

Quad/Graphics, Inc.  
Form 10-Q  
August 11, 2011  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q

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

For the quarterly period ended June 30, 2011

or

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

For the transition period from to  
Commission File Number 001-34806

QUAD/GRAPHICS, INC.

(Exact name of Registrant as specified in its charter)

Wisconsin

(State or other jurisdiction of  
incorporation or organization)

N63 W23075 Highway 74, Sussex, Wisconsin 53089-2827

(Address of principal executive offices) (Zip Code)

39-1152983

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

(414) 566 – 6000

(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 has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No "

Yes x No "

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

Large accelerated filer o

Accelerated filer o

Non-accelerated filer x

Smaller reporting company o

(Do not check if a smaller reporting company)

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date.

Class

Outstanding as of August 11, 2011

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Class A Common Stock	32,846,125
Class B Common Stock	14,198,464
Class C Common Stock	245,353

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## PART I — FINANCIAL INFORMATION

## ITEM 1. Condensed Consolidated Financial Statements

## QUAD/GRAPHICS, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in millions, except per share data)

(UNAUDITED)

	Three Months Ended June		Six Months Ended June 30,	
	30, 2011	2010	2011	2010
Net sales				
Products	\$952.4	\$345.5	\$1,933.2	\$696.8
Services	118.1	48.8	239.6	101.1
Total net sales	1,070.5	394.3	2,172.8	797.9
Cost of sales				
Products	737.5	255.4	1,501.0	515.7
Services	94.5	33.8	184.4	69.9
Total cost of sales	832.0	289.2	1,685.4	585.6
Selling, general and administrative expenses	112.0	49.3	221.0	96.9
Depreciation and amortization	87.7	48.2	178.2	97.5
Restructuring, impairment and transaction-related charges	23.4	31.3	58.2	37.6
Total operating expenses	1,055.1	418.0	2,142.8	817.6
Operating income (loss)	15.4	(23.7)	30.0	(19.7)
Interest expense	29.5	15.0	59.4	30.3
Loss before income taxes and equity in earnings of unconsolidated entities	(14.1)	(38.7)	(29.4)	(50.0)
Income tax benefit	(3.6)	(1.5)	(10.8)	(1.6)
Loss before equity in earnings of unconsolidated entities	(10.5)	(37.2)	(18.6)	(48.4)
Equity in earnings of unconsolidated entities	0.3	1.6	1.1	4.3
Net loss	\$(10.2)	\$(35.6)	\$(17.5)	\$(44.1)
Net earnings attributable to noncontrolling interests	(0.1)	(0.1)	(0.1)	(0.1)
Net loss attributable to Quad/Graphics common shareholders	\$(10.3)	\$(35.7)	\$(17.6)	\$(44.2)
Loss per share attributable to Quad/Graphics common shareholders:				
Basic and Diluted	\$(0.22)	\$(1.27)	\$(0.37)	\$(1.57)

Weighted average number of common shares outstanding:

Basic and Diluted	47.3	28.1	47.3	28.1
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See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited).

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QUAD/GRAPHICS, INC.  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 (in millions)  
 (UNAUDITED)

	June 30, 2011	December 31, 2010
<b>ASSETS</b>		
Cash and cash equivalents	\$ 16.6	\$ 20.5
Receivables, less allowances for doubtful accounts of \$78.5 at June 30, 2011 and \$85.5 at December 31, 2010	649.0	786.4
Inventories	279.7	247.4
Prepaid expenses and other current assets	114.2	64.3
Deferred income taxes	90.6	76.8
Short-term restricted cash	3.1	16.0
 Total current assets	 1,153.2	 1,211.4
Property, plant and equipment—net	2,286.7	2,317.8
Goodwill	803.7	814.7
Other intangible assets—net	335.8	368.3
Long-term restricted cash	80.1	84.5
Equity method investments in unconsolidated entities	85.5	82.5
Other long-term assets	58.4	67.8
 Total assets	 \$ 4,803.4	 \$ 4,947.0
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Accounts payable	\$ 292.8	\$ 332.4
Amounts owing in satisfaction of bankruptcy claims	23.3	26.1
Accrued liabilities	362.8	427.1
Short-term debt and current portion of long-term debt	88.1	102.6
Current portion of capital lease obligations	23.5	14.5
 Total current liabilities	 790.5	 902.7
Long-term debt	1,424.9	1,418.4
Unsecured notes to be issued	44.5	52.5
Capital lease obligations	25.4	43.2
Deferred income taxes	464.3	433.8
Other long-term liabilities	561.2	603.8
 Total liabilities	 3,310.8	 3,454.4
 Commitments and contingencies (Note 10)		
 Redeemable equity (Note 19)	 10.0	 10.6
 Quad/Graphics common stock and other equity (Note 19)		
Preferred stock	—	—

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Common stock, Class A	1.0	1.0
Common stock, Class B	0.4	0.4
Common stock, Class C	—	—
Additional paid-in capital	999.2	1,002.0
Treasury stock, at cost	(287.7	) (295.7
Retained earnings	689.7	720.9
Accumulated other comprehensive income	79.5	52.7
Quad/Graphics common stock and other equity	1,482.1	1,481.3
Noncontrolling interests	0.5	0.7
Total common stock and other equity and noncontrolling interests	1,482.6	1,482.0
Total liabilities and shareholders' equity	\$4,803.4	\$4,947.0

See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited).

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QUAD/GRAPHICS, INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 (in millions)  
 (UNAUDITED)

	Six Months Ended June 30,	
	2011	2010
<b>OPERATING ACTIVITIES</b>		
Net loss	\$(17.5	) \$(44.1
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	178.2	97.5
Impairment charges	—	24.4
Amortization of debt issuance costs	5.6	—
Stock-based compensation charges	4.6	2.5
(Gain) loss on sales or disposal of property, plant and equipment	(0.2	) 0.6
Deferred income taxes	9.4	(1.9
Equity in earnings of unconsolidated entities	(1.1	) (4.3
Dividends from unconsolidated entities	1.6	0.1
Changes in operating assets and liabilities	(63.9	) (0.5
Net cash provided by operating activities	116.7	74.3
<b>INVESTING ACTIVITIES</b>		
Purchases of property, plant and equipment	(98.5	) (42.5
Proceeds from the sale of property, plant and equipment	8.2	0.5
Equity investment in unconsolidated entities	—	(10.0
Transfers from restricted cash	17.3	—
Net cash used in investing activities	(73.0	) (52.0
<b>FINANCING ACTIVITIES</b>		
Payments of long-term debt	(43.6	) (19.7
Payments of capital lease obligations	(8.8	) (7.1
Borrowings on revolving credit facilities	389.5	217.4
Payments on revolving credit facilities	(360.9	) (175.5
Payment of capitalized debt issuance costs	—	(13.7
Proceeds from issuance of common stock	1.6	0.2
Tax benefit on exercise of stock options	0.8	—
Bankruptcy claim payments on unsecured notes to be issued	(8.0	) —
Payment of cash dividends	(9.4	) (14.0
Payment of tax distributions	(4.2	) (9.1
Net cash used in financing activities	(43.0	) (21.5
Effect of exchange rates on cash and cash equivalents	(4.6	) (0.9
Net decrease in cash and cash equivalents	(3.9	) (0.1
Cash and cash equivalents at beginning of period	20.5	8.9



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Cash and cash equivalents at end of period	\$16.6	\$8.8
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See accompanying Notes to Condensed Consolidated Financial Statements (Unaudited).

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QUAD/GRAPHICS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2011

(In millions, except share and per share data and unless otherwise indicated)

Note 1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements for Quad/Graphics, Inc. and its subsidiaries (the "Company" or "Quad/Graphics") have been prepared by the Company pursuant to the rules and regulations for interim financial information of the United States Securities and Exchange Commission ("SEC"). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") have been omitted pursuant to such SEC rules and regulations. These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated annual financial statements as of and for the year ended December 31, 2010 and notes thereto included in the Company's latest Annual Report on Form 10-K filed with the SEC on March 24, 2011.

The Company's business is seasonal, with the majority of historical net sales and operating income recognized in the second half of the fiscal year. Seasonality is driven by increased magazine advertising page counts and retail inserts and catalogs primarily due to back-to-school and holiday related advertising and promotions. Within any year, seasonality could adversely affect the Company's cash flow and results of operations on a quarterly basis. Further, the comparability of the Company's results of operations between the three and six months ended June 30, 2011 and 2010 was materially impacted by the acquisition of World Color Press Inc. ("World Color Press") on July 2, 2010. The results of operations for World Color Press are included in the Company's consolidated results prospectively from July 2, 2010.

The financial information contained herein reflects all adjustments, in the opinion of management, necessary for a fair presentation of the Company's results of operations for the three and six months ended June 30, 2011 and 2010. All significant intercompany transactions have been eliminated in consolidation. These unaudited condensed consolidated financial statements include estimates and assumptions of management that affect the amounts reported in the condensed consolidated financial statements. Actual results could differ from these estimates.

Note 2. Recent Accounting Pronouncements

In June 2011, the Financial Accounting Standards Board ("FASB") issued new guidance on the presentation of comprehensive income. This new guidance requires the components of net income and other comprehensive income to be either presented in one continuous statement, referred to as the statement of comprehensive income, or in two separate, but consecutive statements. This new guidance eliminates the current option to report other comprehensive income and its components in the statement of shareholders' equity. While the new guidance changes the presentation of comprehensive income, there are no changes to the components that are recognized in net income or other comprehensive income under current accounting guidance. This new guidance is effective for the Company beginning January 1, 2012. As this guidance only amends the presentation of the components of comprehensive income, the adoption will not have an impact on our consolidated financial positions, results of operations or cash flows.

Note 3. Acquisitions

On July 2, 2010, the Company completed the acquisition of World Color Press, a provider of comprehensive print, digital and related services to retailers, catalogers, publishers, branded-goods companies and other businesses in North America and Latin American countries. The World Color Press acquisition was completed for \$93.3 million in cash and \$908.6 million in Company class A common stock. The Company also borrowed \$950.0 million of debt to fund a

portion of the transaction and to refinance the World Color Press debt, including a \$250.0 million advance from a revolving credit facility and \$700.0 million from a term loan. The historical World Color Press United States and Canadian operations are included within the North American Print and Related Services segment, and the historical World Color Press Latin American operations are included within the International segment. In connection with the closing of the acquisition, the Company registered its class A common stock with the SEC under the Securities Exchange Act of 1934, as amended, and on July 6, 2010, Quad/Graphics' class A common stock commenced trading on The New York Stock Exchange, LLC ("NYSE") under the symbol "QUAD".

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FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2011

(In millions, except share and per share data and unless otherwise indicated)

The following unaudited pro forma combined financial information presents the Company's results as though Quad/Graphics and World Color Press had combined at January 1, 2010. The pro forma information has been prepared with the following considerations:

- (1) The unaudited pro forma condensed consolidated financial information has been prepared using the acquisition method of accounting under existing GAAP. Quad/Graphics is the acquirer for accounting purposes.
- (2) World Color Press historical amounts have been converted from Canadian generally accepted accounting principles to GAAP.

- (3) The pro forma combined financial information does not reflect any operating synergy savings that the combined company may achieve as a result of the acquisition, the costs necessary to achieve these operating synergy savings or additional charges necessary as a result of the integration, or the tax effects for the Company's transition to a C corporation.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
	(actual)	(pro forma)	(actual)	(pro forma)
Pro forma net sales	\$1,070.5	\$1,075.3	\$2,172.8	\$2,170.9
Pro forma net loss attributable to common shareholders	(10.3	) (5.3	) (17.6	) (23.1
Pro forma diluted loss per share attributable to common shareholders	(0.22	) (0.11	) (0.37	) (0.49

## Note 4. Restructuring, Impairment and Transaction-Related Charges

The Company recorded restructuring, impairment and transaction-related charges for the three and six months ended June 30, 2011 and 2010 as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
Employee terminations	\$5.1	\$1.2	\$20.2	\$1.2
Impairment charges	—	24.4	—	24.4
Transaction-related charges	1.0	2.7	1.0	8.9
Integration costs	8.9	2.2	16.1	2.2
Other restructuring charges	8.4	0.8	20.9	0.9
Total	\$23.4	\$31.3	\$58.2	\$37.6

The restructuring charges recorded are based on restructuring plans that have been committed to by management and are, in part, based upon management's best estimates of future events. Changes to the estimates may require future restructuring charges and adjustments to the restructuring liabilities. The costs related to restructuring activities have been recorded on the condensed consolidated statements of operations as restructuring, impairment and transaction-related charges. For restructuring, impairment and transaction-related charges by segment, see Note 21.

2011 Restructuring Events

For the three and six months ended June 30, 2011, the Company recorded: (1) \$5.1 million and \$20.2 million, respectively, of employee termination costs related to headcount reductions of 523 and 904, respectively, for plant closures and other workforce reductions announced through the second quarter of 2011, as well from workforce reductions that commenced in 2010, (2) \$1.0 million of transaction costs incurred primarily in connection with the transaction with Transcontinental Inc. ("Transcontinental") (see Note 22), (3) \$8.9 million and \$16.1 million, respectively, of World Color Press integration costs and (4) \$8.4 million and \$20.9 million, respectively, of various other restructuring charges including costs to maintain and exit

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2011

(In millions, except share and per share data and unless otherwise indicated)

closed facilities, as well as lease exit charges. The \$16.1 million of integration costs recognized during the six months ended June 30, 2011 included a \$7.1 million gain on the collection of a previously written off note receivable for the June 2008 sale of World Color Press' European operations.

On January 17, 2011, the Company announced the closure of the St. Laurent plant located in Quebec, Canada resulting in 107 headcount reductions. As part of this initiative, the Company recognized \$0 and \$1.3 million of employee termination costs for the three and six months ended June 30, 2011, respectively. The Company has also recognized \$0.5 million and \$0.7 million of other restructuring charges related to equipment removal costs and facility carrying costs for the three and six months ended June 30, 2011, respectively.

On March 15, 2011, the Company announced the closure of the Mt. Morris, Illinois plant resulting in 490 headcount reductions (441 of which were previously included in a workforce reduction initiative during November 2010 and 49 of which were attributable to the March 2011 plant closure). As part of this initiative, the Company recognized \$0.4 million and \$2.8 million of employee termination costs for the three and six months ended June 30, 2011, respectively. The Company has also recognized \$0.5 million and \$0.9 million of other restructuring charges related to equipment removal costs and facility carrying costs for the three and six months ended June 30, 2011, respectively. The Company expects to incur additional restructuring charges for the Mt. Morris plant closure in the future.

On April 18, 2011, the Company announced the closure of the Buffalo, New York plant resulting in 414 headcount reductions. As part of this initiative, the Company recognized \$0.8 million of employee termination costs for the three and six months ended June 30, 2011. The Company has also recognized \$0.2 million of other restructuring charges related to equipment removal costs for the three and six months ended June 30, 2011. The Company expects to incur additional restructuring charges for the Buffalo plant closure in the future.

In addition to these plant closures, the Company continued to execute various workforce reduction and other restructuring initiatives related to the integration of the operations of World Color Press as well as certain corporate and administrative functions, resulting in 109 and 334 additional headcount reductions during the three and six months ended June 30, 2011, respectively. Severance costs also continue to be incurred related to previously announced plant closures and workforce reductions. Due to these initiatives, the Company has recognized the following charges for the three and six months ended June 30, 2011: (1) \$3.9 million and \$15.3 million of employee termination costs, respectively, (2) \$2.2 million and \$6.1 million of facility carrying costs, respectively, (3) \$2.1 million and \$6.0 million of estimated lease exit charges, respectively, and (4) \$2.9 million and \$7.0 million of other restructuring charges. The Company expects to incur additional restructuring charges related to these and other initiatives in the future.

2010 Restructuring Events

For the three and six months ended June 30, 2010, the Company recorded: (1) \$1.2 million of employee termination costs related to 707 headcount reductions for the closure of the Pila, Poland plant, (2) \$24.4 million of impairment charges on assets related to the closure of the Pila, Poland plant, (3) \$2.7 million and \$8.9 million, respectively, of transaction costs incurred primarily in connection with the World Color Press acquisition, (4) \$2.2 million of integration costs incurred related to the acquisition of World Color Press and (5) \$0.8 million and \$0.9 million, respectively, of lease exit charges.



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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2011

(In millions, except share and per share data and unless otherwise indicated)

## Restructuring Reserve

Activity impacting the Company's restructuring reserve for the six months ended June 30, 2011 was as follows:

	Employee Terminations	Impairment Charges	Transaction-Related Charges	Integration Costs	Other Restructuring Charges	Total	
Balance at December 31, 2010	\$24.7	\$—	\$ —	\$1.1	\$42.6	\$68.4	
Reserve provisions	20.2	—	1.0	16.1	20.9	58.2	
Cash payments	(37.7	) —	—	(13.9	) (26.3	) (77.9	)
Non-cash adjustments	—	—	—	(1.6	) (0.5	) (2.1	)
Balance at June 30, 2011	\$7.2	\$—	\$ 1.0	\$1.7	\$36.7	\$46.6	

The restructuring reserves are classified as current accrued liabilities in the condensed consolidated balance sheets, as the Company expects the restructuring reserves to be paid within the next twelve months.

## Note 5. Goodwill and Other Intangible Assets

Goodwill is tested annually for impairment as of October 31 or more frequently if events or changes in circumstances indicate that it is more likely than not that the fair value of a reporting unit is below its carrying value. Goodwill at June 30, 2011 and December 31, 2010 did not include any accumulated impairment losses. No goodwill impairment was recorded during the six months ended June 30, 2011 or 2010.

Goodwill at June 30, 2011 and December 31, 2010 was as follows:

	North America Print and Related Services	International	Total	
Balance at December 31, 2010	\$796.5	\$18.2	\$814.7	
World Color Press acquisition	(12.6	) —	(12.6	)
Translation adjustment	1.2	0.4	1.6	
Balance at June 30, 2011	\$785.1	\$18.6	\$803.7	

The Company completed the World Color Press purchase price allocation during the second quarter of 2011 resulting in a \$12.6 million reduction in the North America Print and Related Services segment goodwill.



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QUAD/GRAPHICS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2011

(In millions, except share and per share data and unless otherwise indicated)

The components of other intangible assets at June 30, 2011 and December 31, 2010 were as follows:

	June 30, 2011				December 31, 2010			
	Weighted Average Amortization Period (Years)	Gross Carrying Amount	Accumulated Amortization and Foreign Exchange	Net Book Value Impairment	Weighted Average Amortization Period (Years)	Gross Carrying Amount	Accumulated Amortization and Foreign Exchange	Net Book Value Impairment
Finite-lived intangible assets:								
Trademarks, patents, licenses and agreements	5	\$ 10.0	\$ (9.3 )	\$ —	5	\$ 10.0	\$ (9.0 )	\$ —
Customer relationships	6	393.8	(63.6 )	—	6	393.7	(32.3 )	—
Capitalized software	5	4.1	(1.4 )	—	5	4.1	(1.0 )	—
Acquired technology	5	5.3	(3.3 )	—	5	5.3	(2.7 )	—
Total finite-lived intangible assets		413.2	(77.6 )	—		413.1	(45.0 )	—
Other indefinite-lived intangible assets		0.2	—	—		1.2	—	(1.0 )
Total		\$413.4	\$ (77.6 )	\$ —		\$414.3	\$ (45.0 )	\$ (1.0 )

Amortization expense for other intangible assets was \$17.1 million and \$33.8 million for the three and six months ended June 30, 2011, respectively, as compared to \$0.6 million and \$1.2 million for the three and six months ended June 30, 2010, respectively. The following table outlines the estimated amortization expense related to intangible assets as of June 30, 2011:

Remainder of 2011	\$34.3
2012	68.0
2013	67.2
2014	66.8
2015	66.0
2016	33.3
Total	\$335.6

## Note 6. Inventories

The components of the Company's inventories at June 30, 2011 and December 31, 2010 were as follows:

	June 30, 2011	December 31, 2010
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Raw materials and manufacturing supplies	\$155.8	\$164.4
Work in process	77.3	52.7
Finished goods	46.6	30.3
Total	\$279.7	\$247.4

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QUAD/GRAPHICS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2011

(In millions, except share and per share data and unless otherwise indicated)

## Note 7. Property, Plant and Equipment

The components of the Company's property, plant and equipment at June 30, 2011 and December 31, 2010 were as follows:

	June 30, 2011	December 31, 2010
Land	\$135.7	\$136.4
Buildings	914.9	919.1
Machinery and equipment	3,431.2	3,344.0
Other	195.0	182.4
Construction in progress	60.1	45.2
	4,736.9	4,627.1
Less: Accumulated depreciation	(2,450.2	) (2,309.3
Total	\$2,286.7	\$2,317.8

Other consists of computer equipment, vehicles, furniture and fixtures, leasehold improvements and communication related equipment.

The Company recognized depreciation expense of \$70.6 million and \$144.4 million for the three and six months ended June 30, 2011, respectively. Depreciation expense of \$47.6 million and \$96.3 million was recorded for the three and six months ended June 30, 2010, respectively.

## Assets Held for Sale

Certain closed World Color Press facilities are considered held for sale. The net book value of the assets held for sale was \$20.0 million as of June 30, 2011 and December 31, 2010. Assets held for sale are included in prepaid expenses and other current assets in the condensed consolidated balance sheets.

## Note 8. Restricted Cash

The components of the Company's restricted cash at June 30, 2011 and December 31, 2010 were as follows:

	June 30, 2011	December 31, 2010
Defeasance of unsecured notes to be issued (see Note 11)	\$81.2	\$89.2
Other	2.0	11.3
Total restricted cash	\$83.2	\$100.5
Less: short-term restricted cash	(3.1	) (16.0
Long-term restricted cash	\$80.1	\$84.5

## Note 9. Equity Method Investments in Unconsolidated Entities

The Company has a 49% ownership interest in Plural Editora e Gráfica ("Plural"), a commercial printer based in São Paulo, Brazil, and a 50% ownership interest in World Color Chile S.A. ("Chile"), a commercial printer based in Santiago, Chile. The Company's ownership interest in Plural is accounted for using the equity method of accounting for all periods presented. The Company's ownership interest in Chile is accounted for using the equity method of accounting since July 2, 2010, when the Company acquired its ownership interest in Chile as part of the World Color Press acquisition.

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QUAD/GRAPHICS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2011

(In millions, except share and per share data and unless otherwise indicated)

The Company's percentage of Plural's and Chile's net results of operations is recorded in the line item entitled equity in earnings of unconsolidated entities in the Company's condensed consolidated statements of operations, and is included within the International segment.

The combined condensed statements of operations for Plural for the three and six months ended June 30, 2011 and 2010, and for Chile for the three and six months ended June 30, 2011 are presented below:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
Net sales	\$49.1	\$23.2	\$103.1	\$46.2
Operating income	1.6	4.0	3.8	11.1
Net earnings	0.6	2.5	2.0	8.0

Note 10. Commitments and Contingencies

Commitments

The Company had firm commitments of \$38.7 million to purchase press and finishing equipment at June 30, 2011.

Litigation

In the normal course of business, the Company is named as a defendant in various lawsuits in which claims are asserted against the Company. In the opinion of management, the liabilities, if any, which ultimately result from such lawsuits are not expected to have a material adverse effect on the condensed consolidated financial statements of the Company.

Environmental Reserves

The Company is subject to various laws, regulations and government policies relating to health and safety, to the generation, storage, transportation, and disposal of hazardous substances, and to environment protection in general. The Company provides for expenses associated with environmental remediation obligations when such amounts are probable and can be reasonably estimated. Such reserves are adjusted as new information develops or circumstances change. The environmental reserves are not discounted. The Company believes it is in compliance with such laws, regulations and government policies in all material respects. Furthermore, the Company does not anticipate that maintaining compliance with such environmental statutes will have a material adverse effect upon the Company's competitive or consolidated financial position.

Note 11. World Color Press Insolvency Proceedings

The Company continues to manage the bankruptcy claim settlement process for the Quebecor World Inc. ("QWI") bankruptcy proceedings in the United States and Canada (QWI changed its name to "World Color Press Inc." upon emerging from bankruptcy on July 21, 2009). To the extent claims are allowed, the holders of such claims are entitled to receive recovery, with the nature of such recovery dependent upon the type and classification of such claims. In this regard, with respect to certain types of claims, the holders thereof are entitled to receive cash and/or unsecured

notes, while the holders of certain other types of claims are entitled to receive a combination of Quad/Graphics common stock and cash, in accordance with the terms of the World Color Press acquisition agreement.

With respect to claims asserted by the holders thereof as being entitled to a priority cash recovery, the Company has estimated that approximately \$23.3 million and \$26.1 million of such recorded claims have yet to be paid as of June 30, 2011 and December 31, 2010, respectively, and this obligation is classified as amounts owing in satisfaction of bankruptcy claims in the condensed consolidated balance sheets.

With respect to unsecured claims held by creditors of the operating subsidiary debtors of Quebecor World (USA) Inc. (the "Class 3 Claims"), each allowed Class 3 Claim will be entitled to receive an unsecured note in an amount not to exceed 50% of such creditor's allowed Class 3 Claim, provided, however, that the aggregate principal amount of all such unsecured

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notes cannot exceed \$75.0 million. In the event that the total of all allowed Class 3 Claims exceeds \$150.0 million, each creditor holding an allowed Class 3 Claim will receive its pro rata share of \$75.0 million of the unsecured notes issued, together with accrued interest and a 5% prepayment redemption premium thereon (the total of which is \$89.2 million). In connection with the World Color Press acquisition, the Company was required to deposit the maximum potential payout to the Class 3 claim creditors of \$89.2 million with a trustee, and that amount will remain with the trustee until either (1) it is paid to a creditor for an allowed Class 3 claim or (2) upon all Class 3 claims being resolved any excess amount will revert to the Company. In the six months ended June 30, 2011, \$8.0 million was paid to Class 3 claim creditors, therefore \$81.2 million remains at June 30, 2011 and is classified as restricted cash in the condensed consolidated balance sheet (see Note 8). Based on the Company's analysis of the outstanding claims, the Company has recorded a liability, classified as unsecured notes to be issued in the condensed consolidated balance sheet, of \$44.5 million at June 30, 2011.

	Restricted Cash	Unsecured Notes to be Issued
Balance at December 31, 2010	\$89.2	\$52.5
Class 3 Claim Payments	(8.0	) (8.0
Balance at June 30, 2011	\$81.2	\$44.5

While the liabilities recorded for any bankruptcy matters are based on management's current assessment of the amount likely to be paid, it is not possible to identify the final amount of priority cash claims or the amount of Class 3 Claims that will ultimately be allowed by the U.S. Bankruptcy Court. Therefore, amounts owing in satisfaction of bankruptcy claims on the condensed consolidated balance sheet could be materially higher than the amounts estimated, which would require additional cash payments to be made for the amount exceeding the Company's estimate. Amounts payable related to the unsecured notes could reach the maximum aggregate principal amount of \$75.0 million, which would not require an additional cash payment as the maximum potential exposure has already been funded in trust, but would require additional liability and expense to be recorded as the Company's June 30, 2011 estimate of total Class 3 Claim payments is \$44.5 million. In light of the substantial number and amount of claims filed, the claims resolution process will take considerable time to complete.

## Note 12. Debt

Long-term debt consisted of the following as of June 30, 2011 and December 31, 2010:

	June 30, 2011	December 31, 2010
Master note and security agreement	\$645.1	\$672.0
Term loan—\$700.0 million	684.0	686.5
Revolving credit facility—\$530.0 million	85.7	57.0
International term loan	76.0	72.1
International revolving credit facility	16.4	14.9
Domestic term loan	—	11.3
Domestic revolving credit agreement	—	1.0
Other	5.8	6.2
Total debt	\$1,513.0	\$1,521.0
Less: short-term and current portion of long-term debt	(88.1	) (102.6

Long-term debt	\$1,424.9	\$1,418.4
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Based upon the interest rates available to the Company for borrowings with similar terms and maturities, the fair value of the Company's total debt was approximately \$1.5 billion at June 30, 2011.



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As of June 30, 2011, the Company's various lending arrangements included certain financial covenants (all financial terms, numbers and ratios are as defined in the Company's debt agreements). Among these covenants, the Company was required to maintain the following (for each covenant, the most restrictive measurement has been included below):

On a rolling twelve-month basis, the total leverage ratio, defined as total consolidated debt to consolidated EBITDA, shall not exceed 3.75 to 1.00 (for the twelve months ended June 30, 2011, the Company's leverage ratio was 2.39 to 1.00).

On a rolling twelve-month basis, the minimum interest coverage ratio, defined as consolidated EBITDA to consolidated cash interest expense, shall not be less than 3.00 to 1.00 (for the twelve months ended June 30, 2011, the Company's interest coverage ratio was 6.05 to 1.00).

On a rolling twelve-month basis, the fixed charge coverage ratio, defined as consolidated EBITDA and rent expense to interest and rent expense, shall not be less than 1.50 to 1.00 (for the twelve months ended June 30, 2011, the Company's fixed charge coverage ratio was 3.01 to 1.00).

Consolidated net worth of at least \$745.8 million plus 40% of positive consolidated net income cumulatively for each year (as of June 30, 2011, the Company's consolidated net worth under the most restrictive covenant per the various lending arrangements was \$1.41 billion).

The covenants also included certain limitations on acquisitions, indebtedness, liens, dividends and repurchases of capital stock. As of and for the rolling twelve-month period ended June 30, 2011, the Company was in compliance with all debt covenants.

Note 13. Income Taxes

The Company records income tax expense on an interim basis. The estimated annual effective income tax rate is adjusted quarterly and items discrete to a specific quarter are reflected in tax expense for that interim period. The estimated annual effective income tax rate reflects the change in a valuation allowance due to expected current year earnings or loss. A valuation allowance is established when necessary to reduce deferred tax assets to the amount more likely than not to be realized. There was no material change in unrecognized tax benefits in the six month period ending June 30, 2011, and the Company does not anticipate a material change in total unrecognized tax benefits within the next 12 months.

Note 14. Financial Instruments and Fair Value Measurements

Certain assets and liabilities are required to be recorded at fair value on a recurring basis, while other assets and liabilities are recorded at fair value on a nonrecurring basis, generally as a result of acquisitions or impairment charges. Fair value is determined based on the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants. The Company records the fair value of its forward contracts, pension plans and other postretirement plans on a recurring basis. Assets measured at fair value on a nonrecurring basis include property, plant and equipment, assets held for sale, goodwill and other intangible assets. The fair value of cash and cash equivalents, receivables, restricted cash, accounts payable, accrued liabilities and amounts owing in satisfaction of

bankruptcy claims approximate their carrying values as of June 30, 2011 and December 31, 2010. See Note 12 for further discussion on the fair value of the Company's debt.

The Company has operations in countries that have transactions outside their functional currencies and periodically enters into foreign exchange contracts. These contracts are used to hedge the net exposures of changes in foreign currency exchange rates and are designated as either cash flow hedges or fair value hedges. Gains or losses on net foreign currency hedges are intended to offset losses or gains on the underlying net exposures in an effort to reduce the earnings volatility resulting from fluctuating foreign currency exchange rates.

The Company also periodically enters into foreign exchange contracts against firm equipment purchase contracts denominated in foreign currencies and natural gas forward purchase contracts to hedge against increases in these costs. Estimated market values were determined based upon quoted market prices.

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There were no open foreign currency exchange contracts at June 30, 2011 or December 31, 2010. During the three and six months ended June 30, 2011 and 2010, the Company's commodity contracts qualified for the exception related to normal purchases and sales as the Company takes delivery in the normal course of business. For the three and six months ended June 30, 2011 and 2010, hedge ineffectiveness was not material.

## Note 15. Other Long-Term Liabilities

Other long-term liabilities consisted of the following as of June 30, 2011 and December 31, 2010:

	June 30, 2011	December 31, 2010
Single employer pension and postretirement obligations	\$294.6	\$330.7
Multiemployer pension plans—withdrawal liability	100.1	100.1
Tax-related liabilities	34.8	34.8
Employee-related liabilities	49.5	53.2
Other	82.2	85.0
Total	\$561.2	\$603.8

## Note 16. Pension and Other Postretirement Benefits

The Company assumed multiple defined benefit pension and postretirement benefit plans as part of the World Color Press acquisition. Prior to the acquisition, the Company did not have defined benefit plans and the resulting pension and postretirement obligations. The components of the estimated pension expense and postretirement benefits income for the three and six months ended June 30, 2011 were as follows:

	Three Months Ended June 30, 2011	Six Months Ended June 30, 2011
Pension expense		
Service cost	\$1.4	\$2.8
Interest cost	12.2	24.4
Expected return on assets	(11.5)	(22.9)
Net pension expense	\$2.1	\$4.3
Postretirement benefits income		
Service cost	\$0.2	\$0.4
Interest cost	0.5	1.0
Amortization of deferred gains, net	(0.8)	(1.6)
Net postretirement benefits income	\$(0.1)	\$(0.2)

## Note 17. Loss Per Share Attributable to Quad/Graphics Common Shareholders

Basic loss per share attributable to Quad/Graphics common shareholders is computed by dividing net loss attributable