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IMAGISTICS INTERNATIONAL INC

Form 10-Q

November 13, 2002

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(MARK ONE)

/X/ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30,  
2002

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

Commission File Number 1-16449

IMAGISTICS INTERNATIONAL INC.

(Exact Name of Registrant as Specified in Its Charter)

DELAWARE

(State or Other Jurisdiction of  
Incorporation or Organization)

06-1611068

(I.R.S. Employer Identification No.)

100 OAKVIEW DRIVE

TRUMBULL, CONNECTICUT

(Address of Principal Executive Offices)

06611

(Zip Code)

(203) 365-7000

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant is an accelerated filer (as  
defined in Rule 126-2 of the Exchange Act). Yes X No\_\_\_

Number of shares of Imagistics Common Stock, par value \$ .01 per share,  
outstanding as of October 31, 2002: 18,206,057

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

IMAGISTICS INTERNATIONAL INC.

CONSOLIDATED INCOME STATEMENTS  
 (DOLLARS IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)  
 (UNAUDITED)

	FOR THE THREE MONTHS ENDED SEPTEMBER 30,	
	2002	2001
	-----	-----
Revenue:		
Sales	\$ 77,081	\$ 79,998
Rentals	58,088	58,549
Support services	20,900	19,775

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Total revenue	156,069	158,322
Cost of sales	47,236	48,816
Cost of rentals	20,991	23,526
Selling, service and administrative expenses	78,707	82,956
Earnings before interest and taxes	9,135	3,024
Interest expense	2,240	2,636
Income before income taxes	6,895	388
Provision for income taxes	2,740	106
Net income	\$ 4,155	\$ 282
Earnings per share:		
Basic	\$ 0.23	\$ 0.01
Diluted	\$ 0.22	\$ 0.01
Shares used in computing earnings per share:		
Basic	17,989,310	19,463,007
Diluted	18,537,611	19,479,121

See Notes to Consolidated Financial Statements

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IMAGISTICS INTERNATIONAL INC.

CONSOLIDATED BALANCE SHEETS  
(DOLLARS IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

ASSETS

Current assets:

Cash

Accounts receivable, less allowances of \$7,095 and \$6,188 at  
September 30, 2002 and December 31, 2001, respectively

Accrued billings

Inventories

Current deferred taxes on income

Other current assets and prepaid expenses

Total current assets

Property, plant and equipment, net

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Rental equipment, net  
Goodwill, net of accumulated amortization of \$4,855 at  
September 30, 2002 and December 31, 2001  
Other assets

Total assets

LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities:

Current portion of long-term debt  
Accounts payable and accrued liabilities  
Advance billings

Total current liabilities

Long-term debt  
Deferred taxes on income  
Other liabilities

Total liabilities

Commitments and contingencies

Stockholders' equity:

Preferred stock (\$1.00 par value; 10,000,000 shares authorized,  
none outstanding at September 30, 2002 and December 31, 2001)  
Common stock (\$0.01 par value; 150,000,000 shares authorized,  
18,205,927 and 19,463,007 outstanding at September 30, 2002  
and December 31, 2001, respectively)  
Additional paid in capital  
Retained earnings (deficit)  
Treasury stock, at cost (1,607,460 shares at September 30, 2002  
and none at December 31, 2001)  
Unearned compensation  
Accumulated other comprehensive loss

Total stockholders' equity

Total liabilities and stockholders' equity

See Notes to Consolidated Financial Statements

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IMAGISTICS INTERNATIONAL INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS  
(DOLLARS IN THOUSANDS)  
(UNAUDITED)

NINE MONTH  
SEPTEMBER

2002

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Cash flows from operating activities:	
Net income	\$ 12,392
Adjustments to reconcile net income to net cash provided by operating activities:	
Depreciation and amortization	60,093
Accounts receivable write-offs	3,765
Provision for inventory obsolescence	10,139
Deferred taxes on income	3,719
Change in assets and liabilities, net of acquisitions:	
Accounts receivable	12,813
Accrued billings	(428)
Inventories	7,869
Other current assets and prepaid expenses	1,286
Accounts payable and accrued liabilities	19,897
Advance billings	(904)
Other, net	1,632
Net cash provided by operating activities	----- 132,273
Cash flows from investing activities:	
Expenditures for fixed assets	(53,583)
Other investing activities	-
Net cash used in investing activities	----- (53,583)
Cash flows from financing activities:	
Due to Pitney Bowes	-
Advances to Pitney Bowes	-
Exercised stock options	35
Purchase of treasury stock	(29,998)
Repayment under term loan	(25,665)
Repayment under revolving credit facility	(17,000)
Net cash used in financing activities	----- (72,628)
Increase in cash	6,062
Cash at beginning of period	18,844
Cash at end of period	----- \$ 24,906 =====

See Notes to Consolidated Financial Statements

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### IMAGISTICS INTERNATIONAL INC.

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(DOLLARS IN THOUSANDS, EXCEPT PER SHARE AMOUNTS AND AS OTHERWISE INDICATED)  
(UNAUDITED)

#### 1. BACKGROUND AND BASIS OF PRESENTATION

Background. The unaudited interim consolidated financial statements of Imagistics International Inc. ("Imagistics" or the "Company") have been prepared in accordance with accounting principles generally accepted in the United States of America and the rules and regulations of the Securities and Exchange Commission (the "SEC") and, in the opinion of the Company, include all adjustments (consisting of normal recurring accruals) necessary for a fair presentation of results of operations, financial position and cash flows as of

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and for the periods presented. Certain prior year amounts have been reclassified to conform to the current year presentation.

The Company believes that the disclosures contained in the unaudited interim consolidated financial statements are adequate to keep the information presented from being misleading. The results for the three and nine months ended September 30, 2002 are not necessarily indicative of the results for the full year. These unaudited interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's latest Annual Report on Form 10-K for the year ended December 31, 2001 filed with the SEC on March 28, 2002.

Imagistics is a large independent direct sales, service and marketing organization offering document imaging solutions, including copiers, facsimile machines and multi-functional products, primarily to large corporate and government customers, as well as to mid-sized and regional businesses. In addition, the Company offers a range of copier and multi-functional product document imaging options including digital, analog, color and/or networked products and systems.

On December 11, 2000, the board of directors of Pitney Bowes Inc. ("Pitney Bowes") initiated a plan to spin-off substantially all of its office systems businesses to its stockholders as an independent publicly traded company. On December 3, 2001, Imagistics was spun off from Pitney Bowes pursuant to a contribution by Pitney Bowes of substantially all of its office systems businesses to the Company and a distribution (the "Distribution") of the stock of the Company to stockholders of Pitney Bowes based on a distribution ratio of 1 share of Imagistics stock for every 12.5 shares of Pitney Bowes stock held at the close of business on November 19, 2001.

The Company was incorporated in Delaware on February 28, 2001 as Pitney Bowes Office Systems, Inc., a wholly owned subsidiary of Pitney Bowes. On that date, 100 shares of the Company's common stock, par value \$.01 per share, were authorized, issued and outstanding. On October 12, 2001, the Company changed its name to Imagistics International Inc. At the Distribution, the Company's authorized capital stock consisted of 10,000,000 shares of preferred stock, par value \$1.00 per share and 150,000,000 shares of common stock, par value \$.01 per share. The Company issued 19,463,007 shares of common stock in connection with the Distribution.

Pitney Bowes has received a tax ruling from the Internal Revenue Service stating that, subject to certain representations, the Distribution qualifies as tax-free to Pitney Bowes and its stockholders for United States federal income tax purposes.

Basis of presentation. The consolidated financial statements include certain historical assets, liabilities and related operations of the United States and United Kingdom office systems businesses, which were contributed to the Company from Pitney Bowes prior to the Distribution. Accordingly, the consolidated financial statements prior to December 3, 2001 were derived from the financial statements and accounting records of Pitney Bowes using the historical results of operations and historical basis of assets and liabilities of the United States and United Kingdom office systems businesses. Prior to the formation of the Company, the office systems business was operated as a division of Pitney Bowes. The Company began accumulating retained earnings on December 3, 2001, the date of the Distribution. Management believes the assumptions underlying the consolidated financial statements are reasonable. However, the consolidated financial statements included herein may not necessarily reflect the Company's financial position, results of operations and cash flows in the future or what its financial position, results of operations and cash flows would have been had the Company operated as a stand-alone entity in prior periods.

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2. GOODWILL AND GOODWILL AMORTIZATION

Effective January 1, 2002, the Company adopted Statement of Financial Accounting Standards ("SFAS") No. 142 "Goodwill and Other Intangible Assets", which requires that goodwill and certain other intangible assets having indefinite lives no longer be amortized to earnings, but instead be subject to periodic testing for impairment. The Company has completed a transitional review of its goodwill for impairment and, based on that review, has determined that its recorded goodwill was not impaired.

For the three and nine month periods ended September 30, 2001, goodwill amortization amounted to \$0.4 million and \$1.1 million, respectively. If the Company had adopted SFAS 142 at the beginning of fiscal 2001 and discontinued goodwill amortization, net income and income per common share on a pro forma basis would have been as follows:

	PRO FORMA	
	THREE MONTHS ENDED SEPTEMBER 30, 2001	NINE MONTHS ENDED SEPTEMBER 30, 2001
Net income	\$ 541	\$ 13,563
Income per common share		
Basic	\$ 0.03	\$ 0.70
Diluted	\$ 0.03	\$ 0.70

The carrying value of goodwill of \$52.6 million as of September 30, 2002 is attributable to the United States geographic segment.

3. SUPPLEMENTAL INFORMATION

Inventories

Inventories consist of the following:

	SEPTEMBER 30, 2002	DECEMBER 31, 2001
Supplies and service parts	\$ 34,860	\$ 35,905
Finished products	71,138	88,101
Total inventories	\$ 105,998	\$ 124,006

Fixed assets

Fixed assets consist of the following:

	SEPTEMBER 30, 2002	DECEMBER 31, 2001
Land	\$ 1,356	\$ 1,356
Buildings and leasehold improvements	9,903	9,515
Machinery and equipment	54,626	39,854

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Property, plant and equipment, gross	65,885	50,725
Accumulated depreciation	(24,025)	(19,911)
Property, plant and equipment, net	\$ 41,860	\$ 30,814
Rental equipment, gross	\$ 377,252	\$ 378,391
Accumulated depreciation	(280,884)	(264,467)
Rental equipment, net	\$ 96,368	\$ 113,924

Depreciation expense was \$19.8 million and \$60.1 million for the three and nine months ended September 30, 2002, respectively, and \$18.0 million and \$56.6 million for the three and nine months ended September 30, 2001, respectively.

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Current liabilities

Accounts payable and accrued liabilities consist of the following:

	SEPTEMBER 30, 2002	DECEMBER 31, 2001
Accounts payable	\$ 20,458	\$ 22,679
Accrued compensation and benefits	18,908	10,848
Other non-income taxes payable	6,731	7,566
Miscellaneous accrued liabilities	28,601	13,678
Accounts payable and accrued liabilities	\$ 74,698	\$ 54,771

Comprehensive income

Comprehensive income consists of the following:

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	2002	2001	2002	2001
Net income	\$ 4,155	\$ 282	\$ 12,392	\$ 12,876
Translation adjustment	998	95	1,289	108
Unrealized loss on cash flow hedges	(1,995)	\$ -	(3,762)	\$ -
Comprehensive income	\$ 3,158	\$ 377	\$ 9,919	\$ 12,984

The Company had interest rate swap agreements in the aggregate notional amount of \$72 million and \$80 million at September 30, 2002 and December 31, 2001, respectively, designated as cash flow hedges. At September 30, 2002, the



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Company recorded a liability of \$3,461 for the fair market value of the interest rate swap agreements. At December 31, 2001, the Company recorded an asset of \$301 for the fair market value of the interest rate swap agreements. The unrealized gain or loss on the change in the market value of the interest rate swap agreements was included in accumulated other comprehensive loss in stockholders' equity.

### Treasury Stock

Treasury stock consists of 1,607,460 shares of the Company's common stock repurchased at a cost of \$29,998.

### Cash flow information

Cash paid for income taxes was \$2,846 and cash paid for interest was \$6,605 for the nine months ended September 30, 2002.

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## 4. BUSINESS SEGMENT INFORMATION

Geographic information. The Company operates in two reportable segments based on geographic area: the United States and the United Kingdom. Revenues are attributed to geographic regions based on where the revenues are derived. Identifiable long-lived assets in the United States at September 30, 2002 and December 31, 2001 include goodwill of \$52.6 million.

	THREE MONTHS ENDED SEPTEMBER 30,		
	2002	2001	
Revenues:			
United States:			
Sales	\$ 73,718	\$ 77,152	\$
Rentals	56,289	56,687	
Support services	20,361	19,447	
Total United States revenues	\$150,368	\$153,286	\$
United Kingdom:			
Sales	\$ 3,363	\$ 2,846	\$
Rentals	1,799	1,862	
Support services	539	328	
Total United Kingdom revenues	5,701	5,036	
Total revenues	\$156,069	\$158,322	\$
Income before income taxes:			
United States	\$ 6,129	\$ (122)	\$
United Kingdom	766	510	
Total income before income taxes	\$ 6,895	\$ 388	\$

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Revenues from Pitney Bowes, substantially all of which are generated in the United States segment, were approximately \$37.1 million and \$106.3 million during the three and nine months ended September 30, 2002 and \$35.8 million and \$88.4 million during the three and nine months ended September 30, 2001. Of the 2002 revenues from Pitney Bowes, approximately \$22.7 million and \$65.4 million were for equipment sold to Pitney Bowes Credit Corporation ("PBCC") for lease to the end user, approximately \$4.7 million and \$18.2 million were for equipment and supplies sold to Pitney Bowes Canada and approximately \$9.6 million and \$22.8 million were for equipment, supplies and services sold to other Pitney Bowes subsidiaries during the three and nine months ended September 30, respectively. In 2001, approximately \$28.0 million and \$71.7 million were for equipment sold to PBCC, approximately \$0.5 million and \$2.4 million were for equipment and supplies sold to Pitney Bowes Canada and approximately \$7.3 million and \$14.3 million were for equipment, supplies and services sold to other Pitney Bowes subsidiaries during the three and nine month periods ended September 30, respectively. No other single customer or controlled group represents 10% or more of the Company's revenues.

	SEPTEMBER 30, 2002	DECEMBER 31, 2001
	-----	-----
Identifiable long-lived assets		
United States	\$ 192,441	\$ 199,837
United Kingdom	5,014	5,133
	-----	-----
Total identifiable long-lived assets	\$ 197,455	\$ 204,970
	=====	=====
 Total assets		
United States	\$ 439,449	\$ 477,710
United Kingdom	24,738	19,967
	-----	-----
Total assets	\$ 464,187	\$ 497,677
	=====	=====

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Concentrations. Concentrations of credit risk with respect to accounts receivable are limited due to the large number of customers and relatively small account balances within the majority of the Company's customer base and their dispersion across different businesses. The Company periodically evaluates the financial strength of its customers and believes that its credit risk exposure is limited.

Most of the Company's product purchases are from overseas vendors, the majority of which are from a limited number of Japanese suppliers. Although the Company currently sources products from a number of manufacturers throughout the world, a significant portion of new copier equipment is currently obtained from one supplier although the Company has recently added a new supplier, in part, to mitigate this risk. If this supplier were unable to deliver products for a significant period of time, the Company would be required to find replacement products from an alternative supplier or suppliers, which may not be available on a timely or cost effective basis. The Company's operating results could be adversely affected if its significant supplier is unable to deliver sufficient product.

### 5. EARNINGS PER SHARE CALCULATION

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Basic earnings per share was calculated by dividing net income available to common stockholders by the weighted average number of common shares outstanding during the period. Since the Distribution was not effective until December 3, 2001, the weighted average number of common shares outstanding for periods prior to the Distribution was assumed to be the number of shares issued in the Distribution.

A reconciliation of the basic and diluted earnings per share computation is as follows:

	THREE MONTHS ENDED SEPTEMBER 30,	
	2002	2001
Net income available to common stockholders	\$ 4,155	\$ 282
Weighted average common shares outstanding	18,336,310	19,463,007
Less: non-vested restricted stock	347,000	-
Weighted average common shares for basic earnings per share	17,989,310	19,463,007
Add: dilutive effect of restricted stock	347,000	-
Add: dilutive effect of stock options	201,301	16,114
Weighted average common shares and equivalents for diluted earnings per share	18,537,611	19,479,121
Basic earnings per share	\$ 0.23	\$ 0.01
Diluted earnings per share	\$ 0.22	\$ 0.01

### 6. LONG-TERM DEBT

Long-term debt consists of the following:

	SEPTEMBER 30, 2002	DECEMBER 31, 2001
Revolving credit facility	\$ -	\$ 17,000
Term loan	74,335	100,000
Total debt	74,335	117,000
Less: current maturities	749	1,000
Total long-term debt	\$ 73,586	\$ 116,000

On November 9, 2001 the Company entered into a Credit Agreement with a group of lenders (the "Credit Agreement") that provided for secured borrowings and the issuance of letters of credit in an aggregate amount not to exceed \$225

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million, comprised of a \$125 million Revolving Credit Facility (the "Revolving Credit Facility") and a \$100 million Term Loan (the "Term Loan"). The Credit Agreement requires us to manage our interest rate risk with respect to at least 50% of the aggregate principal amount of the Term Loan for a period of at least 36 months. Accordingly, we entered into two interest rate swap agreements in notional amounts of \$50 million and \$30 million to convert the variable interest rate payable on the Term Loan to a fixed interest rate in order to hedge the exposure to variability in expected future cash flows. These interest rate swap agreements have been designated as cash flow hedges.

On March 19, 2002, the Credit Agreement was amended to increase the total amount of the Company's stock permitted to be repurchased from \$20 million to \$30 million. On July 19, 2002, the Credit Agreement was further amended to increase the total amount of the Company's stock permitted to be repurchased from \$30 million to \$58 million and to reduce the Term Loan interest rates to LIBOR plus a margin of from 2.75% to 3.75%, from LIBOR plus a margin of from 3.50% to 3.75%, depending on our leverage ratio, or to the Fleet Bank base lending rate plus a margin of from 1.75% to 2.75%, from the Fleet Bank base lending rate plus a margin of from 2.50% to 2.75%, depending on our leverage ratio.

During the third quarter, we revised our cash flow estimates and prepaid \$8 million of the amount outstanding under the Term Loan. This prepayment was covered by a portion of the \$30 million interest rate swap agreement that had been designated as a cash flow hedge. Since it is no longer probable that the hedged forecasted transactions related to the \$8 million Term Loan prepayment will occur, we recognized a loss related to that portion of the swap agreement underlying the amount of the prepayment by reclassifying \$386 from accumulated other comprehensive loss into interest expense. We also unwound \$8 million of the \$30 million interest rate swap agreement.

### 7. COMMITMENTS AND CONTINGENCIES

Legal matters. In connection with the Distribution, the Company agreed to assume all liabilities associated with the Company's business, and to indemnify Pitney Bowes for all claims relating to the Company's business, including lawsuits relating to the Company's business. In the normal course of business, the Company and Pitney Bowes have been named as a party to occasional lawsuits relating to the Company's business. These lawsuits and other claims may involve disputes relating to, among other things, contractual rights under vendor, insurance or other contracts, trademark, patent or other intellectual property rights, equipment, service or payment disputes with customers and disputes with employees.

In connection with the Distribution, liabilities were transferred to the Company for matters where Pitney Bowes was a plaintiff or a defendant in lawsuits, relating to the business or products of the Company. The Company has not recorded liabilities for loss contingencies since the ultimate resolutions of the legal matters cannot be determined. In the opinion of the Company's management, none of these proceedings, individually or in the aggregate, should have a material adverse effect on the Company's financial position, results of operations or cash flows.

Risks and uncertainties. The Company has a limited history operating as an independent entity, may be unable to make the changes necessary to operate successfully as a stand-alone entity, or may incur greater costs as a stand-alone entity that may cause the Company's profitability to decline. Prior to the Distribution, the Company's business was operated by Pitney Bowes as a segment of its broader corporate organization rather than as a separate stand-alone entity. Pitney Bowes assisted the Company by providing corporate functions such as legal, tax and information technology functions. Following the Distribution, Pitney Bowes has no obligation to provide assistance to the

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Company other than certain interim and transitional services to be provided by Pitney Bowes. Because the Company's business had not previously been operated as a stand-alone entity, there can be no assurance that the Company will be able to successfully implement the changes necessary to operate independently or will not incur additional costs as a result of operating independently. The Company is implementing an enterprise resource planning ("ERP") system intended to replace the information technology ("IT") services provided by Pitney Bowes under the transition services agreement. Due to unanticipated delays in implementation of the ERP system, the Company has entered into discussions with Pitney Bowes regarding the extension until December 2003, of the transition services agreement as it relates to IT related services. Before entering into any extension of these transition services beyond June 2003 we will seek the approval by the Internal Revenue Service (IRS) of a ruling request confirming that such extension will not affect the tax-free nature of the spin-off. The Company is working together with Pitney Bowes to prepare and file the necessary ruling request. Although the Company expects that the ruling request will be granted in the ordinary course and that Pitney Bowes will continue to provide the IT related services during the period necessary for the Company to implement business critical ERP applications, there can be no assurance that the IRS will provide the requested ruling or that Pitney Bowes will grant the necessary extension of the IT related services. Any failure to obtain a favorable IRS ruling or to extend the required IT related services for the period required to permit the Company to implement replacement systems would have a material adverse affect on the operations and financial position of the Company.

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### 8. SEPARATION AGREEMENTS

The Company and Pitney Bowes entered into a transition services agreement that provides for Pitney Bowes to supply certain services to the Company, on a transitional basis. These services include information technology, computing, telecommunications, accounting, field service of equipment and dispatch call center services. In 2002, the Company will pay Pitney Bowes for its costs for the services provided, including a proportionate share of its overhead, if applicable, computed in accordance with Pitney Bowes' internal charge back practices. For the three and nine months ended September 30, 2002, the Company paid Pitney Bowes \$4.9 million and \$17.1 million, respectively, in connection with the transition services agreement.

Upon extension of the transition services agreement for IT related services as discussed in note 7, Commitments and Contingencies, above, the fees for such services would be set at a rate negotiated at arms length and would likely be significantly higher than the cost based fees for such services currently applicable.

The Company also entered into certain other agreements covering intellectual property, commercial relationships and leases and licensing arrangements. The pricing terms of the products and services covered by the other commercial agreements reflect negotiated prices.

The Company and Pitney Bowes entered into a tax separation agreement, which governs the Company's and Pitney Bowes' respective rights, responsibilities and obligations after the Distribution with respect to taxes for the periods ending on or before the Distribution. In addition, the tax separation agreement generally obligates the Company not to enter into any transaction that would adversely affect the tax-free nature of the Distribution for the two-year period following the Distribution, and obligates the Company to indemnify Pitney Bowes and affiliates to the extent that any action the Company takes or fails to take gives rise to a tax liability with respect to the Distribution.

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### ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with the audited consolidated financial statements and the notes thereto, included in the Company's latest Annual Report on Form 10-K for the year ended December 31, 2001 filed with the Securities and Exchange Commission on March 28, 2002, as well as the unaudited consolidated financial statements and notes thereto included elsewhere in this Quarterly Report on Form 10-Q. This Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements that involve risks and uncertainties. Please see "Risk Factors That Could Cause Results To Vary" and "Special Note About Forward-Looking Statements" for a discussion of the uncertainties, risks and assumptions associated with these forward-looking statements. Our actual results could differ materially from those forward-looking statements discussed in this section. For the purposes of the following discussion, unless the context otherwise requires, "Imagistics International Inc.," "Imagistics," and "the Company" refer to Imagistics International Inc. and subsidiary.

The unaudited consolidated financial statements have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC") and, in the opinion of the Company, include all adjustments (consisting of normal recurring accruals) necessary for a fair presentation of results of operations, financial position and cash flows as of and for the periods presented. The Company believes that the disclosures contained in the unaudited consolidated financial statements are adequate to keep the information presented from being misleading. The results for the three and nine months ended September 30, 2002 are not necessarily indicative of the results for the full year.

#### CRITICAL ACCOUNTING POLICIES AND SIGNIFICANT ESTIMATES

##### REVENUE RECOGNITION

Our revenues include revenues from the sale, rental and service of copiers, facsimile machines, multi-functional products and other document imaging equipment, including related supplies. Sales revenue is recognized when contractual obligations have been satisfied, title and risk of loss have been transferred to the customer and collection of the resulting receivable is reasonably assured. Certain rental contracts provide for invoicing in advance, generally quarterly. The revenue billed in advance is deferred and recognized as earned revenue over the billed period. Certain rental contracts provide for invoicing in arrears, generally quarterly. Revenue on contracts billed in arrears is accrued and recognized in the period in which it is earned. Rental terms generally range from one to three years. Support services revenue is recognized over the term of the service contract.

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##### OVERVIEW

Imagistics is a large independent direct sales, service and marketing organization offering document imaging solutions, including copiers, facsimile machines and multifunctional products, primarily to large corporate and government customers known as national accounts, as well as to mid-size and regional businesses known as commercial accounts. In addition, we offer a range of copier and multi-functional product document imaging options, including digital, analog, color and/or networked products and systems.

Our strategy is to become the leading independent provider of enterprise

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office imaging and document solutions by leveraging our product and marketplace strengths in customer support to drive customer loyalty. Our goal is also to achieve operational excellence and benchmark productivity and to pursue opportunistic expansion and investments.

### REVENUES

(Dollars in thousands)

The following table shows our revenue sources by product line for the periods indicated.

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	2002	2001	2002	2001
Copier product line	\$ 91,440	\$ 91,999	\$266,407	\$264,751
Facsimile product line	59,904	65,800	184,951	200,220
Sales to Pitney Bowes Canada	4,725	523	18,163	2,370
<b>Total revenue</b>	<b>\$156,069</b>	<b>\$158,322</b>	<b>\$469,521</b>	<b>\$467,341</b>

The following table shows our revenue sources by segment for the periods indicated.

	THREE MONTHS ENDED SEPTEMBER 30,		NINE MONTHS ENDED SEPTEMBER 30,	
	2002	2001	2002	2001
United States	\$150,368	\$153,286	\$453,388	\$451,874
United Kingdom	5,701	5,036	16,133	15,467
<b>Total revenue</b>	<b>\$156,069</b>	<b>\$158,322</b>	<b>\$469,521</b>	<b>\$467,341</b>

The following table shows the growth rates by revenue type and product line for the three and nine months ended September 30, 2002 compared with the same period in the prior year.

	FOR THE THREE MONTHS ENDED SEPTEMBER 30,	FOR THE NINE MONTHS ENDED SEPTEMBER 30,
<b>Sales</b>		
Copier products	(3.4%)	2.0%
Facsimile products	(4.2%)	(1.8%)
<b>Total sales</b>	<b>(3.6%)</b>	<b>0.7%</b>
<b>Rentals</b>		
Copier products	13.2%	9.6%
Facsimile products	(8.8%)	(6.3%)
<b>Total rentals</b>	<b>(0.8%)</b>	<b>(0.7%)</b>
<b>Support services</b>	<b>5.7%</b>	<b>2.9%</b>
<b>Total revenue</b>	<b>(1.4%)</b>	<b>0.5%</b>

## RESULTS OF OPERATIONS

The following table shows our statement of income data, expressed as a percentage of total revenue, for the periods indicated. The table also shows cost of sales as a percentage of sales revenue and cost of rentals as a percentage of rental revenue:

	AS A % OF TOTAL REVENUE, EXCEPT AS NOTED		
	THREE MONTHS ENDED SEPTEMBER 30, 2002	THREE MONTHS ENDED SEPTEMBER 30, 2001	NINE MONTHS ENDED SEPTEMBER 30, 2001
Revenue:			
Sales	49.4 %	50.5 %	
Rentals	37.2	37.0	
Support services	13.4	12.5	
Total revenue	100.0	100.0	100.0
Cost of sales	30.3	30.8	
Cost of rentals	13.4	14.9	
Selling, service and administrative	50.4	52.4	
Earnings before interest and taxes	5.9	1.9	
Interest expense	1.4	1.7	
Income before income taxes	4.5	0.2	
Provision for income taxes	1.8	-	
Net income	2.7 %	0.2 %	
Cost of sales as a percentage of sales revenue			
Including Pitney Bowes Canada	61.3 %	61.0 %	
Excluding Pitney Bowes Canada	59.0 %	60.8 %	
Excluding inventory obsolescence and Pitney Bowes Canada	55.1 %	55.2 %	
Cost of rentals as a percentage of rental revenue	36.1 %	40.2 %	
Effective tax rate	39.7 %	27.3 %	



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Revenue. For the three months ended September 30, 2002, total revenue of \$156,069 declined 1% versus revenue of \$158,322 for the three months ended September 30, 2001 reflecting lower sales and rental revenue, partially offset by higher support service revenue. Revenue attributable to sales to Pitney Bowes Canada pursuant to a reseller agreement between the Company and Pitney Bowes Canada that became effective upon the Distribution, amounted to \$4,725. Excluding the impact of sales to Pitney Bowes Canada, total revenue declined 4% versus the prior year.

Equipment and supply sales revenue of \$77,081 declined 4% for the three months ended September 30, 2002 from \$79,998 for the three months ended September 30, 2001. Excluding the impact of sales to Pitney Bowes Canada, total sales revenue declined 9% compared with the prior year. Total copier sales revenue declined 8% due to lower equipment and supply sales. Total facsimile sales revenue declined 12% on reduced equipment and supply sales.

Equipment rental revenue of \$58,088 for the three months ended September 30, 2002 declined slightly versus equipment rental revenue of \$58,549 for the three months ended September 30, 2001, reflecting lower facsimile rental revenues partially offset by an increase in copier rental revenues resulting from a continuing copier marketing focus on national accounts, which prefer a rental placement strategy similar to that of our facsimile product placement strategy. We continued to implement this strategic shift in our copier systems product line by increasing the focus on renting our copiers, responding to a need for flexible office equipment procurement options in the national account marketplace. Rental revenue derived from our copier product line increased 13% reflecting growth in the overall installed rental population as well as the impact of increased placements of our high-end digital products. Rental revenue from our facsimile product line declined 9% versus the prior year reflecting lower pricing and a lower installed base.

Support services revenue for the three months ended September 30, 2002 of \$20,900, primarily derived from stand-alone service contracts, increased 6% versus support services revenue of \$19,775 for the three months ended September 30, 2001, reflecting the combination of higher contract pricing associated with the increased placement of high end digital products in the United States and increased facsimile placements in the United Kingdom.

Cost of sales. Cost of sales was \$47,236 for the three months ended September 30, 2002 compared with \$48,816 for the same period in 2001 and as a percentage of sales revenue increased to 61.3% from 61.0%. This increase resulted from lower pricing on equipment sales to Pitney Bowes Canada under the reseller agreement and an increase in the mix of copier and multifunctional products which have a higher cost of sales percentage than facsimile sales, partially offset by lower product costs and lower provision for obsolete inventory. The provision for obsolete inventory declined \$1,735 in the United States geographic segment and increased \$48 in the United Kingdom geographic segment. Excluding the provision for obsolete inventory and sales to Pitney Bowes Canada, cost of sales as a percentage of revenue declined 0.1 percentage points to 55.1%.

Cost of rentals. Cost of rentals was \$20,991 for the three months ended September 30, 2002 compared with \$23,526 for the three months ended September 30, 2001 and as a percentage of rental revenue declined 4.1 percentage points to 36.1% for the three months ended September 30, 2002 from 40.2% for the three months ended September 30, 2001. This decline was due to the impact of our disciplined focus on improving profit margins coupled with product cost improvements, partially offset by an increase in the mix of copier and multifunctional product rentals which have a higher cost as a percentage of rental revenue than facsimile machines.

Selling, service and administrative expenses. Selling, service and

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administrative expenses of \$78,707 were 50.4% of total revenue for the three months ended September 30, 2002 compared with \$82,956, or 52.4% of total revenue for the three months ended September 30, 2001. Selling, service and administrative expenses declined 5% versus prior year reflecting lower accounts receivable write-offs, the impact of fewer employees and the absence of severance charges recorded during the third quarter of 2001, partially offset by advertising expense associated with a major brand awareness campaign and the expenditures for Enterprise Resource Planning ("ERP") technology designed to improve long term operational efficiency and deliver higher levels of customer support and service. Of the \$4,249 decline in selling, service and administrative expenses, United States geographic segment expenses declined \$4,329, while United Kingdom geographic segment expenses increased \$80. Field sales and service operating expenses are included in selling, service and administrative expenses because no meaningful allocation of these expenses to cost of sales, cost of rentals or cost of support services is practicable.

Earnings before interest and taxes. Earnings before interest and taxes were \$9,135 or 5.9% of total revenue for the three months ended September 30, 2002 compared with \$3,024 or 1.9% of total revenue for the three months ended September 30, 2001.

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Interest expense. Interest expense was \$2,240 for the three months ended September 30, 2002 compared with \$2,636 for the three months ended September 30, 2001, primarily as a result of lower debt levels. Interest expense for the three months ended September 30, 2002 includes a loss of \$386 resulting from the prepayment of \$8 million of the Term Loan and associated unwinding of a portion of the interest rate swap agreements. Prior to the Distribution, we participated in Pitney Bowes' centralized cash management program, which was used to finance our operations and interest expense for the three months ended September 30, 2001 represents an allocation from Pitney Bowes based upon the proportion of our net assets to Pitney Bowes' net assets. The weighted average interest rate for the three months ended September 30, 2002 was 7.1%. The Pitney Bowes weighted average borrowing rate for the three months ended September 30, 2001 was 6.7%.

Effective tax rate. Our effective tax rate was 39.7% for the three months ended September 30, 2002 compared with 27.3% for the three months ended September 30, 2001. The low effective tax rate for the three months ended September 30, 2001 results from the tax provision associated with the United Kingdom geographic segment, offset by the tax benefit associated with the United States geographic segment, which is at a higher rate. For the three months ended September 30, 2001, our income was included in the Pitney Bowes consolidated income tax returns and income tax expense was calculated as if Imagistics and Pitney Bowes filed separate income tax returns.

NINE MONTHS ENDED SEPTEMBER 30, 2002 AND SEPTEMBER 30, 2001

Revenue. For the nine months ended September 30, 2002, total revenue of \$469,521 increased slightly versus revenue for the nine months ended September 30, 2001 of \$467,341 reflecting higher sales and support service revenue, partially offset by lower rental revenue. The increase in revenue is attributable to sales to Pitney Bowes Canada pursuant to the reseller agreement. Excluding the impact of sales to Pitney Bowes Canada, total revenue declined 3% versus the prior year.

Equipment and supply sales revenue increased 1% to \$232,645 for the nine months ended September 30, 2002 from \$231,041 for the nine months ended September 30, 2001. Excluding the impact of sales to Pitney Bowes Canada, total sales revenue declined 6% compared with the prior year. Total copier sales

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revenue declined 4% due to lower equipment and supply sales. Total facsimile sales revenue declined 11% on reduced equipment and supply sales.

Equipment rental revenue declined 1% to \$172,955 for the nine months ended September 30, 2002 from \$174,179 for the nine months ended September 30, 2001, reflecting a decline in facsimile rental revenue largely offset by an increase in copier rental revenue associated with the continuing copier marketing focus on national account placements. Rental revenue derived from our copier product line increased 10% reflecting growth in the overall installed rental population as well as the impact of increased placements of our high-end digital products. Rental revenue from our facsimile product line declined 6% versus the prior year reflecting lower pricing and a lower installed base.

Support services revenue, primarily derived from stand-alone service contracts, increased 3% to \$63,921 for the nine months ended September 30, 2002 from \$62,121 for the nine months ended September 30, 2001, reflecting higher contract pricing associated with changing product mix coupled with increased placements.

Cost of sales. Cost of sales was \$145,044 for the nine months ended September 30, 2002 compared with \$145,033 for the same period in 2001 and as a percentage of sales revenue declined to 62.3% from 62.8%. This decline resulted from lower provisions for obsolete inventory and product cost reductions partially offset by an increase in the mix of copier and multifunctional products which have a higher cost of sales percentage than facsimile sales. The provision for obsolete inventory declined \$7,234, of which \$2,696 is attributable to the United Kingdom geographic segment and \$4,538 is attributable to the United States geographic segment. Excluding the provision for obsolete inventory and sales to Pitney Bowes Canada, cost of sales as a percentage of revenue declined 0.1 percentage points to 54.8%.

Cost of rentals. Cost of rentals was \$64,446 for the nine months ended September 30, 2002 compared with \$69,837 for the nine months ended September 30, 2001 and as a percentage of rental revenue declined 2.8 percentage points to 37.3% for the nine months ended September 30, 2002 from 40.1% for the nine months ended September 30, 2001. This decline was due to the impact of our disciplined focus on improving profit margins coupled with product cost improvements, partially offset by an increase in the mix of copier and multifunctional product rentals, which have a higher cost as a percentage of rental revenue than facsimile machines.

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Selling, service and administrative expenses. Selling, service and administrative expenses of \$233,042 were 49.6% of total revenue for the nine months ended September 30, 2002 compared with \$222,718, or 47.7% of total revenue for the nine months ended September 30, 2001. Selling, service and administrative expenses increased 5% versus prior year reflecting increased finance and administrative costs associated with becoming an independent public company, the expenditures for ERP technology and advertising expenditures associated with a brand awareness campaign, partially offset by the impact of fewer employees and lower accounts receivable write offs. Of the \$10,324 increase in selling, service and administrative expenses, United States geographic segment expenses increased \$10,445 while United Kingdom geographic segment expenses declined \$121. Field sales and service operating expenses are included in selling, service and administrative expenses because no meaningful allocation of these expenses to cost of sales, cost of rentals or cost of support services is practicable.

Earnings before interest and taxes. Earnings before interest and taxes were

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\$26,989 or 5.8% of total revenue for the nine months ended September 30, 2002 compared with \$29,753 or 6.4% of total revenue for the nine months ended September 30, 2001.

Interest expense. Interest expense was \$6,429 for the nine months ended September 30, 2002 compared with \$8,484 for the nine months ended September 30, 2001, primarily as a result of lower debt levels. Interest expense for the nine months ended September 30, 2002 includes a loss of \$386 resulting from the prepayment of \$8 million of the Term Loan and associated unwinding of a portion of the interest rate swap agreements. Prior to the Distribution, we participated in Pitney Bowes' centralized cash management program, which was used to finance our operations. Interest expense for the nine months ended September 30, 2001 represents an allocation from Pitney Bowes based upon the proportion of our net assets to Pitney Bowes' net assets. The weighted average interest rate for the nine months ended September 30, 2002 was 7.1%. The Pitney Bowes weighted average borrowing rate for the nine months ended September 30, 2001 was 6.7%.

Effective tax rate. Our effective tax rate was 39.7% for the nine months ended September 30, 2002 compared with 39.5% for the nine months ended September 30, 2001. For the nine months ended September 30, 2001, our income was included in the Pitney Bowes consolidated income tax returns and income tax expense was calculated as if Imagistics and Pitney Bowes filed separate income tax returns.

### LIQUIDITY AND CAPITAL RESOURCES

On November 9, 2001 we entered into a Credit Agreement with a group of lenders. The Credit Agreement provides for secured borrowings and the issuance of letters of credit in an aggregate amount not to exceed \$225 million and was comprised of a \$125 million Revolving Credit Facility and a \$100 million Term Loan. The term of the Revolving Credit Facility is five years and the term of the Term Loan is six years. The original borrowings of \$100 million under the Term Loan were payable in 20 consecutive equal quarterly installments of \$0.3 million due March 31, 2002 through December 31, 2006, three consecutive equal quarterly installments of \$23.8 million due March 31, 2007 through September 30, 2007 and a final payment of \$23.8 million due at maturity. Our Credit Agreement received a BB+ rating from Standard & Poors and a rating of Ba3 from Moody's Investor Services.

We have pledged substantially all of our assets plus 65% of the stock of our subsidiary as security for our obligations under the Credit Agreement. Available borrowings and letter of credit issuance under the Revolving Credit Facility are determined by a borrowing base consisting of a percentage of our eligible accounts receivable, inventory, rental assets and accrued and advance billings, less outstanding borrowings under the Term Loan.

The Credit Agreement contains financial covenants that require the maintenance of minimum earnings before interest, taxes, depreciation and amortization and a maximum leverage ratio, as well as other covenants, which, among other things, place limits on dividend payments and capital expenditures. On March 19, 2002, we amended the Credit Agreement to increase the total amount of our stock permitted to be repurchased from \$20 million to \$30 million. We entered into a second amendment to the Credit Agreement on July 19, 2002 that increased the amount of our stock permitted to be repurchased from \$30 million to \$58 million. The Credit Agreement allows us to make acquisitions up to an aggregate consideration of \$30 million. At September 30, 2002, we were in compliance with all financial covenants and expect to continue to be in compliance with these covenants.

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Amounts borrowed under the Revolving Credit Facility bear interest at variable rates based, at our option, on either the LIBOR rate plus a margin of from 2.25% to 3.00%, depending on our leverage ratio, or the Fleet Bank base lending rate plus a margin of from 1.25% to 2.00%, depending on our leverage ratio. Amounts borrowed under the Term Loan bear interest, as amended by the second amendment, at variable rates based, at our option, on either the LIBOR rate plus a margin of from 2.75% to 3.75%, depending on our leverage ratio, or the Fleet Bank base lending rate plus a margin of from 1.75% to 2.75%, depending on our leverage ratio. A commitment fee of from 0.375% to 0.500%, depending on our leverage ratio, on the average daily unused portion of the Revolving Credit Facility is payable quarterly, in arrears. From July 1, 2002 through July 18, 2002, the interest rate on our Term Loan was LIBOR plus 3.50%. Since July 19, 2002, the interest rate on our Term Loan has been LIBOR plus 2.75%.

The Credit Agreement requires us to manage our interest rate risk with respect to at least 50% of the aggregate principal amount of the Term Loan for a period of at least 36 months. Accordingly, we entered into two interest rate swap agreements in notional amounts of \$50 million and \$30 million to convert the variable interest rate payable on the Term Loan to a fixed interest rate in order to hedge the exposure to variability in expected future cash flows. The two interest rate swap agreements expire in February 2005. These interest rate swap agreements have been designated as cash flow hedges. The counterparties to the interest rate swap agreements are major international financial institutions. We monitor the credit quality of these financial institutions and do not anticipate any losses as a result of counterparty non-performance. Under the terms of the swap agreements, we will receive payments based upon the 90-day LIBOR rate and will remit payments based upon a fixed rate. The fixed interest rates are 4.165% and 4.320% for the \$50 million and the \$30 million swap agreements, respectively. During the third quarter, we revised our cash flow estimates and prepaid \$8 million of the amount outstanding under the Term Loan. This prepayment was covered by a portion of the \$30 million interest rate swap agreement that had been designated as a cash flow hedge. Since it is no longer probable that the hedged forecasted transactions related to the \$8 million Term Loan prepayment will occur, we recognized a loss related to that portion of the swap agreement underlying the amount of the prepayment by reclassifying \$386 from accumulated other comprehensive loss into interest expense. We also unwound \$8 million of the \$30 million interest rate swap agreement. At September 30, 2002, two swap agreements in the notional amounts of \$50 million and \$22 million were outstanding, the aggregate fair value of which was an obligation of \$3.5 million, which was recorded in other liabilities. The unrealized loss relating to the outstanding swap agreements was included in accumulated other comprehensive loss in stockholders' equity. The interest rate swap agreements were 100% effective for the three and nine months ended September 30, 2002.

Our initial borrowings of \$150 million under the Credit Agreement, consisting of \$100 million under the Term Loan and \$50 million under the Revolving Credit Facility, were used to repay amounts due to Pitney Bowes and to pay a dividend to Pitney Bowes. At September 30, 2002, approximately \$74 million of borrowings were outstanding under the Credit Agreement, consisting solely of borrowings under the Term Loan. Based upon the borrowing base at September 30, 2002, substantially all of the Revolving Credit Facility is available for borrowing.

Historically, our cash flow has been positive as a result of our high percentage of recurring revenues from rental, supplies and service. We expect our cash flow to remain positive although we do expect our cash generation to moderate as the Company's ability to continue to provide cash through changes in working capital is reduced.

Net cash provided by operating activities was \$132,273 and \$105,863 for the nine months ended September 30, 2002 and 2001, respectively. Net income was \$12,392 and \$12,876, respectively. Non-cash charges for depreciation and

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amortization, accounts receivable write offs and inventory obsolescence provisions provided cash of \$73,997 and \$84,196 for the nine months ended September 30, 2002 and 2001, respectively. Changes in the principal components of working capital provided cash of \$40,533 and \$7,860 in the nine months ended September 30, 2002 and 2001, respectively. Of the \$40,533 of cash provided by working capital changes in the nine months ended September 30, 2002, approximately \$16 million was a result of accruals for stand-alone expenses such as employee benefits and incentive compensation, which had been included in amounts due to Pitney Bowes in periods prior to the Distribution.

We used \$53,583 and \$59,840 in investing activities for the nine months ended September 30, 2002 and 2001, respectively. Investment in rental equipment assets totaled \$38,723 and \$48,519 for the nine months ended September 30, 2002 and 2001, respectively. Capital expenditures for property, plant and equipment were \$14,860, and \$7,900 for the nine months ended September 30, 2002 and 2001, respectively. Investment in ERP accounted for \$9,138 of the capital expenditures for property, plant and equipment for the nine months ended September 30, 2002.

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Cash used in financing activities was \$72,628 for the nine months ended September 30, 2002 reflecting repayments under the Revolving Credit Facility and Term Loan and the repurchase of outstanding stock. As a result of repayments, the remaining outstanding borrowings under the Term Loan at September 30, 2002 are payable in 17 consecutive equal quarterly installments of \$0.2 million due December 31, 2002 through December 31, 2006, three consecutive equal quarterly installments of \$17.8 million due March 31, 2007 through September 30, 2007 and a final payment of \$17.8 million due at maturity. On March 27, 2002, we began repurchasing our stock under the \$30 million stock buy back program previously approved by the Board of Directors and, as of September 30, 2002, accumulated approximately 1.6 million shares of treasury stock at a cost of \$30 million. Cash used in financing activities in 2001 reflects decreases in amounts due to Pitney Bowes for corporate allocations and other intercompany charges. In October 2002, the Board of Directors authorized the repurchase of an additional \$28 million of our stock raising the total authorization to \$58 million.

The ratio of current assets to current liabilities declined to 2.6 to 1 at September 30, 2002 compared with 3.4 to 1 at December 31, 2001 due to reductions in accounts receivable and inventory and an increase in accounts payable and accrued liabilities. At September 30, 2002 our total debt as a percentage of total capitalization declined to 22% from 29% at December 31, 2001 due to debt repayments offset in part by stock repurchases.

We had no material commitments other than supply agreements with vendors that extend only to equipment ordered under purchase orders; there are no long-term purchase requirements. We will continue to make additional investments in facilities, rental equipment, computer equipment and systems and our distribution network as required to support our revenue growth. We anticipate investments in rental equipment assets for new and replacement programs in amounts consistent with prior years. We estimate that we will spend approximately \$30 million to \$35 million over the next 18-24 months to enhance our information systems infrastructure and implement our ERP system.

Our cash flow from operations, together with borrowings under the Credit Agreement, are expected to adequately finance our ordinary operating cash requirements and capital expenditures for the foreseeable future. We expect to fund further expansion and long-term growth primarily with cash flows from operations, borrowings under the Credit Agreement and possible future sales of additional equity or debt securities.

RISK FACTORS THAT COULD CAUSE RESULTS TO VARY

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### Risk Factors Relating to Separating Our Company From Pitney Bowes

We have only recently been operating as an independent entity and may be unable to make the changes necessary to operate effectively as a stand-alone entity or may incur greater costs as a stand-alone entity causing our profitability to decline.

Prior to the Distribution our business was operated as part of Pitney Bowes' broader corporate organization rather than as a stand-alone company. We are in the process of creating our own, or engaging third parties to provide systems, warehousing and distribution, service call center and dispatch services and other business functions to replace many of the systems and business functions historically provided by Pitney Bowes. There can be no assurance that we will be able to successfully implement these changes or will not incur additional costs as a result. In particular, we need to have our own IT and ERP systems in place in order to operate our business without interruption. Due to unanticipated delays in implementation of the ERP system, the Company has entered into discussions with Pitney Bowes regarding the extension of the transition services agreement as it relates to IT related services until December 2003. Before entering into any extension of these transition services beyond June 2003 we will seek the approval by the IRS of a ruling request confirming that such extension will not affect the tax-free nature of the spin-off. The Company is working together with Pitney Bowes to prepare and file the necessary ruling request. Although the Company expects that the ruling request will be granted in the ordinary course and that Pitney Bowes will continue to provide the IT related services during the period necessary for the Company to implement business critical ERP applications, there can be no assurance that the IRS will provide the requested ruling or that Pitney Bowes will grant the necessary extension of the IT related services. Any failure to obtain a favorable IRS ruling or to extend the required IT related services for the period required to permit the Company to implement replacement systems would have a material adverse affect on the operations and financial position of the Company.

Pitney Bowes has been and is expected to continue to be a significant customer. For the three and nine months ended September 30, 2002, revenues from Pitney Bowes, exclusive of equipment sales to PBCC for lease to the end user, accounted for 9.2% and 8.7% of our total revenue, respectively. However, no assurance can be given that Pitney Bowes will continue to purchase our products and services.

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In connection with the Distribution, Imagistics and Pitney Bowes entered into a non-exclusive intellectual property agreement that allows us to operate under the "Pitney Bowes" brand name for a term of up to two years after the Distribution. However, this agreement may be terminated if Pitney Bowes or we elect to terminate the non-competition obligations contained in the distribution agreement. In 2002, we began introducing products under the "Imagistics" brand name and we may be required to expend substantial resources to establish our new brand name. Brand name recognition is an important part of our overall business strategy and we cannot assure you that customers will maintain the same level of interest in our products when we are no longer associated with Pitney Bowes.

### Risk Factors Relating to Our Business

The document imaging and management industry is undergoing an evolution in product offerings, moving toward the use of digital and color technology in a multi-functional office environment. Our continued success will depend to a great extent on our ability to respond to this rapidly changing environment by

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providing new options and document imaging solutions for our customers.

The proliferation of e-mail, multi-functional printers and other technologies in the workplace may lead to a reduction in the use of traditional copiers and fax machines. We cannot anticipate whether other technological advancements will substantially minimize the need for our products in the future. Many of our rental customers have contract provisions allowing for technology and product upgrades during the term of their contract. If we have priced these upgrades improperly, this may have an adverse effect on our profitability and future business. If many of our customers exercise their contractual rights to upgrade to digital equipment, we may experience returns of a large number of analog machines and a subsequent loss of book value on these machines.

The document imaging solutions industry is very competitive and we may be unable to compete favorably, causing us to lose sales to our competitors. Our future success depends, in part, on our ability to deliver enhanced products and service packages while also offering competitive price levels.

We rely on outside suppliers to manufacture the products that we distribute, many of whom are located in the Far East. In addition, one manufacturer supplies a significant portion of our new copier equipment. If these manufacturers discontinue their products or are unable to deliver us products in the future or if political changes, economic disruptions or natural disasters occur where their production facilities are located, we will be forced to identify an alternative supplier for the product. Although we are confident that we can identify alternate sources of supply, we may not be successful in doing so. Even if we are successful, the replacement product may be more expensive or may lack certain features of the discontinued product and we will experience some delay in obtaining the product.

In addition, a substantial portion of the Company's equipment, supplies and spare parts inventory is sourced from the Far East and imported through West Coast ports. If the recent work stoppage at the West Coast docks were to resume after the end of the Taft-Hartley cooling off period, the Company would be required to re-route future inventory shipments to other ports, possibly resulting in sales disruptions, increased transportation expenses for future inventory shipments and the need to maintain higher levels of inventory. This could adversely affect the Company's operating results.

Other events that disrupt the shipment to or receipt of ocean freight at U.S. ports, such as future labor unrest, war or terrorist activity could delay, prevent or add substantial cost to the Company's receipt of such products. Any of these events would cause disruption to our customers and could have an adverse effect on our business.

Much of our international business is transacted in local currency. Currently, less than 30% of our total new product, supplies and parts purchases, based on costs, are denominated in yen. We do not currently utilize any form of derivative financial instruments to manage our exchange rate risk. We manage our foreign exchange risk by attempting to pass through to our customers any cost increases related to foreign currency exchange. However, no assurance can be given that we will be successful in passing cost increases through to our customers in the future.

A substantial majority of our new equipment is produced in China. Products produced in China are not currently eligible for inclusion on the Federal Government Services Administration ("GSA") Schedule. Inclusion on the GSA Schedule is often required before federal government and other state and local governmental customers will consider these products for rental or purchase. If products produced in China are not approved for listing on the GSA Schedule, our ability to maintain our business with these governmental customers could be



impaired.

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Governmental contracts typically contain provisions permitting the governmental customers to terminate the contract if funds for such contracts are not appropriated by the applicable legislative body. In addition, many of our rental agreements with governmental customers and certain other customers contain provisions allowing early termination in whole or in part. Historically there has not been a significant number of contract terminations, however, we can provide no assurance that our business will not be adversely affected by early rental contract terminations.

#### SPECIAL NOTE ABOUT FORWARD-LOOKING STATEMENTS

Statements contained in this discussion and elsewhere in this report that are not purely historical are forward-looking statements, within the meaning of the Private Securities Litigation Reform Act of 1995, and are based on management's beliefs, certain assumptions and current expectations. These statements may be identified by their use of forward-looking terminology such as the words "expects", "projects", "anticipates", "intends" and other similar words. Such forward-looking statements involve risks and uncertainties that could cause actual results to differ materially from those projected. The forward-looking statements contained herein are made as of the date hereof and, except as required by law, we do not undertake any obligation to update any forward-looking statements, whether as a result of future events, new information or otherwise.

#### RECENT ACCOUNTING PRONOUNCEMENTS

In August 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 143, "Accounting for Asset Retirement Obligations." SFAS No. 143 requires the recognition of an asset retirement obligation when an entity incurs a legal obligation associated with the retirement of a tangible long-lived asset and the amount of the liability can be reasonably estimated. We will adopt SFAS No. 143 on January 1, 2003. We are currently assessing the effect, if any, SFAS No. 143 may have on our financial position, results of operations, or cash flows.

In October 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." SFAS No. 144 supercedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and of Long-Lived Assets to be Disposed of" and establishes accounting and reporting standards for long-lived assets, excluding goodwill, to be used, held for sale or disposed of other than by sale. SFAS No. 144 requires an entity to recognize an impairment loss in an amount equal to the difference between the carrying amount of the long-lived asset and its fair value if the carrying amount of the asset is not recoverable from undiscounted cash flows. We adopted SFAS No. 144 effective January 1, 2002. The adoption of this accounting standard did not have a material impact on our consolidated financial position, results of operations, or cash flows.

In April 2002, the FASB issued SFAS No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections." SFAS No. 145 updates, clarifies and simplifies existing accounting pronouncements. As a result of rescinding SFAS No. 4 and SFAS No. 64, the criteria in Accounting Principles Bulletin No. 30 will be used to classify gains and losses from extinguishment of debt. We will adopt SFAS No. 145 on January 1, 2003. The adoption of SFAS No. 145 will not have a material impact on our financial position, results of operations, or cash flows.

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In September 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." SFAS No. 146 provides guidance on the recognition and measurement of liabilities associated with disposal activities. We will adopt SFAS No. 146 on January 1, 2003. We are currently assessing the effect, if any, SFAS No. 146 may have on our financial position, results of operations, or cash flows.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We have certain exposures to market risk related to changes in interest rates, foreign currency exchange rates and commodities. There have been no material changes in market risk since the filing of our Annual Report on Form 10-K for the fiscal year ended December 31, 2001.

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### ITEM 4. CONTROLS AND PROCEDURES

Within the 90 days prior to the date of this report, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as described in Exchange Act Rule 13a-14. In conducting the evaluation, such officers noted that we continued to be reliant on certain Pitney Bowes information systems for the generation of financial information. Based upon our existing internal controls, such officers' knowledge of Pitney Bowes' systems and internal controls and a review of Pitney Bowes' Exchange Act filings and related certifications, the Chief Executive Officer and the Chief Financial Officer have concluded that the information generated by the Pitney Bowes information systems is subject to adequate controls. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective in timely alerting them to material information required to be included in our periodic SEC filings relating to the Company (including its consolidated subsidiary).

There were no significant changes in our internal controls or in other factors that could significantly affect these internal controls subsequent to the date of our most recent evaluation.

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## PART II - OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

#### LEGAL MATTERS

In connection with the Distribution, we agreed to assume all liabilities associated with our business, and to indemnify Pitney Bowes for all claims relating to our business. In the course of normal business, we have been party to occasional lawsuits relating to our business. These may involve litigation or other claims by or against Pitney Bowes or Imagistics relating to, among other things, contractual rights under vendor, insurance or other contracts, trademark, patent and other intellectual property rights, equipment, service or payment disputes with customers and disputes with employees.

In connection with the Distribution, liabilities were transferred to us for matters where Pitney Bowes was a plaintiff or a defendant in lawsuits relating to our business or products. We have not recorded liabilities for loss

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contingencies since the ultimate resolutions of the legal matters cannot be determined and a minimum cost or amount of loss cannot be reasonably estimated. In our opinion, none of these proceedings, individually or in the aggregate, should have a material adverse effect on our consolidated financial position, results of operations or cash flows.

### ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits. The following documents are filed as exhibits hereto:

EXHIBIT NUMBER -----	DESCRIPTION -----
3.1	Amended and Restated Certificate of Incorporation (3)
3.2	Amended and Restated Bylaws (1)
3.3	Certificate of Designation of Series A Junior Participating Preferred Stock, dated August 1, 2002 (6)
4.1	Form of Imagistics International Inc. Common Stock Certificate (1)
10.1	Tax Separation Agreement between Pitney Bowes Inc. and Imagistics International Inc. (3)
10.2	Transition Services Agreement between Pitney Bowes Inc. and Imagistics International Inc. (3)
10.3	Distribution Agreement between Pitney Bowes Inc. and Imagistics International Inc. (3)
10.4	Intellectual Property Agreement between Pitney Bowes Inc. and Imagistics International Inc. (3)
10.5	Reseller Agreement between Pitney Bowes Management Services and Imagistics International Inc. (3)
10.6	Reseller Agreement between Pitney Bowes of Canada and Imagistics International Inc. (3)
10.7	Vendor Financing Agreement between Pitney Bowes Credit Corporation and Imagistics International Inc. (3)
10.8	Form of Sublease Agreement between Pitney Bowes Inc. and Imagistics International Inc. (2)
10.9	Form of Sublease and License Agreement between Pitney Bowes Inc. and Imagistics International Inc. (2)
10.10	Form of Assignment and Novation Agreement between Pitney Bowes Inc. and Imagistics International Inc. (2)
10.11	Imagistics International Inc. 2001 Stock Plan (1)
10.12	Imagistics International Inc. Key Employees' Incentive Plan (3)
10.13	Imagistics International Inc. Non-Employee Directors' Stock Plan (1)
10.14	Letter Agreement between Pitney Bowes Inc. and Marc C. Breslawsky (1)
10.15	Letter Agreement between Pitney Bowes Inc. and Joseph D. Skrzypczak (1)
10.16	Letter Agreement between Pitney Bowes Inc. and Mark S. Flynn (1)
10.17	Credit Agreement between Imagistics International Inc. and Merrill Lynch, Merrill Lynch, Pierce Fenner & Smith Incorporated, as Syndication Agent, Fleet Capital Corporation, as Administrative Agent (3)
10.18	Rights Agreement between Imagistics International Inc. and EquiServe Trust Company, N.A. (3)
10.19	Employment Agreement between Imagistics International Inc. and Marc C. Breslawsky (3)
10.20	Employment Agreement between Imagistics International Inc. and Joseph D. Skrzypczak (3)
10.21	Employment Agreement between Imagistics International Inc. and Christine B. Allen (3)
10.22	Employment Agreement between Imagistics International Inc. and John C. Chillock (3)
10.23	Employment Agreement between Imagistics International Inc. and Chris C. Dewart (3)
10.24	Employment Agreement between Imagistics International Inc. and Mark S. Flynn (3)
10.25	Employment Agreement between Imagistics International Inc. and

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- Nathaniel M. Gifford (3)  
10.26 Employment Agreement between Imagistics International Inc. and Joseph W. Higgins (3)  
10.27 Amendment No. 1 to Credit Agreement between Imagistics International and Merrill Lynch & Co., Merrill Lynch, Pierce, Fenner & Smith, as Syndication Agent, Fleet Capital Corporation, as Administrative Agent, and the Lenders identified therein (4)

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- 10.28 Amendment No. 2 to Credit Agreement between Imagistics International and Merrill Lynch & Co., Merrill Lynch, Pierce, Fenner & Smith, as Syndication Agent, Fleet Capital Corporation, as Administrative Agent, and the Lenders identified therein (5)  
10.29 First Amendment to Imagistics International Inc. 2001 Stock Plan (6)  
10.30 First Amendment to Rights Agreement between Imagistics International Inc. and EquiServe Trust Company, N.A. (6)  
13.1 Portions of the 2001 Annual Report to Stockholders (3)  
18.1 Preferability letter from PricewaterhouseCoopers regarding change in accounting principle (3)  
21.1 Subsidiaries of Imagistics International Inc. (3)  
23.1 Consent of PricewaterhouseCoopers LLP (3)

- (1) Incorporated by reference to Amendment No. 1 to the Registrant's Form 10 filed July 13, 2001.  
(2) Incorporated by reference to Amendment No. 2 to the Registrant's Form 10 filed August 13, 2001.  
(3) Incorporated by reference to Registrant's Form 10-K filed March 28, 2002.  
(4) Incorporated by reference to Registrant's Form 10-Q filed May 14, 2002.  
(5) Incorporated by reference to the Registrant's Form 8-K dated July 23, 2002.  
(6) Incorporated by reference to the Registrant's Form 10-Q filed August 14, 2002.  
  
(b) Reports on Form 8-K.

On July 23, 2002, the Company filed a Current Report on Form 8-K, reporting under Item 5 thereof, the Second Amendment to the Credit Agreement, dated as of July 19, 2002.

On September 20, 2002, the Company filed a Current Report on Form 8-K, reporting under Item 9 thereof, the resignation of Michael J. Critelli as a member of the board of directors and governance committee of the Company effective as of September 30, 2002.

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SIGNATURES

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

Date: November 13, 2002

Imagistics International Inc.

-----  
(Registrant)

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By: /s/ Joseph D. Skrzypczak  
-----  
Name: Joseph D. Skrzypczak  
Title: Chief Financial Officer  
and Authorized Signatory

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CERTIFICATION

I, Marc C. Breslawsky, certify that,

1. I have reviewed this quarterly report on Form 10-Q of Imagistics International Inc.;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
  - a) Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiary, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - c) Presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

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- a) All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: November 13, 2002 /s/ Marc C. Breslawsky  
Chief Executive Officer

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### CERTIFICATION

I, Joseph D. Skrzypczak, certify that,

1. I have reviewed this quarterly report on Form 10-Q of Imagistics International Inc.;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:
  - a) Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiary, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - c) Presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our

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evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):
- a) All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: November 13, 2002

/s/ Joseph D. Skrzypczak

Chief Financial Officer