errors under both the iron curtain and the rollover methods.



SAB 108 permits existing public companies to initially apply its provisions by (i) restating prior financial statements as if the “dual approach” had always been used or (ii) recording the cumulative effect of initially applying the “dual approach” as adjustments to the carrying value of assets and liabilities as of November 1, 2006, with an offsetting adjustment recorded to the opening balance of retained earnings. Use of the “cumulative effect” transition method requires detailed disclosure of the nature and amount of each individual error being corrected through the cumulative adjustment and how and when it arose.

We will initially apply the provisions of SAB 108 using the cumulative effect transition method in connection with the preparation of our annual financial statements for the year ending October 31, 2007. When we initially apply the provisions of SAB 108, we currently anticipate an increase in fixed assets of approximately \$95,000, an increase in accounts receivable of approximately \$101,000, a decrease in accrued payroll of approximately \$215,000, a decrease in accrued professional fees of approximately \$83,000 and an increase in retained earnings of approximately \$294,000, net of tax, as of November 1, 2006. The accompanying financial statements do not reflect these adjustments.

#### FIN 48

In June 2006, the FASB issued FASB Interpretation No. 48 (FIN 48), this interpretation clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109, "Accounting for Income Taxes" (SFAS 109). This interpretation is effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the impact of this standard on the financial statements.

#### EITF 06-3

In June 2006, the FASB Emerging Issues Tax Force (EITF) issued EITF 06-3 "How Sales Taxes Collected from Customers and Remitted to Governmental Authorities Should be Presented in the Income Statement" (That is, Gross Versus Net Presentation) to clarify diversity in practice on the presentation of different types of taxes in the financial statements. The task force concluded that, for taxes within the scope of the issue, a company may adopt a policy of presenting taxes either gross within revenue or net. That is, it may include charges to customers for taxes within revenues and the charges for the taxes from the taxing authority within cost of sales, or alternatively, it may net the charge to the customer and the charge from the taxing authority. If taxes subject to EITF 06-3 are significant, a company is required to disclose its accounting policy for presenting taxes and the amounts of such taxes that are recognized on a gross basis. The guidance in this consensus is effective for the first interim reporting period beginning after December 15, 2006 (the second quarter of our fiscal year 2007). We do not expect the adoption of EITF 06-3 to have a material impact on our results of operations, financial position or cash flow.

#### Reclassifications

Certain prior-year amounts have been reclassified to conform to the current year financial statement presentation.

#### 2. Inventories

Inventories consisted of the following:

|                                      | <b>October 31,</b> |               |
|--------------------------------------|--------------------|---------------|
|                                      | <b>2006</b>        | <b>2005</b>   |
| Printing:                            |                    |               |
| Raw materials                        | \$ 2,121,843       | \$ 2,198,882  |
| Work in process                      | 1,800,517          | 1,766,862     |
| Finished goods                       | 4,404,162          | 4,013,041     |
| Office products and office furniture | 2,660,068          | 3,100,941     |
|                                      | \$ 10,986,590      | \$ 11,079,726 |

**Champion Industries, Inc. and Subsidiaries**

## Notes to Consolidated Financial Statements (continued)

**3. Long-term Debt**

Long-term debt consisted of the following:

|   | <b>October 31,</b>  |                     |
|---|---------------------|---------------------|
|   | <b>2006</b>         | <b>2005</b>         |
| Secured term note payable to a bank, due in monthly principal and interest installments approximating \$53,633 at October 31, 2006 and \$93,279 at October 31, 2005 with interest at the Wall Street Journal prime rate maturing October 2008, collateralized by substantially all assets of the Syscan Corporation and the Chapman Printing Charleston division. | \$ 452,386          | \$ 3,024,861        |
| Installment notes payable to banks, due in monthly installments plus interest at rates approximating the bank's prime rate maturing in various periods ranging from April 2008 - September 2011, collateralized by equipment, vehicles, inventory and accounts receivable.  | 5,382,199           | 3,791,439           |
| Capital lease obligations, due in monthly installments totaling \$8,322 through December 2005 at a fixed rate of interest of 7.0%.  | -                   | 16,483              |
|   | <b>5,834,585</b>    | <b>6,832,783</b>    |
| Less current portion  | <b>1,614,861</b>    | <b>1,684,280</b>    |
| Long-term debt, net of current portion  | <b>\$ 4,219,724</b> | <b>\$ 5,148,503</b> |

The unsecured term note agreements contain restrictive financial covenants requiring the Company to maintain certain financial ratios. The Company was in compliance with these covenants at October 31, 2006.

Maturities of long-term debt for each of the next five years follow:

|             |              |
|-------------|--------------|
| <b>2007</b> | \$ 1,614,861 |
| <b>2008</b> | 1,091,699    |
| <b>2009</b> | 971,460      |
| <b>2010</b> | 1,733,354    |
| <b>2011</b> | 423,211      |
|             | \$ 5,834,585 |

**Champion Industries, Inc. and Subsidiaries**

Notes to Consolidated Financial Statements (continued)

On August 1, 2003, the Company obtained an unsecured revolving line of credit with a bank for borrowings to a maximum of \$10,000,000 with interest payable monthly at the prime rate of interest. The line of credit expires in July 2008 and contains certain restrictive financial covenants. The line of credit essentially replaced a previous \$10,000,000 facility with another bank. The Company had outstanding borrowings of approximately \$0 and \$1.6 million under this facility at October 31, 2006 and 2005.

The Company has an unsecured revolving line of credit with a bank for borrowings to a maximum of \$1,000,000 with interest payable monthly at the Wall Street Journal prime rate. The line of credit expires in April 2007 and contains certain financial covenants. There were no borrowings outstanding under this facility at October 31, 2006 or 2005.

In December 2006, the Company entered into a \$1,351,225 five year term debt agreement with a bank with interest at prime rate.

The prime rate, the base interest rate on the above loans, approximated 8.25% and 6.75% at October 31, 2006 and 2005. Interest paid during the years ended October 31, 2006, 2005 and 2004 approximated \$616,000, \$615,000 and \$320,000. The Company capitalized interest of \$19,000 during fiscal 2004 related to the purchase of a building in Baton Rouge, Louisiana.

The Company's non-cash activities for 2006, 2005 and 2004 included equipment purchases of approximately \$1,322,000, \$277,000 and \$0, which were financed by a bank and the accrual for the contingent earn out payment to Syscan of \$1,350,725 in 2006.

#### **4. Employee Benefit Plans**

The Company had a Profit Sharing Plan that covered all eligible employees and qualified as a Savings Plan under Section 401(k) of the Internal Revenue Code. Effective January 1, 1998, the Profit Sharing Plan was merged into The Champion Industries, Inc. 401(k) Plan (the "Plan"). The Plan covers all eligible employees who satisfy the age and service requirements. Each participant may elect to contribute up to 15% of annual compensation and the Company is obligated to contribute 100% of the participant's contribution not to exceed 2% of the participant's annual compensation. The Company may make discretionary contributions to the Plan. The Company's expense under these Plans was approximately \$437,000, \$447,000 and \$383,000 for the years ended October 31, 2006, 2005 and 2004.

The Company's accrued vacation liability as of October 31, 2006 and 2005 was approximately \$605,000 and \$668,000. This item is classified as a component of accrued expenses on the financial statements.

The Company's 1993 Stock Option Plan provides for the granting of both incentive and non-qualified stock options to management personnel for up to 762,939 shares of the Company's common stock. In March 2004, the Company's 2003 stock option plan was adopted to provide for the granting of both incentive and non-qualified stock options to management personnel for up to 475,000 shares of the Company's common stock.

**Champion Industries, Inc. and Subsidiaries**

## Notes to Consolidated Financial Statements (continued)

The option price per share for incentive stock options shall not be lower than the fair market value of the common stock at the date of grant. The option price per share for non-qualified stock options shall be at such price as the Compensation Committee of the Board of Directors may determine at its sole discretion. All options to date are incentive stock options. Exercise prices for options outstanding as of October 31, 2006 ranged from \$2.49 to \$4.29. Options vest immediately and may be exercised within five years from the date of grant. The weighted average remaining contractual life of those options is 3.00 years.

A summary of the Company's stock option activity and related information for the years ended October 31 follows:

|  | <b>2006</b> | <b>Weighted<br/>Average<br/>Exercise<br/>Price</b> | <b>2005</b> | <b>Weighted<br/>Average<br/>Exercise<br/>Price</b> | <b>2004</b> | <b>Weighted<br/>Average<br/>Exercise<br/>Price</b> |
|--|-------------|--|-------------|--|-------------|--|
| Outstanding-beginning of year                                  | 570,000     | \$ 3.67  | 379,000     | \$ 3.33  | 312,000     | \$ 3.25  |
| Granted  | -           | -  | 247,000     | 4.26   | 123,000     | 4.29   |
| Exercised  | (177,000)   | 2.91   | (12,000)    | 2.63   | (20,000)    | 2.80   |
| Forfeited or expired   | (11,000)    | 3.80   | (44,000)    | 4.26   | (36,000)    | 6.26   |
| Outstanding-end of year  | 382,000     | 4.01   | 570,000     | 3.67   | 379,000     | 3.33   |
| Weighted average fair value of options granted during the year | \$ -        |  | \$ 1.20     |  | \$ 1.49     |  |

A summary of stock options outstanding and exercisable at October 31, 2006, follows:

| <b>Exercise Price</b> | <b>Number Outstanding</b> | <b>Remaining Life</b> |
|-----------------------|---------------------------|-----------------------|
| 2.49                  | 21,000                    | 0.05                  |
| 2.77                  | 37,000                    | 1.12                  |
| 4.29                  | 98,000                    | 2.13                  |
| 4.26                  | 226,000                   | 3.96                  |

The Company has a deferred compensation agreement with one employee of Blue Ridge Printing Co., Inc. providing for payments totaling approximately \$500,000 over a ten year period after retirement. The Company had accrued approximately \$375,000 and \$372,000 at October 31, 2006 and 2005 relating to this agreement. The amount expensed for this agreement for the years ended October 31, 2006, 2005 and 2004 approximated \$4,000, \$7,000 and \$11,000. To assist in funding the deferred compensation agreement, the

**Champion Industries, Inc. and Subsidiaries**

## Notes to Consolidated Financial Statements (continued)

Company has invested in life insurance policies, which had a cash surrender value of approximately \$567,000 and \$509,000 for years 2006 and 2005.

**5. Income Taxes**

Income tax expense consisted of the following:

|                  | <b>Year Ended October 31,</b> |                   |                   |
|------------------|-------------------------------|-------------------|-------------------|
|                  | <b>2006</b>                   | 2005              | 2004              |
| Current expense: |                               |                   |                   |
| Federal          | \$ 3,282,566                  | \$ 1,009,920      | \$ 461,383        |
| State            | 835,428                       | 297,543           | 156,575           |
| Deferred benefit | (388,431)                     | (461,308)         | (35,866)          |
|                  | <b>\$ 3,729,563</b>           | <b>\$ 846,155</b> | <b>\$ 582,092</b> |

Deferred tax assets and liabilities are as follows:

|   | <b>October 31,</b>  |                     |
|---|---------------------|---------------------|
|   | <b>2006</b>         | 2005                |
| Deferred tax assets:                                    |                     |                     |
| Allowance for doubtful accounts                         | \$ 633,118          | \$ 574,083          |
| Deferred compensation                                   | 150,122             | 150,122             |
| Net operating loss carryforward of acquired companies   | 458,519             | 649,074             |
| Accrued vacation  | 238,055             | 270,946             |
| Other accrued liabilities                               | 183,973             | 180,254             |
| Other assets  | 232,422             | 172,576             |
| Gross deferred tax assets                               | <b>1,896,209</b>    | 1,997,055           |
| Deferred tax liabilities:                               |                     |                     |
| Property and equipment                                  | 2,669,440           | 3,074,502           |
| Intangible assets                                       | 1,351,429           | 1,435,644           |
| Gross deferred tax liability                            | <b>4,020,869</b>    | 4,510,146           |
| Net deferred tax liabilities before valuation allowance | <b>2,124,660</b>    | 2,513,091           |
| Valuation allowance:                                    |                     |                     |
| Beginning balance                                       | 303,317             | 285,250             |
| Increase during the period                              | -                   | 18,067              |
| Ending balance  | <b>303,317</b>      | 303,317             |
| Net deferred tax liabilities                            | <b>\$ 2,427,977</b> | <b>\$ 2,816,408</b> |

**Champion Industries, Inc. and Subsidiaries**

## Notes to Consolidated Financial Statements (continued)

The above net deferred tax liability is presented on the balance sheet as follows:

|                                    | 2006           | 2005           |
|------------------------------------|----------------|----------------|
| Deferred tax asset - current       | \$ 1,200,037   | \$ 1,168,526   |
| Deferred tax liability - long-term | (3,628,014)    | (3,984,934)    |
|                                    | \$ (2,427,977) | \$ (2,816,408) |

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

|  | Year Ended October 31, |       |       |
|--|------------------------|-------|-------|
|  | 2006                   | 2005  | 2004  |
| Statutory federal income tax rate                | 34.0 %                 | 34.0% | 34.0% |
| State taxes, net of federal benefit              | 5.2                    | 6.5   | 7.5   |
| Change in valuation allowance                    | -                      | 0.6   | -     |
| Selling expenses                                 | 0.7                    | 4.0   | 5.7   |
| Cash surrender value of life insurance accretion | (0.3)                  | (1.4) | (1.3) |
| Other  | 0.9                    | (0.6) | (2.2) |
| Effective tax rate                               | 40.5 %                 | 43.1% | 43.7% |

Income taxes paid during the years ended October 31, 2006, 2005 and 2004 approximated \$3,608,000, \$930,000 and \$1,119,000.

The Company has available for income tax purposes net operating loss carryforwards from acquired companies of approximately \$958,000, of which \$26,000 expires in 2011, \$899,000 in 2012, and \$33,000 in 2013. The Company has available for state income tax purposes net operating loss carryforwards from acquired companies of approximately \$1,677,000 of which \$60,000 expires in 2012, \$108,000 expires in 2013, \$306,000 expires in 2014, \$268,000 expires in 2015, \$478,000 expires in 2016, \$48,000 expires in 2018, \$120,000 expires in 2019, \$281,000 expires in 2020 and \$8,000 expires in 2021. There was no change in the valuation allowance in 2006. During 2005, the valuation allowance increased by \$18,067 which is primarily reflective of the losses incurred during 2005 in Mississippi of which the realizability of the utilization of the resulting net operating losses resulted in an increase in the valuation allowance. There was no change in the valuation allowance in 2004.

**6. Related Party Transactions and Operating Lease Commitments**

The Company leases operating facilities from entities controlled by its Chief Executive Officer, his family and affiliates as well as facilities controlled by a Company owned by the former sole owner of Syscan

**Champion Industries, Inc. and Subsidiaries**

## Notes to Consolidated Financial Statements (continued)

pursuant to the acquisition of Syscan (see note 8). The original terms of these leases, which are accounted for as operating leases, range from two to fifteen years.

A summary of significant related party transactions follows:

|   | <b>Year Ended October 31,</b> |            |            |
|---|-------------------------------|------------|------------|
|   | <b>2006</b>                   | 2005       | 2004       |
| Rent expense paid to affiliated entities for  |                               |            |            |
| for operating facilities  | <b>\$ 449,000</b>             | \$ 519,000 | \$ 394,000 |
| Sales of office products, office furniture and printing services to affiliated entities | <b>693,000</b>                | 1,030,000  | 1,066,000  |

In addition, the Company leases property and equipment from unrelated entities under operating leases. Rent expense amounted to \$714,000, \$807,000 and \$862,000 for the years ended October 31, 2006, 2005 and 2004.

Under the terms and conditions of the above-mentioned leases, the Company is primarily responsible for all taxes, assessments, maintenance, repairs or replacements, utilities and insurance. The Champion Output Solutions' lease excludes taxes and insurance during the initial lease term. The Company has renewal options for certain leases covering varying periods.

Future minimum rental commitments for all noncancelable operating leases including related party commitments with initial terms of one year or more consisted of the following at October 31, 2006:

|      |                     |
|------|---------------------|
| 2007 | \$ 1,124,779        |
| 2008 | 890,647             |
| 2009 | 517,666             |
| 2010 | 255,056             |
| 2011 | 157,042             |
|      | <b>\$ 2,945,190</b> |

The Company participates in a self-insurance program for employee health care benefits with affiliates controlled by its Chief Executive Officer and as such is responsible for paying claims of company participants as required by the plan document. The Company is allocated costs primarily related to the reinsurance premiums based on its proportionate share to provide such benefits to its employees. The Company's expense related to this program for the years ended October 31, 2006, 2005 and 2004 was approximately \$3,792,000, \$3,236,000 and \$3,197,000.

During 2006, 2005 and 2004, the Company utilized an aircraft from an entity controlled by its Chief Executive Officer and reimbursed the controlled entity for the use of the aircraft, fuel, aircrew, ramp fees and other expenses attendant to the Company's use, in amounts aggregating \$119,000, \$118,000 and \$95,000. The Company believes that such





**Champion Industries, Inc. and Subsidiaries**

Notes to Consolidated Financial Statements (continued)

amounts are at or below the market rate charged by third-party commercial charter companies for similar aircraft.

The Company believes that the terms of its related party transactions are no less favorable to the Company than could be obtained with an independent third party.

**7. Commitments and Contingencies**

As reported in Form 8-K filed May 6, 2005, the Company entered into an agreement to settle all claims in a Mississippi lawsuit asserting that the Company and its Dallas Printing Company, Inc. subsidiary had engaged in unfair competition and other wrongful acts in hiring certain employees of National Forms & Systems Group, Inc.

Following trial of this matter, titled National Forms & Systems Group Inc. v. Timothy V. Ross; Todd Ross and Champion Industries, Inc.; and Timothy V. Ross v. National Forms & Systems Group, Inc. and Mickey McCardle; in the Circuit Court of the First Judicial District of Hinds County, Mississippi; Case No. 251-00-942-CIV, on February 16, 2002, a jury had awarded plaintiff \$1,745,000 in actual damages and \$750,000 in punitive damages. Additionally, the trial court had granted plaintiff \$645,119 in attorney fees and expenses, and ordered that interest on the amount of the jury award accrue from February 22, 2002.

The Company successfully appealed the jury award and attorney fee and expense award in both the Court of Appeals of the State of Mississippi and the Supreme Court of Mississippi, with the appellate courts' rulings having the effect of reversing the jury's award of damages and the trial court's award of attorney fees and expenses, and granting a new trial on plaintiff's claims.

Terms of the settlement called for all parties' claims to be dismissed with prejudice, as fully compromised and released. The Company has paid plaintiff \$440,000 cash and did forego collection of and released its \$60,276 cost judgment awarded as a result of the reversal on appeal.

The Company is subject to the environmental laws and regulations of the United States and the states in which it operates concerning emissions into the air, discharges into the waterways and the generation, handling and disposal of waste materials. The Company's past expenditures relating to environmental compliance have not had a material effect on the Company and are included in normal operating expenses. These laws and regulations are constantly evolving, and it is impossible to predict accurately the effect they may have upon the capital expenditures, earnings, and competitive position of the Company in the future. Based upon information currently available, management believes that expenditures relating to environmental compliance will not have a material impact on the financial position of the Company.

**Champion Industries, Inc. and Subsidiaries**

## Notes to Consolidated Financial Statements (continued)

The Company is subject to various claims and legal actions, other than the claim discussed above, that arise in the ordinary course of business as well as various governmental audits and examinations. In the opinion of management, after consulting with legal counsel where applicable, the Company believes that the ultimate resolution of these claims, audits and legal actions will not have a material effect on the consolidated financial statements of the Company.

The Company entered into a purchase commitment for a printing press with a manufacturer for \$1,850,000. As a result of this commitment, the Company paid this manufacturer a deposit of \$185,000 and received an associated trade-in allowance of \$100,000 as of October 31, 2006.

**8. Acquisitions**

On September 7, 2004, the Company acquired all the issued and outstanding capital stock of Syscan Corporation (“Syscan”), a West Virginia corporation, for a cash price of \$3,500,000 and a contingent purchase price, dependent upon satisfaction of certain conditions, not to exceed the amount of \$1,500,000. On December 14, 2006, the Company paid the contingent purchase price in the amount of \$1,350,725. This amount was accrued at October 31, 2006. The Company also purchased a building from an entity controlled by Syscan’s sole shareholder for \$117,000 concurrent with the Syscan acquisition. After considering the cash received, the acquisition of a building and acquisition costs the net assets acquired totaled approximately \$2,688,000. Syscan Corporation is a provider of integrated business products, with a primary emphasis on office and data products, printing, mailing and fulfillment services, and office furniture. The acquisition was consummated based on significant identified synergies which could be achieved due to a duplication of market territory. The acquisition brought additional supply chain management and mailing expertise to the Company and allowed Syscan to offer a broader array of printing services to its existing customer base.

The Williams Land Corporation has the option to put the 3000 Washington Street building occupied by Syscan to the Company for a purchase price of \$1.5 million and the Company has the option to purchase the building for \$1.5 million at the conclusion of the five year lease term ending September 1, 2009. This option may be exercised no later than 60 days prior to the end of the lease and closing of said purchase cannot exceed 45 days from the end of the lease.

Two months of operations of Syscan Corporation are included in the Company’s Statement of Operations commencing concurrent with the acquisition in 2004, and a full year of operations are included in the 2005 and 2006 Statements of Operations.

**Syscan Acquisition**

|                                      |             |
|--------------------------------------|-------------|
| Current assets, net of cash received | \$1,846,000 |
| Property, plant, and equipment       | 782,000     |
| Non-compete agreement                | 1,000,000   |
| Customer relationships               | 2,461,000   |

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|                          |             |
|--------------------------|-------------|
| Other assets             | 127,000     |
| Total assets<br>acquired | 6,216,000   |
| Current<br>liabilities   | (1,343,000) |
| Long-term<br>debt        | (760,000)   |

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**Champion Industries, Inc. and Subsidiaries**

## Notes to Consolidated Financial Statements (continued)

|                               |              |
|-------------------------------|--------------|
| Deferred tax                  | (1,425,000)  |
| Total liabilities<br>acquired | (3,528,000)  |
| Net assets<br>acquired        | \$ 2,688,000 |

The identifiable intangible assets of Syscan are being amortized on a straight-line basis over a period of 7 years for the non-compete agreement and 20 years for the customer relationships. The weighted average life of the intangible assets at the acquisition date was approximately 16 years. The contingent purchase price of \$1,350,725 was recorded as a component of goodwill at October 31, 2006.

On May 13, 2004, the Company acquired certain assets of Cincinnati, Ohio Westerman Print Company.

Pro forma financial information and all disclosures required by SFAS 141 and SFAS 142 related to these acquisitions have not been presented because such information would not be materially different from amounts reported herein or is not significant.

All of the above transactions have been accounted for using the purchase method of accounting.

**9. Industry Segment Information**

The Company operates principally in two industry segments organized on the basis of product lines: the production, printing and sale, principally to commercial customers, of printed materials (including brochures, pamphlets, reports, tags, continuous and other forms); and the sale of office products and office furniture including interior design services. The Company employs approximately 730 people, of whom approximately 70 or 10% are covered by a collective bargaining agreement, which expires on May 31, 2010.

## Champion Industries, Inc. and Subsidiaries

## Notes to Consolidated Financial Statements (continued)

The table below presents information about reported segments for the years ended October 31:

|  | Office<br>Products &<br>Furniture |               |                |
|--|-----------------------------------|---------------|----------------|
| 2006                                       | Printing                          | Furniture     | Total          |
| <b>Revenues</b>                            | \$ 120,891,348                    | \$ 47,758,730 | \$ 168,650,078 |
| <b>Elimination of intersegment revenue</b> | (14,477,685)                      | (8,984,517)   | (23,462,202)   |
| <b>Consolidated revenues</b>               | \$ 106,413,663                    | \$ 38,774,213 | \$ 145,187,876 |
| <b>Operating income</b>                    | 6,804,181                         | 2,949,166     | 9,753,347      |
| <b>Depreciation &amp; amortization</b>     | 3,975,850                         | 182,898       | 4,158,748      |
| <b>Capital expenditures</b>                | 3,995,745                         | 278,184       | 4,273,929      |
| <b>Identifiable assets</b>                 | 53,714,643                        | 12,274,083    | 65,988,726     |
| <b>Goodwill</b>                            | 2,226,837                         | 1,184,674     | 3,411,511      |

|                                     | Office<br>Products &<br>Furniture |               |                |
|-------------------------------------|-----------------------------------|---------------|----------------|
| 2005                                | Printing                          | Furniture     | Total          |
| Revenues                            | \$ 112,680,275                    | \$ 44,931,089 | \$ 157,611,364 |
| Elimination of intersegment revenue | (14,222,258)                      | (8,463,870)   | (22,686,128)   |
| Consolidated revenues               | \$ 98,458,017                     | \$ 36,467,219 | \$ 134,925,236 |
| Operating income                    | 779,790                           | 1,654,878     | 2,434,668      |
| Depreciation & amortization         | 4,546,612                         | 149,493       | 4,696,105      |
| Capital expenditures                | 2,821,379                         | 192,207       | 3,013,586      |
| Identifiable assets                 | 51,014,174                        | 10,630,996    | 61,645,170     |
| Goodwill                            | 1,774,344                         | 286,442       | 2,060,786      |

|                                     | Office<br>Products &<br>Furniture |               |                |
|-------------------------------------|-----------------------------------|---------------|----------------|
| 2004                                | Printing                          | Furniture     | Total          |
| Revenues                            | \$ 107,696,605                    | \$ 34,919,102 | \$ 142,615,707 |
| Elimination of intersegment revenue | (12,372,291)                      | (5,841,844)   | (18,214,135)   |
| Consolidated revenues               | \$ 95,324,314                     | \$ 29,077,258 | \$ 124,401,572 |
| Operating income                    | 632,232                           | 705,887       | 1,338,119      |
| Depreciation & amortization         | 4,247,164                         | 142,594       | 4,389,758      |
| Capital expenditures                | 4,912,115                         | 61,719        | 4,973,834      |
| Identifiable assets                 | 54,378,626                        | 9,771,258     | 64,149,884     |
| Goodwill                            | 1,774,344                         | 286,442       | 2,060,786      |

**Champion Industries, Inc. and Subsidiaries**

## Notes to Consolidated Financial Statements (continued)

A reconciliation of total segment revenue, assets and operating income to consolidated income before income taxes for the years ended October 31, 2006, 2005 and 2004 is as follows:

|   | 2006           | 2005           | 2004           |
|---|----------------|----------------|----------------|
| <b>Revenues:</b>                        |                |                |                |
| Total segment revenues                  | \$ 168,650,078 | \$ 157,611,364 | \$ 142,615,707 |
| Elimination of intersegment revenue     | (23,462,202)   | (22,686,128)   | (18,214,135)   |
| Consolidated revenue                    | \$ 145,187,876 | \$ 134,925,236 | \$ 124,401,572 |
| <b>Operating income:</b>                |                |                |                |
| Total segment operating income          | \$ 9,753,347   | \$ 2,434,668   | \$ 1,338,119   |
| Interest income                         | 28,251         | 18,472         | 6,663          |
| Interest expense                        | (609,881)      | (610,787)      | (300,742)      |
| Other income                            | 31,694         | 120,436        | 287,750        |
| Consolidated income before income taxes | \$ 9,203,411   | \$ 1,962,789   | \$ 1,331,790   |
| <b>Identifiable assets:</b>             |                |                |                |
| Total segment identifiable assets       | \$ 65,988,726  | \$ 61,645,170  | \$ 64,149,884  |
| Elimination of intersegment assets      | -              | -              | -              |
| Total consolidated assets               | \$ 65,988,726  | \$ 61,645,170  | \$ 64,149,884  |

**10. Accounting for Costs Associated with Exit or Disposal Activities and Impact of Hurricane Katrina**

During the second quarter of 2004, the Company incurred plant consolidation and facility relocation costs related to the closure of the Blue Ridge Printing Knoxville plant and consolidation into the Blue Ridge Printing Asheville plant, and the facility consolidations in Baton Rouge related to Bourque, Transdata and Diez. The facility consolidation and relocation costs approximated \$150,000 and the personnel severance related costs approximated \$37,000.

**Champion Industries, Inc. and Subsidiaries**

Notes to Consolidated Financial Statements (continued)

The costs associated with the aforementioned relocation of the Blue Ridge and Baton Rouge consolidations were reflected in the consolidated statements of operations statement in the category where the expenses historically have been classified and are part of the printing segment.

During the second quarter of 2005, the Company relocated its Chapman Printing Company Charleston division to a facility leased by the Company as a result of the acquisition of Syscan. The Company is currently evaluating its facility needs in Charleston, West Virginia and the future use, if any, of this building.

The Company moved its Dallas operations to an existing facility in Baton Rouge, Louisiana in August 2005. The Company is currently evaluating its options regarding this facility.

On August 29, 2005, Hurricane Katrina made landfall and subsequently caused extensive flooding and destruction along the coastal areas of the Gulf of Mexico, including New Orleans and other communities in Louisiana and Mississippi in which Champion conducts business. Operations in many of the Company's markets were disrupted by both the evacuation of large portions of the population as well as damage and/or lack of access to the Company's operating facility in New Orleans.

The Company filed insurance claims related to both actual and contingent losses. The Company received an advance to claim from an insurance company of \$300,000 in February 2006. A second advance to claim of \$200,000 was received in April 2006 and a check in the amount of \$78,000 in full settlement of any and all claims was received in May 2006. The Company recorded all of the payments as insurance recoveries for the year ended October 31, 2006.

The Company has categorized the costs associated with Hurricane Katrina as follows:

- 1.) Personnel costs representing costs associated with payment of personnel primarily in New Orleans during the time period the city was essentially shut down;
- 2.) Plant costs represent all facilities, equipment and inventory charges incurred as a result of the hurricane using the most current available information;
- 3.) The allowance for doubtful accounts charge represents accounts receivable specifically reserved based on a collectibility analysis performed by the Company using the most current available information for customers located in the New Orleans area at that time;
- 4.) The relocation costs represent costs of closing the New Orleans production facility and associated costs of moving equipment.



The following table summarizes the cumulative costs incurred as October 31, 2006 relating to Hurricane Katrina.

|   |            |
|---|------------|
| Personnel                                   | \$ 88,423  |
| Plant                                       | 745,035    |
| Allowance for doubtful accounts             | 208,310    |
| Moving and relocation costs                 | 255,215    |
| Total pre-tax hurricane expense             | 1,296,983  |
| Lease settlement recovery                   | 75,583     |
| Insurance recoveries                        | 577,677    |
| Total recoveries                            | 653,260    |
| Cumulative impact of Hurricane Katrina, net | \$ 643,723 |

The Company recorded costs of \$1,020,999 for the three months ended October, 31 2005 and costs of \$275,984 and recoveries of \$653,260 for the year ended October 31, 2006 relating to Hurricane Katrina.

The costs and recoveries associated with Hurricane Katrina are reflected in the consolidated statements of operations in the category "Hurricane and relocation costs, net of recoveries" and are part of the printing segment.

**Champion Industries, Inc. and Subsidiaries**

Notes to Consolidated Financial Statements (continued)

**11. Fair Value of Financial Instruments**

The carrying amount reported in the balance sheet for cash and cash equivalents approximates its fair value. The fair value of long-term debt was estimated using discounted cash flows and it approximates its carrying value.

**12. Acquired Intangible Assets and Goodwill**

|   | 2006                        |                             | 2005                        |                             |
|---|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
|   | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization |
| Amortizable<br>intangible assets:       |                             |                             |                             |                             |
| Non-compete agreement                   | \$ 1,000,000                | \$ 309,524                  | \$ 1,000,000                | \$ 166,667                  |
| Customer relationships                  | 2,451,073                   | 294,348                     | 2,661,610                   | 160,554                     |
| Other                                   | 509,946                     | 231,456                     | 509,946                     | 146,967                     |
|   | 3,961,019                   | 835,328                     | 4,171,556                   | 474,188                     |
| Unamortizable<br>intangible assets:     |                             |                             |                             |                             |
| Goodwill                                | 3,918,789                   | 507,278                     | 2,568,064                   | 507,278                     |
| Total goodwill and other<br>intangibles | \$ 7,879,808                | \$ 1,342,606                | \$ 6,739,620                | \$ 981,466                  |

**Champion Industries, Inc. and Subsidiaries**

## Notes to Consolidated Financial Statements (continued)

Amortization expense for the years ended October 31, 2006, 2005 and 2004 was \$361,000, \$358,000 and \$104,000 respectively. Estimated amortization expense for each of the following years is:

|            |              |
|------------|--------------|
| 2007       | \$ 349,444   |
| 2008       | 344,338      |
| 2009       | 303,366      |
| 2010       | 282,455      |
| 2011       | 258,645      |
| Thereafter | 1,587,443    |
|            | \$ 3,125,691 |

The changes in the carrying amount of goodwill for the years ended October 31, 2006 and 2005 were:

|   | <b>2006</b>  | 2005         |
|---|--------------|--------------|
| Balance as of<br>November 1, 2005<br>and 2004     | \$ 2,060,786 | \$ 2,060,786 |
| Goodwill acquired<br>during the year<br>additions | 1,350,725    | -            |
| Balance as of October<br>31, 2006 and 2005        | \$ 3,411,511 | \$ 2,060,786 |

**Champion Industries, Inc. and Subsidiaries**

Notes to Consolidated Financial Statements (continued)

The changes in the carrying amounts of goodwill and other intangibles attribute to each segment at October 31, 2006 and 2005 are as follows:

**GOODWILL**

|                             | <b>October<br/>31, 2005</b> | <b>Amortization<br/>Expense</b> | <b>Other</b>        | <b>October<br/>31, 2006</b> |
|-----------------------------|-----------------------------|---------------------------------|---------------------|-----------------------------|
| Printing                    | \$ 1,774,344                | \$ -                            | \$ 452,493          | \$ 2,226,837                |
| Office products & furniture | 286,442                     | -                               | 898,232             | 1,184,674                   |
| <b>Total</b>                | <b>\$ 2,060,786</b>         | <b>\$ -</b>                     | <b>\$ 1,350,725</b> | <b>\$ 3,411,511</b>         |

|                             | <b>October<br/>31, 2004</b> | <b>Amortization<br/>Expense</b> | <b>Other</b> | <b>October<br/>31, 2005</b> |
|-----------------------------|-----------------------------|---------------------------------|--------------|-----------------------------|
| Printing                    | \$ 1,774,344                | \$ -                            | \$ -         | \$ 1,774,344                |
| Office products & furniture | 286,442                     | -                               | -            | 286,442                     |
| <b>Total</b>                | <b>\$ 2,060,786</b>         | <b>\$ -</b>                     | <b>\$ -</b>  | <b>\$ 2,060,786</b>         |

**OTHER INTANGIBLES**

|                             | <b>October<br/>31, 2005</b> | <b>Amortization<br/>Expense</b> | <b>Other</b>        | <b>October<br/>31, 2006</b> |
|-----------------------------|-----------------------------|---------------------------------|---------------------|-----------------------------|
| Printing                    | \$ 1,448,342                | \$ 164,912                      | \$ (70,531)         | \$ 1,212,899                |
| Office products & furniture | 2,249,026                   | 196,228                         | (140,006)           | 1,912,792                   |
| <b>Total</b>                | <b>\$ 3,697,368</b>         | <b>\$ 361,140</b>               | <b>\$ (210,537)</b> | <b>\$ 3,125,691</b>         |

|                             | <b>October<br/>31, 2004</b> | <b>Amortization<br/>Expense</b> | <b>Other</b>      | <b>October<br/>31, 2005</b> |
|-----------------------------|-----------------------------|---------------------------------|-------------------|-----------------------------|
| Printing                    | \$ 1,498,323                | \$ 159,582                      | \$ 109,601        | \$ 1,448,342                |
| Office products & furniture | 2,313,728                   | 198,339                         | 133,637           | 2,249,026                   |
| <b>Total</b>                | <b>\$ 3,812,051</b>         | <b>\$ 357,921</b>               | <b>\$ 243,238</b> | <b>\$ 3,697,368</b>         |

**13. Certain Significant Estimates**

Our estimates that influence the financial statements are normally based on knowledge and experience about past and current events and assumptions about future events. The following estimates affecting the financial statements are particularly sensitive

**Champion Industries, Inc. and Subsidiaries**

Notes to Consolidated Financial Statements (continued)

because of their significance and it is at least reasonably possible that a change in these estimates will occur in the near term.

**Goodwill and Intangible Assets**

We evaluate the recoverability of the goodwill and intangible assets of each of our reporting units as required under SFAS 142 by comparing the fair value of each reporting unit with its carrying value. The fair values of our reporting units are determined using a combination of a discounted cash flow analysis and market multiples based on historical and projected financial information. We apply our best judgment when assessing the reasonableness of the financial projections used to determine the fair value of each reporting unit.

**Allowance for Doubtful Accounts**

The Company encounters risks associated with sales and the collection of the associated accounts receivable. As such, the Company records a monthly provision for accounts receivable that are considered to be uncollectible. In order to calculate the appropriate monthly provision, the Company primarily utilizes a historical rate of accounts receivables written off as a percentage of total revenue. This historical rate is applied to the current revenues on a monthly basis. The historical rate is updated periodically based on events that may change the rate such as a significant increase or decrease in collection performance and timing of payments as well as the calculated total exposure in relation to the allowance. Periodically, the Company compares the identified credit risks with the allowance that has been established using historical experience and adjusts the allowance accordingly. The underlying assumptions used for the allowance can change from period to period and could potentially cause a material impact to the income statement and working capital.

**Champion Industries, Inc. and Subsidiaries**

Notes to Consolidated Financial Statements (continued)

**14. Earnings Per Share**

Earnings per share (EPS) were computed as follows:

|   | Income       | Weighted<br>Average<br>Shares | Per<br>Share<br>Amount |
|---|--------------|-------------------------------|------------------------|
| <b>Year Ended October 31, 2006</b>                              |              |                               |                        |
| Net income  | \$ 5,473,848 |                               |                        |
| Basic earnings per share  |              |                               |                        |
| Income available to common shareholders                         | 5,473,848    | 9,818,000                     | \$ 0.56                |
| Effect of dilutive securities stock options                     |              | 154,000                       |                        |
| Diluted earnings per share                                      |              |                               |                        |
| Income available to common shareholders and assumed conversions | \$ 5,473,848 | 9,972,000                     | \$ 0.55                |
| <b>Year Ended October 31, 2005</b>                              |              |                               |                        |
| Net income  | \$ 1,116,634 |                               |                        |
| Basic earnings per share  |              |                               |                        |
| Income available to common shareholders                         | 1,116,634    | 9,735,000                     | \$ 0.11                |
| Effect of dilutive securities stock options                     |              | 74,000                        |                        |
| Diluted earnings per share                                      |              |                               |                        |
| Income available to common shareholders and assumed conversions | \$ 1,116,634 | 9,809,000                     | \$ 0.11                |
| <b>Year Ended October 31, 2004</b>                              |              |                               |                        |
| Net income  | \$ 749,698   |                               |                        |
| Basic earnings per share  |              |                               |                        |
| Income available to common shareholders                         | 749,698      | 9,729,000                     | \$ 0.08                |
| Effect of dilutive securities stock options                     |              | 96,000                        |                        |
| Diluted earnings per share                                      |              |                               |                        |
| Income available to common shareholders and assumed conversions | \$ 749,698   | 9,825,000                     | \$ 0.08                |

**Champion Industries, Inc. and Subsidiaries**

Notes to Consolidated Financial Statements (continued)

**15. Quarterly Results of Operations (unaudited)**

The following is a summary of the quarterly results of operations for the years ended October 31, 2006 and 2005.

|  | First<br>Quarter (1) | Second<br>Quarter (2) | Third<br>Quarter     | Fourth<br>Quarter (3) |
|--|----------------------|-----------------------|----------------------|-----------------------|
| <b>Revenues</b>                                    |                      |                       |                      |                       |
| <b>2006</b>  | <b>\$ 36,292,000</b> | <b>\$ 37,421,000</b>  | <b>\$ 34,510,000</b> | <b>\$ 36,965,000</b>  |
| 2005   | \$ 34,440,000        | \$ 33,552,000         | \$ 32,255,000        | \$ 34,678,000         |
| <b>Gross profit</b>                                |                      |                       |                      |                       |
| <b>2006</b>  | <b>\$ 10,597,000</b> | <b>\$ 11,512,000</b>  | <b>\$ 9,758,000</b>  | <b>\$ 11,527,000</b>  |
| 2005   | \$ 9,511,000         | \$ 9,207,000          | \$ 9,258,000         | \$ 10,276,000         |
| <b>Net income<br/>(loss)</b>                       |                      |                       |                      |                       |
| <b>2006</b>  | <b>\$ 1,146,000</b>  | <b>\$ 1,578,000</b>   | <b>\$ 777,000</b>    | <b>\$ 1,973,000</b>   |
| 2005   | \$ 263,000           | \$ (97,000)           | \$ 382,000           | \$ 569,000            |
| <b>Earnings (loss)<br/>per share</b>               |                      |                       |                      |                       |
| Basic  |                      |                       |                      |                       |
| <b>2006</b>  | <b>\$ 0.12</b>       | <b>\$ 0.16</b>        | <b>\$ 0.08</b>       | <b>\$ 0.20</b>        |
| 2005   | \$ 0.03              | \$ (0.01)             | \$ 0.04              | \$ 0.06               |
| Diluted  |                      |                       |                      |                       |
| <b>2006</b>  | <b>\$ 0.12</b>       | <b>\$ 0.16</b>        | <b>\$ 0.08</b>       | <b>\$ 0.20</b>        |
| 2005   | \$ 0.03              | \$ (0.01)             | \$ 0.04              | \$ 0.06               |
| <b>Weighted<br/>average shares<br/>outstanding</b> |                      |                       |                      |                       |
| Basic  |                      |                       |                      |                       |
| <b>2006</b>  | <b>9,746,000</b>     | <b>9,746,000</b>      | <b>9,865,000</b>     | <b>9,916,000</b>      |
| 2005   | 9,734,000            | 9,734,000             | 9,734,000            | 9,739,000             |
| Diluted  |                      |                       |                      |                       |
| <b>2006</b>  | <b>9,831,000</b>     | <b>9,947,000</b>      | <b>10,089,000</b>    | <b>10,087,000</b>     |
| 2005   | 9,802,000            | 9,734,000             | 9,812,000            | 9,820,000             |

(1) Includes in 2006, approximately \$258,000 of pre-tax recoveries, net of expenses, associated with Hurricane Katrina. (See Note 10 of the Consolidated Financial Statements.)

(2) Includes in 2005, approximately \$800,000 in pre-tax charges related to various legal related costs associated with various legal settlements, accruals and expenses, including \$440,000 settlement related to a Mississippi lawsuit. (See Note 7 Commitments and Contingencies.) Includes in 2006, pre-tax recoveries, net of expenses, associated with Hurricane Katrina of \$44,000. (See Note 10 of the Consolidated Financial Statements.)

(3) Includes in 2005, approximately \$1.0 million of pre-tax charges incurred as a result of Hurricane Katrina. Includes in 2006, approximately \$76,000 in pre-tax recoveries associated with Hurricane Katrina. (See Note 10 of the Consolidated Financial Statements.)

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**Champion Industries, Inc. and Subsidiaries**

Schedule II

Valuation and Qualifying Accounts

Years Ended October 31, 2006, 2005 and 2004

| Description                     | Balance<br>at<br>beginning<br>of period | Balances<br>of<br>acquired<br>companies | Additions<br>charged<br>to<br>costs and<br>expenses | Deductions<br>(1) | Balance<br>at end<br>of period |
|---------------------------------|---|---|---|-------------------|--------------------------------|
| <b>2006</b>                     |   |   |   |                   |                                |
| Allowance for doubtful accounts | \$ 1,410,308                            | \$ -                                    | \$ 979,089  | \$ (831,502)      | \$ 1,557,895                   |
| <b>2005</b>                     |   |   |   |                   |                                |
| Allowance for doubtful accounts | \$ 1,421,922                            | \$ (25,000)                             | \$ 420,673  | \$ (407,287)      | \$ 1,410,308                   |
| <b>2004</b>                     |   |   |   |                   |                                |
| Allowance for doubtful accounts | \$ 1,190,996                            | \$ 207,250                              | \$ 487,550  | \$ (463,874)      | \$ 1,421,922                   |

(1) Uncollectible accounts written off, net of recoveries.

