

TREX CO INC  
Form 10-K/A  
August 10, 2009  
Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-K/A**

(Amendment No. 1)

(Mark One)

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

For the fiscal year ended December 31, 2008

**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: 001-14649

**Trex Company, Inc.**

(Exact name of registrant as specified in its charter)

Edgar Filing: TREX CO INC - Form 10-K/A

<b>Delaware</b> (State or other jurisdiction of incorporation or organization)	<b>54-1910453</b> (I.R.S. Employer Identification No.)
<b>160 Exeter Drive, Winchester, Virginia</b> (Address of principal executive offices)	<b>22603-8605</b> (Zip Code)

(540) 542-6300

Registrant's telephone number, including area code:

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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

<b>Title of each class:</b> Common Stock	<b>Name of each exchange on which registered:</b> New York Stock Exchange
---	--

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

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes  No

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

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

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

Large accelerated filer  Accelerated filer  Non-accelerated filer

## Edgar Filing: TREX CO INC - Form 10-K/A

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

The aggregate market value of the registrant's common equity held by non-affiliates of the registrant at June 30, 2008, which was the last business day of the registrant's most recently completed second fiscal quarter, was approximately \$170.0 million based on the closing price of the common stock as reported on the New York Stock Exchange on such date and assuming, for purposes of this computation only, that the registrant's directors, executive officers and beneficial owners of 10% or more of the registrant's common stock are affiliates.

The number of shares of the registrant's common stock outstanding on August 3, 2009 was 15,376,744.

**Table of Contents**

**EXPLANATORY STATEMENT**

**Why we are filing this Amendment to our Form 10-K**

During the preparation of the Quarterly Report on Form 10-Q for the three-month period ended June 30, 2009, the Company's management team discovered that, beginning in 2007, the Company incorrectly calculated the valuation allowance related to its deferred tax assets.

In determining the valuation allowance, the Company considered as a source of future taxable income existing taxable temporary differences related to indefinite-lived intangible assets. Because the timing of reversal of these deferred tax liabilities is unknown, they are not a reliable source of recovery of deferred tax assets. The result of this error is that the valuation allowance for deferred tax assets was understated at December 31, 2007 and each subsequent financial reporting date through December 31, 2008.

As a result of the foregoing, the Company understated reported net loss in 2007 by approximately \$1.6 million and overstated net income in 2008 by approximately \$0.3 million. The combined effect of the misstatements in years 2007 and 2008 resulted in a cumulative overstatement of net income totaling approximately \$1.9 million.

This amendment also contains reclassifications of certain amounts which either individually or in the aggregate are not considered material. These reclassifications result in an increase to Cost of sales and a decrease to Selling, general and administrative expenses for expenses related to certain amounts that were previously reported as Selling, general and administrative expenses.

The Company is filing this amendment on Form 10-K/A to amend and restate the Company's consolidated balance sheets as of December 31, 2007 and 2008 and its restated consolidated statements of operations, stockholders' equity and cash flows for the fiscal years ended December 31, 2007 and 2008. The amendment also restates the quarterly financial information previously included in Note 16 to the consolidated financial statements with respect to the fiscal quarters ended March 31, 2008, June 30, 2007 and 2008, September 30, 2007 and 2008 and December 31, 2007 and 2008. The Company does not intend to amend its Quarterly Reports on Form 10-Q for these fiscal quarters.

In May 2008, the Financial Accounting Standards Board issued Staff Position No. APB 14-1, *Accounting for Convertible Debt Instruments that May be Settled in Cash Upon Conversion* ( FSP APB 14-1 ). FSP APB 14-1 requires the proceeds from the issuance of convertible debt instruments that may be settled in cash upon conversion to be allocated between a liability component and an equity component. The resulting debt discount is amortized over the period the convertible debt is expected to be outstanding as non-cash interest expense. The Company adopted FSP APB 14-1, which requires retrospective presentation, effective January 1, 2009. This amendment also adjusts the historic financial statements to reflect the retrospective adoption of the standard. The application of FSP APB 14 -1 resulted in a decrease to 2007 reported net loss of \$12.1 million and a decrease to 2008 reported net income of \$5.7 million.

The restatement adjustments and the retrospective adoption of FSP APB 14-1 had the cumulative effect of increasing the Company's reported net income for the fiscal years ended December 31, 2007 through 2008 by \$4.5 million.

**Amended Items of Form 10-K**

We are amending the following items of our 2008 10-K:

Part II	Item 6	Selected Financial Data
Part II	Item 7	Management's Discussion and Analysis of Financial Condition and Results of Operations
Part II	Item 8	Financial Statements and Supplementary Data
Part II	Item 9A	Controls and Procedures
Part IV	Item 15	Exhibits and Financial Statement Schedules

**All information not affected by the restatement is unchanged**

Except as set forth above, we have not changed any information included in the Original Filing that is not affected by the restatement or the retrospective adoption of FSP APB 14-1. Accordingly, the information included in the Original Filing and included in this amendment that is not affected by the restatement describes conditions as they existed and were presented in the Original Filing at the time we filed that report with the

## Edgar Filing: TREX CO INC - Form 10-K/A

Securities and Exchange Commission on March 12, 2009. Except as set forth above or other immaterial changes, we have not taken into account any other events occurring after we filed the Original Filing that might have affected those disclosures, nor have we modified or updated those disclosures, including the exhibits to the Original Filing, to reflect any other subsequent events. Accordingly, in conjunction with reading this amendment to the Original Filing, you should also read all other filings we have made with the Securities and Exchange Commission since March 12, 2009.

**Table of Contents**

**TABLE OF CONTENTS**

	<b>Page</b>
<b><u>PART II</u></b>	
Item 6. <u>Selected Financial Data</u>	1
Item 7. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	3
Item 8. <u>Financial Statements and Supplementary Data</u>	11
Item 9A. <u>Controls and Procedures</u>	12
<b><u>PART IV</u></b>	
Item 15. <u>Exhibits and Financial Statement Schedules</u>	15
<u>Index to Consolidated Financial Statements</u>	21

**Table of Contents****PART II****Item 6. Selected Financial Data**

The selected financial data for the fiscal years ended December 31, 2007, and 2008 set forth in this Item 6 have been restated to reflect adjustments to our consolidated financial statements and other financial information contained in our Annual Report on Form 10-K for the fiscal year ended December 31, 2008, originally filed with the Securities and Exchange Commission ( SEC ) on March 12, 2009 (the 2008 10-K ). The following selected financial data should be read in conjunction with our restated consolidated financial statements and the related notes to consolidated financial statements.

	Year Ended December 31,				
	2004	2005	2006	2007 As Restated (2)	2008 As Restated (2)
<b>Statement of Operations Data:</b>					
Net sales	\$ 253,628	\$ 294,133	\$ 336,956	\$ 328,952	\$ 329,194
Cost of sales	150,793	213,897	257,671	289,529	240,170
Gross profit	102,835	80,236	79,285	39,423	89,024
Selling, general and administrative expenses	56,351	77,378	73,223	119,439	66,958
Income (loss) from operations	46,484	2,858	6,062	(80,016)	22,066
Interest expense, net	3,064	2,626	3,011	11,503	15,282
Income (loss) before income taxes	43,420	232	3,051	(91,519)	6,784
Provision (benefit) for income taxes	15,933	(2,019)	708	(26,105)	(750)
Net income (loss)	\$ 27,487	\$ 2,251	\$ 2,343	\$ (65,414)	\$ 7,534
Basic earnings (loss) per share	\$ 1.88	\$ 0.15	\$ 0.16	\$ (4.39)	\$ 0.50
Basic weighted average shares outstanding	14,636,959	14,769,799	14,829,832	14,884,174	14,956,927
Diluted earnings (loss) per share	\$ 1.85	\$ 0.15	\$ 0.16	\$ (4.39)	\$ 0.50
Diluted weighted average shares outstanding	14,834,718	14,879,661	14,892,966	14,884,174	15,113,083
<b>Cash Flow Data:</b>					
Cash provided by (used in) operating activities	\$ 45,265	\$ 11,234	\$ (4,038)	\$ (1,163)	\$ 33,042
Cash used in investing activities	(56,319)	(29,374)	(27,743)	(24,035)	(8,594)
Cash provided by (used in) financing activities	26,859	(4,432)	31,058	24,592	(1,325)
<b>Other Data (unaudited):</b>					
EBITDA (1)	\$ 60,197	\$ 18,997	\$ 26,324	\$ (57,525)	\$ 47,942
<b>Balance Sheet Data:</b>					
Cash and cash equivalents and restricted cash	\$ 44,926	\$ 1,395	\$ 672	\$ 66	\$ 23,189
Working capital	78,910	40,061	29,559	48,385	65,085
Total assets	286,772	285,714	352,317	320,529	307,084
Total debt	78,497	73,606	104,637	98,002	103,563
Total stockholder s equity	159,937	164,708	169,415	128,385	137,828

## Edgar Filing: TREX CO INC - Form 10-K/A

- (1) EBITDA represents net income before interest, income taxes, depreciation and amortization. EBITDA is not a measurement of financial performance under accounting principles generally accepted in the United States, or GAAP. The company has included data with respect to EBITDA because management evaluates and projects the performance of the company's business using several measures, including EBITDA. Management considers EBITDA to be an important supplemental indicator of the company's operating performance, particularly as compared to the operating performance of the company's competitors, because this measure eliminates many differences among companies in capitalization and tax structures, capital investment cycles and ages of related assets, as well as some recurring non-cash and non-operating charges to net income or loss. For these reasons, management believes that EBITDA provides important supplemental information to investors regarding the operating performance of the company and facilitates comparisons by investors between the operating performance of the company and the operating performance of its competitors. Management believes that consideration of EBITDA should be supplemental, because EBITDA has limitations as an analytical financial measure. These limitations include the following:

EBITDA does not reflect the company's cash expenditures, or future requirements for capital expenditures, or contractual commitments;

EBITDA does not reflect the interest expense, or the cash requirements necessary to service interest or principal payments, on the company's indebtedness;



**Table of Contents**

although depreciation and amortization are non-cash charges, the assets being depreciated and amortized will often have to be replaced in the future, and EBITDA does not reflect any cash requirements for such replacements;

EBITDA does not reflect the effect of earnings or charges resulting from matters the company considers not to be indicative of its ongoing operations; and

not all of the companies in the company's industry may calculate EBITDA in the same manner in which the company calculates EBITDA, which limits its usefulness as a comparative measure.

The company compensates for these limitations by relying primarily on its GAAP results to evaluate its operating performance and by considering independently the economic effects of the foregoing items that are not reflected in EBITDA. As a result of these limitations, EBITDA should not be considered as an alternative to net income, as calculated in accordance with GAAP, as a measure of operating performance, nor should it be considered as an alternative to cash flows as a measure of liquidity. The following table sets forth, for the years indicated, a reconciliation of EBITDA and net income. The applicable amounts shown in the table have been restated as described in Note 2 to the company's consolidated financial statements appearing elsewhere in this report.

	Year Ended December 31,				
	2004	2005	2006	2007 As Restated (2)	2008 As Restated (2)
	(In thousands)				
Net income (loss)	\$ 27,487	\$ 2,251	\$ 2,343	\$ (65,414)	\$ 7,534
Plus interest expense, net	3,064	2,626	3,011	11,503	15,282
Plus income taxes provision (benefit)	15,933	(2,019)	708	(26,105)	(750)
Plus depreciation and amortization	13,713	16,139	20,262	22,491	25,876
<b>EBITDA</b>	<b>\$ 60,197</b>	<b>\$ 18,997</b>	<b>\$ 26,324</b>	<b>\$ (57,525)</b>	<b>\$ 47,942</b>

(2) See Note 2 to the Company's consolidated financial statements appearing elsewhere in this report.

---

## **Table of Contents**

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

*This Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. We intend our forward-looking statements to be covered by the safe harbor provisions for forward-looking statements in these sections. All statements regarding our expected financial position and operating results, our business strategy, our financing plans, forecasted demographic and economic trends relating to our industry and similar matters are forward-looking statements. These statements can sometimes be identified by our use of forward-looking words such as may, will, anticipate, estimate, expect or intend. We cannot promise you that our expectations in such forward-looking statements will turn out to be correct. Our actual results could be materially different from our expectations because of various factors, including the factors discussed under Item 1A. Risk Factors in this report.*

#### **Restatement**

On July 26, 2009, the Audit Committee of the Company's Board of Directors concluded, based upon the recommendation of the Company's management, that the Company should restate its financial results, including quarterly results, to correct an error in its Annual Reports on Form 10-K for fiscal years ended December 31, 2007 and 2008. Accordingly, we have restated our financial statements to correct this error, as described more fully in Note 2 of the consolidated financial statements in this Form 10-K/A. In addition, the restatements reflect the effects of the adoption of FASB Staff Position APB 14-1, *Accounting for Convertible Debt Instruments that May Be Settled in Cash upon Conversion* ( FSP APB 14-1 ), which was effective January 1, 2009 and required retroactive application. Together, the adjustments related to the error and the adoption of FSP APB 14-1 have the cumulative effect of decreasing the Company's reported net loss for 2007 by \$10.5 million and decreasing the Company's reported net income for 2008 \$6.0 million. This Management's Discussion and Analysis of Financial Condition and Results of Operations has been modified and updated principally to reflect the effect of these restatements.

The amendment also includes restated quarterly financial information in Note 16 to the consolidated financial statements with respect to the fiscal quarters ended March 31, 2007 and 2008, June 30, 2007 and 2008, September 30, 2007 and 2008 and December 31, 2007 and 2008.

#### **Overview**

*General.* Trex Company, Inc., (the Company), is the largest U.S. manufacturer of wood-alternative decking, railing, fencing and trim products, which are marketed under the brand name Trex®. The Company offers a comprehensive set of aesthetically durable, low maintenance product offerings and believes that the range and variety of our product offerings allow consumers to design personal outdoor living space using Trex brand products.

The Company has six decking product lines: Trex Contours®, Trex Origins®, Trex Accents®, Trex Accents Fire Defense®, Trex Brasilia® and Trex Escapes® two railing product lines: Trex Designer Series Railing® and Trex Artisan Series Railing® a fencing product, Trex Seclusions® and a cellular PVC outdoor trim product, TrexTrim . In addition, the Company offers Trex Hideaway®, which is a hidden fastening system for specially grooved boards.

The Company's products are primarily manufactured from waste wood fiber and reclaimed polyethylene, which is sometimes referred to as PE material in this report. The Company's primary manufacturing process involves mixing wood particles with plastic, heating and finally extruding, or forcing, the highly viscous and abrasive material through a profile die. The Company has many proprietary and skill-based advantages in this process. The Company believes that the use of recycled raw materials gives it a low-cost competitive advantage in the composite decking industry. The Company outsources the production of certain products to third-party manufacturers.

Management considers growth in net sales, gross margin, selling, general and administrative expenses, and net income as key indicators of our operating performance. Growth in net sales reflects consumer acceptance of the Company's decking, railing, fencing and trim products, the demand for Trex over competing products, the success of our branding strategy, the effectiveness of our distributors, and the strength of our dealer network and contractor franchise. Management emphasizes gross margin as a key measure of performance because it reflects the Company's ability to price its products accurately and to manage effectively its manufacturing unit costs. Managing selling, general and administrative expenses is important to support profitable growth. The Company's investment in research and development activities, which is included in selling, general and administrative expenses, enables it to enhance manufacturing operations, develop new products and analyze new technologies. Management considers net income to be a measure of the Company's overall financial performance.

The Company reported net income of \$7.5 million on \$329.2 million of net sales for the year ended December 31, 2008 compared to a net loss of \$65.4 million on \$329.0 million of net sales for the year ended December 31, 2007. Diluted earnings (loss) per share rose in 2008 to \$0.50 from (\$4.39) in 2007.

## Edgar Filing: TREX CO INC - Form 10-K/A

Management took several actions in 2007 and 2008 to streamline the Company's operations, reduce costs and improve liquidity. In September 2007, the Company's board of directors approved a plan to reduce operating costs and improve the efficiency of the Company's manufacturing operations. Under the plan, the Company suspended operations at its manufacturing facility in Olive Branch, Mississippi, for an indeterminate period and consolidated all of its manufacturing operations into its other two plants, located in Winchester, Virginia and Fernley, Nevada. Further improvements to the Company's manufacturing operations and cost reductions initiatives enacted during 2008 resulted in positive effects on gross margins and reduced selling, general and administrative expenses.

## **Table of Contents**

The Company continues to focus on effective management of raw material costs and broadening the range of material it can use to produce a consistent, high-quality product. During recent years the Company applied a significant portion of its capital investments to the purchase and installation of PE material processing equipment. These investments have enabled the Company to enhance the management of its cost of PE material and to improve its manufacturing performance.

Management is also committed to reducing inventory levels and improving cash flow from operations. Inventories declined by \$18.9 million and \$23.2 million in 2007 and 2008, respectively, and cash flow from operations improved significantly in 2008 compared to 2007.

*Nevada Facility Product Replacement and Warranty Reserve.* The Company warrants that its products will be free from material defects in workmanship and material and will not check, split, splinter, rot or suffer structural damage from termites or fungal decay. If there is such a defect in any of its products, the Company has an obligation either to replace the defective product or refund the purchase price. The Company maintains a warranty reserve to provide for estimated future expenses as a result of product defects that result in claims.

As previously reported, during the three months ended September 30, 2007, the Company experienced a significant increase in the number of customer claims related to Trex products produced at the Nevada manufacturing facility beginning in 2003 that exhibited surface defects. The Company believes that changes made to its manufacturing process and quality control procedures have prevented any additional product with this type of defect from reaching the market after mid-2006.

In 2007, the Company increased its warranty reserve by recording a charge to earnings of \$45.2 million in the three months ended September 30, 2007 and \$1.5 million in the three months ended December 31, 2007. During 2008, the Company continued to fund payments for product defect claims from the established reserve.

The costs related to the replacement of product material are reflected in net sales as product replacement costs, thereby reducing net sales, while the costs related to installation labor are reflected in selling, general and administrative expenses as consumer relations expenses. These costs had a material adverse effect on 2007 profitability but did not have a material adverse effect on 2008 profitability.

*Net Sales.* Net sales consist of sales and freight, net of returns, discounts, sales incentives and changes in the warranty reserve. The level of net sales is principally affected by sales volume and the prices paid for Trex. The Company's branding and product differentiation strategy enables it to command premium prices over wood and to maintain price stability for Trex. To ensure adequate availability of product to meet anticipated seasonal consumer demand, the Company has historically provided its distributors and dealers incentives to build inventory levels before the start of the prime deck-building season. These incentives include prompt payment discounts or extended payment terms. In addition, the Company from time to time may offer price discounts on specified products and other incentives based on increases in distributor purchases as part of specific promotional programs. There is no product return right granted to the Company's distributors except those granted pursuant to the warranty provisions of the Company's agreement with its distributors.

The Company was advised by one of its distributors, which accounted for approximately 11% of the Company's gross sales in the year ended December 31, 2008, that it was terminating its agreement with the Company effective September 17, 2008. Subsequently, the Company secured new and existing distributors to distribute its products in the affected territories previously serviced by the terminated distributor. The transition of the affected territories to the new distributors did not have a material adverse effect on the Company's annual net sales or operating results.

*Gross Profit.* Gross profit represents the difference between net sales and cost of sales. Cost of sales consists of raw materials costs, direct labor costs, manufacturing costs and freight. Raw materials costs generally include the costs to purchase and transport waste wood fiber, PE material and pigmentation for coloring Trex products. Direct labor costs include wages and benefits of personnel engaged in the manufacturing process. Manufacturing costs consist of costs of depreciation, utilities, maintenance supplies and repairs, indirect labor (including wages and benefits), and warehouse and equipment rental activities.

*Selling, General and Administrative Expenses.* The largest components of selling, general and administrative expenses are branding and other sales and marketing costs. Sales and marketing costs consist primarily of salaries, commissions and benefits paid to sales and marketing personnel, consumer relations, advertising expenses and other promotional costs. General and administrative expenses include salaries and benefits of personnel engaged in research and development, procurement, accounting and other business functions, office occupancy costs attributable to these functions, and professional fees. As a percentage of net sales, selling, general and administrative expenses have varied from quarter to quarter due, in part, to the seasonality of the Company's business. During 2007, the Company experienced an increase in consumer relations expenses resulting from an increase in the warranty reserve described above.



---

## **Table of Contents**

### **Critical Accounting Policies, Estimates and Risks and Uncertainties**

Our significant accounting policies are described in note 3 to our consolidated financial statements appearing elsewhere in this report. Critical accounting policies include the areas where we have made what we consider to be particularly difficult, subjective or complex judgments in making estimates, and where these estimates can significantly affect our financial results under different assumptions and conditions. We prepare our financial statements in conformity with accounting principles generally accepted in the United States. As a result, we are required to make estimates, judgments and assumptions that we believe are reasonable based upon the information available. These estimates, judgments and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the periods presented. Actual results could be different from these estimates.

*Inventories.* The Company accounts for its inventories at the lower of cost (last-in, first-out, or LIFO) or market value. The Company believes that its current inventory of finished goods will be saleable in the ordinary course of business and, accordingly, has not established significant reserves for estimated slow moving products or obsolescence. The Company has written down to its estimated market value the estimated portion of PE material and other raw materials that are not consumable. At December 31, 2008, the excess of the replacement cost of inventory over the LIFO value of inventory was approximately \$30.3 million. The Company cannot estimate at this time the effect of future reductions, if any, in inventory levels on its future operating results.

*Long-Lived Assets.* In accordance with the Statement of Financial Accounting Standards, or SFAS, No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, the Company reviews its long-lived assets, including property, plant and equipment, whenever events or changes in circumstances indicate that the carrying amount of the assets may not be fully recoverable. To determine the recoverability of its long-lived assets, the Company evaluates the probability that future estimated undiscounted net cash flows will be less than the carrying amount of the long-lived assets. If the estimated cash flows are less than the carrying amount of the long-lived assets, the assets are written down to their fair value. The Company's estimates of anticipated cash flows and the remaining estimated useful lives of long-lived assets could be reduced in the future. As a result, the carrying amount of long-lived assets could be reduced in the future.

Property, plant and equipment are depreciated on a straight-line basis over the estimated useful lives of the assets. The depreciable lives of these assets range from three to 40 years. Estimates of the useful lives are based, in part, upon historical performance of similar assets. The Company periodically reviews the remaining estimated useful lives of property, plant and equipment to determine if any revisions to the estimates are necessary. Changes to the estimate of the useful lives of property, plant and equipment could have a material effect on the Company's financial position or results of operations.

Of the Company's \$176.3 million of net property, plant and equipment at December 31, 2008, approximately \$42.7 million is located at the Olive Branch, Mississippi manufacturing facility. The Company suspended manufacturing operations at the Olive Branch facility in the third quarter of 2007 for an indeterminate period. Management believes that as general macroeconomic conditions improve and demand for the Company's products continues to increase the Company will need to resume operations at the Olive Branch facility. Changes in the plans regarding the future operation of the facility or the expected cash flows generated by the facility in the future may result in material impairment charges and reduced earnings.

*Product Warranty.* The Company warrants that its products will be free from material defects in workmanship and material and will not check, split, splinter, rot or suffer structural damage from termites or fungal decay. If there is such a defect in any of its products, the Company has an obligation either to replace the defective product or refund the purchase price. The Company establishes warranty reserves to provide for estimated future expenses as a result of product defects that result in claims. Reserve estimates are based on management's judgment, considering such factors as historical experience and other available information. Management reviews and adjusts these estimates, if necessary, on a quarterly basis based on the differences between actual experience and historical estimates.

During the three months ended September 30, 2007, the Company experienced a significant increase in the number of customer claims related to Trex product that exhibited surface defects and which the Company has determined was produced at the Nevada manufacturing facility beginning in 2003. Following a detailed analysis of the additional claims data, production samples, operating data and the incubation period after deck installation and other factors, the Company believes that only a small percentage of the product manufactured from 2003 to mid-2006 at the Nevada plant was affected, and that products manufactured at its other facilities are not affected. The Company believes that changes made to its manufacturing process and quality control procedures have prevented any additional product with this type of defect from reaching the market after mid-2006. Based on the available data, the Company revised its estimate of expected future product replacement and consumer relations expenses related to the defect and increased its warranty reserve by recording a charge to earnings of \$45.2 million in the three months ended September 30, 2007. In addition, during the three months ended December 31, 2007, the Company elected to alter its handling of future customer claims. As a result of the effect of this change on the estimated cost to settle claims, the Company recorded an additional \$1.5 million increase to its warranty reserve. During 2008, the Company continued to fund payments for product defect claims from the established reserve. Although the Company adjusts the warranty reserve accordingly by recording the best estimate of the expected costs, due to the inherent

## Edgar Filing: TREX CO INC - Form 10-K/A

subjectivity of estimating future claims, it is possible that the ultimate settlement of the claims may exceed the amount recorded and may result in future charges against income. For additional information about product warranties, see notes 3 and 14 to the consolidated financial statements appearing elsewhere in this report.

---

**Table of Contents**

*Contract Termination Costs.* In anticipation of relocating the Company's corporate headquarters, the Company entered into a lease agreement in 2005. The Company reconsidered and decided not to move its headquarters. The lease, which began on January 1, 2006 and extends through June 30, 2019, currently obligates the Company to lease 55,047 square feet and increases to 80,071 square feet in 2012. As of January 10, 2008, the Company had executed subleases for the entire 55,047 square feet it currently leases. The terms of the existing subleases extend through years 2012 to 2015. The Company estimates that the present value of the estimated future sublease rental receipts, net of transaction costs, will be less than the Company's remaining minimum lease payment obligations under its lease for the office space. Accordingly, the Company accounts for the costs associated with the lease as contract termination costs in accordance with SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities*.

To estimate future sublease receipts for the periods beyond the term of the existing subleases and for the additional space the Company is obligated to lease, the Company has assumed that the existing subleases will be renewed or new subleases will be executed at rates consistent with rental rates in the current subleases. However, management cannot be certain that the timing of future subleases or the rental rates contained in future subleases will not differ from current estimates. Factors such as the delivery of a significant amount of new office space or poor economic conditions could have a negative effect on vacancy rates and rental rates in the area. The inability to sublet the office space in the future or unfavorable changes to key management assumptions used in the estimate of the future sublease receipts may result in additional charges to selling, general and administrative expenses in future periods.

*Contingencies and Other Liabilities.* The Company is subject, from time to time, to various lawsuits and other claims related to patent infringement, product liability and other matters. The Company is required to assess the likelihood of any adverse judgments or outcomes to these matters as well as potential ranges of probable losses. The Company makes a determination of the amount of reserves required, if any, for these contingencies after an analysis of each lawsuit and claim. The required reserves may change in the future as a result of new developments in any such matter or changes in approach, such as a change in settlement strategy in dealing with a particular matter. In the opinion of management, adequate provision has been made for any probable losses as of December 31, 2008.

*Revenue Recognition.* The Company recognizes revenue when title is transferred to customers, which is generally upon shipment of the product to the customer. The Company does not grant contractual product return rights to its customers other than pursuant to its product warranty. The Company does not expect future product returns to be material and, consequently, does not maintain an allowance for product returns.

Pursuant to Emerging Issues Task Force (EITF) Issue 00-10, *Accounting for Shipping and Handling Fees and Costs*, the Company records all shipping and handling fees in sales and records all of the related costs in cost of sales. The Company offers several sales incentive programs to dealers and distributors, including rebates, pricing discounts, extended terms and cooperative advertising, many of which result in cash consideration made to dealers and distributors. The Company accounts for consideration made pursuant to these programs in accordance with EITF Issue 01-09, *Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)*. With the exception of cooperative advertising, the Company classifies sales incentives as a reduction in revenue in Net sales. Sales incentives are recorded in the period in which they are earned by customers. The Company's cooperative advertising program meets the requirements of EITF Issue 01-09, paragraph 9 for exclusion from net sales and the costs are recorded as expenses in Selling, general and administrative expenses in the accompanying consolidated statements of operations. Cooperative advertising costs are accrued as incurred.

*Valuation of Deferred Tax Assets.* The Company provides for valuation allowances against its deferred tax assets in accordance with the requirements of SFAS No. 109, *Accounting for Income Taxes*. At December 31, 2008, the Company had a valuation allowance of \$5.6 million primarily attributable to the uncertainty related to the realizability of the Company's excess deferred tax assets. The Company has considered all available evidence, both positive and negative, in determining the need for a valuation allowance. Based upon this analysis, including a consideration of the Company's cumulative loss history in the three-year period ended December 31, 2008, management determined that it is not more likely than not that its excess deferred tax assets will be realized.

*Stock-Based Compensation.* Under the provisions of FAS 123(R), we calculate the grant date fair value of share-based awards using the Black-Scholes valuation model for grants subsequent to the adoption of FAS 123(R). Determining the fair value of share-based awards is judgmental in nature and involves the use of significant estimates and assumptions, including the term of the share-based awards, risk-free interest rates over the vesting period, expected dividend rates, the price volatility of our shares and forfeiture rates of the awards. Prior to adopting FAS 123(R), we recognized forfeitures only as they occurred. We base our fair value estimates on assumptions we believe to be reasonable but that are inherently uncertain. Actual future results may differ from those estimates.

As mandated by FAS 123(R), beginning in the first quarter of 2006, we also report the benefits of tax deductions in excess of recognized compensation expense as a financing cash inflow in the consolidated statements of cash flows. Prior to the adoption of FAS 123(R), we reported these tax benefits as an operating cash flow.





**Table of Contents****Results of Operations**

The following table shows, for the last three years, selected statement of operations data as a percentage of net sales:

	Year Ended December 31,		
	2006	2007 As Restated (1)	2008 As Restated (1)
Net sales	100.0%	100.0%	100.0%
Cost of sales	76.5	88.0	73.0
Gross profit	23.5	12.0	27.0
Selling, general and administrative expenses	21.7	36.3	20.3
Income (loss) from operations	1.8	(24.3)	6.7
Interest expense, net	0.9	3.5	4.6
Income (loss) before taxes and extraordinary item	0.9	(27.8)	2.1
Provision (benefit) for income taxes	0.2	(7.9)	(0.2)
Net income (loss)	0.7%	(19.9)%	2.3%

(1) See Note 2 to the company's consolidated financial statements appearing elsewhere in this report.

**2008 Compared to 2007**

*Net Sales.* Net sales in 2008 increased 0.1% to \$329.2 million from \$329.0 million in 2007. Net sales in 2007 were adversely affected by charges of \$37.8 million. The Company recorded \$25.5 million of charges against net sales for product replacement expenses, driven by the increase in the warranty liability recorded in 2007 and \$12.3 million of charges against net sales for distributor credits primarily related to the voluntarily return of product. Payments for the product replacement were recognized against the existing warranty liability during 2008 and, therefore, did not affect net sales. Before giving effect to these charges, net sales in 2008 were \$329.2 million compared to \$366.8 million in 2007 which represents a 10.2% decrease. In 2008 sales volume decreased by 14.6% and was partially offset by a 5.7% increase in the average price per unit. The Company believes that the decrease in sales volume is a result of lower consumer demand attributable to poor macroeconomic conditions, which includes continued softness in the building materials industry, the erosion of home values and the tightening of the credit market. The increase in average price per unit is primarily a result of a January 2008 price increase of 7.0% and a favorable mix of products sold.

*Gross Profit.* Gross profit increased 125.8% to \$89.0 million in 2008 from \$39.4 million in 2007. Gross profit in 2007 was adversely affected by \$37.8 million of charges discussed above in *Net Sales* and \$11.0 million recognized in cost of sales primarily related to inventory valuation adjustments for certain inventories reclaimed for use in the manufacturing process. Gross profit in 2008 was adversely impacted by aggregate charges of \$4.4 million comprised of \$2.9 million of inventory valuation adjustments primarily related to certain inventories being reclaimed for use in the manufacturing process, \$0.9 million of freight charges to move inventories from the idled Olive Branch facility to the Company's two other production facilities and \$0.6 million of charges recognized upon a write-down of certain assets. Before giving effect to these charges gross profit in 2008 and 2007 was \$93.4 million and \$88.2 million, respectively, an improvement of \$5.2 million or 5.9%. The \$5.2 million increase was primarily attributable to lower unit manufacturing costs partially offset by the 14.6% decrease in sales volume. The lower manufacturing costs resulted primarily from production efficiencies and cost containment initiatives. Before giving effect to the aforementioned charges, gross profit as a percentage of net sales, or gross margin, increased to 28.4% in 2008 from 24.1% in 2007. Gross margin was positively affected by improved production rates and yields and process control and cost reduction initiatives, which accounted for a 6.5% increase in gross margin and the affects of the 2008 price increase and product mix, which accounted for a 4.1% increase in gross margin in 2008 as compared to 2007. The positive effect of the foregoing factors on gross margin in 2008 was offset, in part, by the negative effect on gross margin of 5.6% from reduced capacity utilization.

*Selling, General and Administrative Expenses.* Selling, general and administrative expenses decreased 43.9% to \$67.0 million in 2008 from \$119.4 million in 2007. As a percentage of net sales, total selling, general and administrative expenses decreased to 20.3% in 2008 from 36.3%

## Edgar Filing: TREX CO INC - Form 10-K/A

in 2007. Selling, general and administrative expenses in 2007 reflected \$40.4 million of expenses related to replacement of product that exhibited surface defects, primarily driven by the increase in the warranty liability and \$6.1 million of charges for losses on disposal of fixed assets, partially offset by a \$3.25 million recovery pursuant to a settlement with ExxonMobil for the recovery of legal fees. Payment for claims related to the aforementioned surface defects were recognized against the existing warranty liability during 2008 and, therefore, did not affect selling, general and administrative expenses. In 2008 selling, general and administrative expenses were adversely affected by incremental incentive compensation of \$7.2 million, \$1.0 million of severance expense primarily related to the Company's reduction in force, \$0.8 million related to a patent infringement legal proceeding and \$0.5 million for losses on disposal of fixed assets. Before giving effect to these charges, selling, general and administrative expenses in 2008 and 2007 were \$57.5 million and \$76.2 million, respectively, a decrease of \$18.7 million or 24.5%. The \$18.7 million lower selling, general and administrative expenses in 2008 were comprised principally of a decrease in salaries and personnel related expenses of \$7.2 million, a \$5.6 million reduction in branding expense, a \$2.8 million reduction in allowance for doubtful accounts and a \$1.2 million decrease in professional fees.

**Table of Contents**

*Interest Expense.* Net interest expense increased 32.9% to \$15.3 million in 2008 from \$11.5 million in 2007. The increase in net interest expense was primarily attributable to an increase of \$3.2 million of non-cash interest related to the adoption of FSP APB 14-1, combined with a \$0.8 million reduction of interest capitalized in 2008 as compared to 2007 due to less capital spending in 2008 and a \$0.5 million increase in unrealized losses related the change in the fair value of interest rate swaps in 2008 as compared to 2007. These factors were partially offset by a \$0.6 million prepayment penalty recorded in 2007 related to the payment of the Company's Senior Secured Notes.

*Provision for Income Taxes.* The Company recorded a benefit for income taxes of \$0.8 million in 2008 compared to a benefit for income taxes of \$26.1 million in 2007, which resulted in an effective tax rate of -11.1% in 2008 and 28.5% in 2007. The effective tax rates in both 2007 and 2008 were lower than the expected statutory tax rate primarily due to changes in the valuation allowance related to the Company's deferred tax assets. The valuation allowance increased by \$7.4 million in 2007 which offset, in part, the expected statutory tax benefit and lowered the resulting effective tax rate. The valuation allowance decreased by \$4.0 million in 2008 due to the realization of certain deferred tax assets as a result of net income generated. The \$4.0 million decrease in the valuation allowance substantially offset the expected statutory tax expense and lowered the effective tax rate. The 2008 effective tax rate was also affected by a \$0.5 million benefit recognized due to the reversal of liabilities related to uncertain tax positions upon the expiration of their statute of limitations and the recognition of certain refundable federal tax credits of \$0.2 million.

***2007 Compared to 2006***

*Net Sales.* Net sales in 2007 decreased 2.4% to \$329.0 million from \$337.0 million in 2006. Net sales in 2007 were adversely affected by charges of \$37.8 million. The Company recorded \$25.5 million of charges against net sales for product replacement expenses, driven by the increase in the warranty liability recorded in 2007 and \$12.3 million of charges against net sales for distributor credits primarily related to the voluntarily return of older-generation Trex Accents products. Net sales in 2006 were adversely affected by charges of \$3.6 million for product replacement expenses. Before giving effect to these charges, net sales in 2007 were \$366.8 million compared to \$340.5 million in 2006 which represents a 7.7% increase. The increase in net sales was primarily attributable to an increase in revenue per product unit and lower sales discounts. The increase in revenue per product unit resulted from a price increase of 7% on all products effective in May 2006. Lower sales discounts resulted from lower costs under the Company's early buy sales program and the extension of fewer incentives to distributors in the Company's annual sales discount programs.

The Company offered various sales incentives to its distributor customers during both 2006 and 2007. The Company has historically utilized an annual early buy sales program to create an incentive for distributors and dealers to commit to purchase Trex products before the start of the decking season. The Company's early buy program in 2006 and 2007 for purchases in the first four months of each year consisted of an option of extended terms or an early payment discount and a cash rebate for shipments that are sent directly to the dealer locations. The expense, which the Company recognized in 2007 for the early payment discount, was comparable to the expense it recognized in 2006. The payment options provided in the 2006 early buy program included prompt payment discounts from 0.5% to 2.0% or extended payment terms from 30 to 90 days. The payment options provided in the 2007 early buy program included prompt payment discounts from 0.5% to 3.0% or extended payment terms from 30 to 90 days. The Company recognized an expense of \$1.2 million for direct-to-dealer shipments in 2007 during the early buy sales program compared to an expense of \$2.3 million for direct-to-dealer shipments in 2006, as a lower percentage of shipments during the early buy sales program went direct-to-dealer in 2007. In addition, the Company offers certain annual sales incentives to dealers, which vary based on the level of sales activity from those dealers. The Company reduced the annual incentive program during 2007. The expenses recognized through the annual dealer incentive program in 2007 was \$1.8 million compared to \$3.8 million in 2006.

*Gross Profit.* Gross profit decreased 50.3% to \$39.4 million in 2007 from \$79.3 million in 2006. Gross profit in 2007 was adversely affected by \$37.8 million of charges discussed above in *Net Sales* and \$11.0 million recognized in cost of sales primarily related to inventory valuation adjustments for certain inventories reclaimed for use in the manufacturing process. Gross profit in 2006 was adversely impacted by the \$3.6 million of charges discussed in *Net Sales*. Before giving effect to these charges gross profit in 2007 and 2006 was \$88.2 million and \$82.9 million, respectively, an increase of \$5.3 million or 6.5%. The \$5.3 million increase was primarily attributable to the 2006 price increase which was partially offset by higher unit manufacturing costs, which resulted principally from production inefficiencies and lower manufacturing utilization. Before giving effect to the aforementioned charges, gross profit as a percentage of net sales, or gross margin, decreased to 24.1% in 2007 from 24.3% in 2006. Such decrease in gross margin in 2007, resulted from a decrease in production rates and yields, higher raw materials costs and higher labor and manufacturing costs due to product quality initiatives and lower manufacturing utilization, which accounted for a 5.5% decrease in gross margin. The negative effect of these factors in 2007 was offset in part by higher sales prices and an improved product mix, which accounted for a 5.3% increase in gross margin.

*Selling, General and Administrative Expenses.* Selling, general and administrative expenses increased 63.1% to \$119.4 million in 2007 from \$73.2 million in 2006. Selling, general and administrative expenses in 2007 reflected \$40.4 million of expenses related to replacement of product that exhibited surface defects, primarily driven by the increase in the warranty liability and \$6.1 million of charges for losses on disposal of fixed assets, partially offset by a \$3.25 million recovery pursuant to a settlement with ExxonMobil for the recovery of legal fees. In 2006 selling,

general and administrative expenses were adversely affected by \$6.6 million of expense

---

## **Table of Contents**

related to replacement of product that exhibited surface defects. Before giving effect to these charges, selling, general and administrative expenses in 2007 and 2006 were \$76.2 million and \$66.6 million, respectively, an increase of \$9.6 million or 14.4%. The \$9.6 million increase principally resulted from \$4.6 million of expense related to the suspension of operation of the Company's Olive Branch, Mississippi manufacturing facility, a \$3.5 million increase in personnel-related costs, and an increase of \$3.3 million in branding expenses. As a result of the suspension of operations at the Olive Branch facility, all costs related to the facility are recognized in selling, general and administrative expenses until such time as the facility is placed back into service. The \$4.6 million of expense recognized in 2007 in selling, general and administrative expenses related to the Olive Branch facility consisted of \$3.3 million of costs specifically related to the suspension of operations and \$1.3 million of ongoing costs, which primarily reflected depreciation charges of \$1.0 million. The \$3.3 million of incremental costs specifically related to the suspension of operations included personnel costs and raw material storage costs under contractual commitments, including a \$0.4 million contract termination charge on a leased facility for raw material storage and inventory management costs associated with transfers of raw material and finished goods inventory to the Company's Winchester, Virginia and Fernley, Nevada manufacturing plants. The effect of these factors was offset in part by a \$2.0 million decrease in expenses associated with the lease for office space the Company is subletting.

*Interest Expense.* Net interest expense increased to \$11.5 million in 2007 from \$3.0 million in 2006. The increase in net interest expense resulted primarily from an increase in average debt balances under the Company's revolving credit facility and from an increase in total debt as a result of the Company's combined issuance of \$97.5 million principal amount of convertible senior subordinated notes in June and July 2007, and, to a lesser extent, as a result of an additional \$2.5 million in non-cash interest expense recorded in 2007 due to the adoption on FSP ABP 14-1 and a \$0.6 million prepayment penalty paid in connection with the retirement of the Company's senior secured notes. The higher average debt balances under the Company's revolving credit facility during 2007 were required to fund the higher levels of inventories at each manufacturing location. The Company capitalized \$1.0 million and \$1.8 million of interest on construction in process in 2007 and 2006, respectively.

*Provision for Income Taxes.* The Company recorded a benefit for income taxes of \$26.1 million in 2007 compared to a provision for income taxes of \$0.7 million in 2006 which resulted in an effective tax rate of 28.5% in 2007 and 23.2% in 2006. The effective tax rate in 2007 was lower than the expected statutory tax rate primarily due to a \$7.4 million increase in the valuation allowance related to the Company's deferred tax assets. The increase in the valuation allowance 2007 offset, in part, the expected statutory tax benefit and lowered the resulting effective tax rate. The effective tax rate in 2006 was lower than the expected statutory tax rate primarily due primarily to the recognition of certain federal and state tax credits and incentives.

## **Liquidity and Capital Resources**

The Company finances its operations and growth primarily with cash flow from operations, borrowings under its credit facility and other loans, operating leases and normal trade credit terms from operating activities.

*Sources and Uses of Cash.* Net cash provided by operating activities totaled \$33.0 million in 2008 compared to net cash used in operating activities of \$1.2 million in 2007. The Company generated operating cash flow before the change in operating assets and liabilities of \$42.5 million in 2008 compared to a use of \$55.3 million before the change in operating assets and liabilities in 2007. The increase is attributable to a net increase of \$72.9 million in net income combined with an increase of \$6.6 million in depreciation and amortization. Net changes in operating assets and liabilities decreased \$9.4 million in 2008 compared to an increase of \$54.1 million in 2007. The decrease in cash flow related to changes in operating assets and liabilities resulted primarily from decreases in accounts payable and accrued expenses, primarily as a result of warranty payments, offset in part by decreases in inventories. In 2008, inventories decreased \$23.2 million compared to a decrease of \$18.9 million in 2007. In 2008, accounts payable and accrued expenses decreased \$12.5 million compared to an increase of \$19.3 million in 2007. Net cash used in operations decreased \$2.9 million in 2007 from 2006 as a result of decreased working capital usage and lower net income.

Net cash used in investing activities totaled \$8.6 million in 2008 compared to cash used in investing activities of \$24.0 million in 2007. This reduction was a direct result in reduced capital expenditures in 2008 compared to 2007. Capital expenditures in 2008 were applied primarily to the purchase of plastic reprocessing equipment and other equipment to improve product quality and reduce costs. In 2007, net cash used in investing activities totaled \$24.0 million compared to \$27.7 million in 2006.

Net cash used in financing activities was \$1.3 million in 2008 compared to cash provided for financing activities of \$24.6 million in 2007. In 2008, the Company reduced net debt by \$1.2 million and repaid borrowings under the revolving credit facility. In 2007, the \$94.2 million of net proceeds received by the Company from its sale of \$97.5 million principal amount of convertible senior subordinated notes was offset in part by net debt reductions of \$45.7 million under its revolving credit facility and \$24.0 million under its outstanding senior secured notes, which were repaid with such net proceeds. Net cash provided by financing activities was \$24.6 million in 2007, compared to net cash provided by financing activities of \$31.1 million in 2006.

## Edgar Filing: TREX CO INC - Form 10-K/A

*Indebtedness.* At December 31, 2008, the Company's indebtedness, including the fair value of the interest rate swaps, totaled \$133.8 million and the annualized overall weighted average interest rate of such indebtedness, including the effect of the Company's interest rate swaps, was approximately 5.57%.

*Sale of Convertible Notes and Related Debt Agreement Amendments.* On June 18, 2007, the Company issued \$85.0 million principal amount of its 6.00% convertible senior subordinated notes due 2012, or convertible notes, through an underwritten public offering. The Company used a portion of net proceeds of \$82.1 million from the sale of the convertible notes to repay in full \$24.0

---

**Table of Contents**

million principal amount of its 8.32% senior secured notes due July 19, 2009 and \$45.7 million principal amount of borrowings outstanding under its revolving credit facility. The Company paid a prepayment penalty of \$0.6 million in connection with the retirement of the senior secured notes. On July 12, 2007, the underwriters of the convertible notes offering exercised their over-allotment option to purchase an additional \$12.5 million principal amount of convertible notes. The Company received net proceeds of \$12.1 million from the sale of the additional convertible notes, which it issued on July 17, 2007. For information about the convertible notes, see note 7 to the consolidated financial statements appearing elsewhere in this report.

Effective on June 18, 2007, in connection with its offering of the convertible notes, the Company entered into amendments to its credit agreement with BB&T and its reimbursement and credit agreement, or reimbursement agreement, with JPMorgan Chase Bank, N.A., or JPMorgan, relating to the outstanding bonds issued in December 2004 by a Mississippi public corporation to finance specified costs relating to solid waste disposal facilities used in connection with the Company's manufacturing plant in Olive Branch, Mississippi. Among other things, the amendments to the agreements:

extended the maturity of the revolving credit facility to June 30, 2010;

reset the maximum revolving commitment amount under the revolving credit facility to be (a) \$70 million for the period commencing December 1 of each calendar year to and including May 31 of the immediately succeeding calendar year, and (b) \$40 million for the period commencing June 1 to and including November 30 of each calendar year;

amended the financial covenants the Company is required to observe under the agreements, to provide the Company with additional operating flexibility;

amended the applicable real estate term loan margin, the applicable revolving loan margin and the unused commitment fee percentage definitions in the credit agreement so that such loan margins and fee percentage will be determined with reference to the Company's ratio of funded net senior debt to EBITDA, as defined for purposes of the reimbursement agreement; and

revised the annual facility fee payable by the Company under the reimbursement agreement, which will be calculated based on the Company's ratio of funded net senior debt to EBITDA, as defined for purposes of the reimbursement agreement.

On June 18, 2007, concurrently with the effectiveness of the foregoing amendments to the credit agreement and the reimbursement agreement, the Company executed three promissory notes to BB&T under the credit agreement secured by real property of the Company in the aggregate principal amount of approximately \$6.7 million. The three promissory notes, which replaced previously outstanding promissory notes, extended the maturity of the underlying indebtedness to June 30, 2011.

After June 18, 2007, the Company entered into additional amendments to its debt agreements, including the credit agreement and the reimbursement agreement, as discussed below under *Compliance with Debt Covenants*.

Amounts drawn under the revolving credit facility are subject to a borrowing base consisting of accounts receivable and finished goods inventories. As of December 31, 2007, and 2008, respectively, no amount was outstanding under the revolving credit facility and the borrowing base totaled approximately \$52.6 million and \$63.8 million, respectively.

Consistent with generally accepted accounting principles, the Company capitalized \$4.0 million of financing-related expenses as deferred financing costs in 2007 relating to the refinancing of the Company's revolving credit facility and issuance of the convertible notes and the foregoing real estate notes. The deferred financing costs will be amortized over the terms of the various debt instruments for periods that will vary between three to five years.

*Compliance With Debt Covenants.* The Company's ability to make scheduled principal and interest payments on its real estate loans, convertible notes and bond loan agreement, borrow and repay amounts under its revolving credit facility, and continue to comply with its loan covenants will depend primarily on its ability to generate substantial cash flow from operations. To remain in compliance with its credit facility, real estate



## Edgar Filing: TREX CO INC - Form 10-K/A

loans and reimbursement agreement, the Company must maintain specified financial ratios based on its levels of debt, capital, net worth, fixed charges, and earnings (excluding extraordinary gains and extraordinary non-cash losses) before interest, taxes, depreciation and amortization, all of which are subject to the risks of its business, some of which are discussed in this report under Risk Factors.

The Company was in compliance with all covenants contained in its loan agreements at December 31, 2008.

Effective January 1, 2009, financial covenants related to the credit agreement and reimbursement agreement with BB&T and JPMorgan reset to the following so that:

the Company's senior debt ratio, or ratio of consolidated senior debt to consolidated EBITDA (as defined for purposes of the agreements), may not be greater than (a) 3.0 to 1 for the period commencing January 1, 2009 to and including March 31, 2009 and (b) thereafter (A) 2.5 to 1 for any measurement period ending June 30 or September 30, and (B) 3.0 to 1 for any measurement period ending December 31 or March 31;

the Company's fixed charge coverage ratio, or ratio of consolidated EBITDA to fixed charges (as defined for purposes of the agreements), may not be less than (a) 1.4 to 1 for any measurement period commencing after January 1, 2009;

**Table of Contents**

The Company's ratio of total consolidated debt to total consolidated capitalization (as defined for purposes of the agreements) may not be greater than (a) 60% for the period commencing January 1, 2009 to and including March 31, 2009, and (b) thereafter (A) 50% for each period commencing April 1 of a calendar year to and including September 30 of such calendar year, and (B) 60% for each period commencing October 1 of a calendar year to and including March 31 of the immediately succeeding calendar year; and

the Company's consolidated tangible net worth (as defined for purposes of the agreements) may not be less than the sum of (a) \$85 million, (b) 100% of the net proceeds of all stock issued after January 1, 2008, plus (c) 50% of consolidated net income after December 31, 2007 (taken as one accounting period), but excluding from such calculation of consolidated net income for purposes of (c) any quarter in which consolidated net income is negative.

*Contractual Obligations.* The following tables show, as of December 31, 2008, the Company's contractual obligations and commercial commitments, which consist primarily of long-term debt, interest payments on long-term debt, purchase commitments and operating leases (in thousands):

**Contractual Obligations****Payments Due by Period**

	<b>Total</b>	<b>Less than 1 year</b>	<b>1-3 years</b>	<b>4-5 years</b>	<b>After 5 years</b>
Long-term debt	\$ 131,734	\$ 1,293	\$ 5,986	\$ 98,834	\$ 25,621
Interest payments on long-term debt (1)	27,719	6,530	12,788	4,047	4,354
Purchase commitments (2)	99,971	32,771	67,200		
Operating leases	47,557	7,792	13,267	9,454	17,044
<b>Total contractual cash obligations</b>	<b>\$ 306,981</b>	<b>\$ 48,386</b>	<b>\$ 99,241</b>	<b>\$ 112,335</b>	<b>\$ 47,019</b>

(1) A portion of the interest expense disclosed is subject to variable interest rates. The amounts disclosed above assume that variable interest rates are equal to rates at December 31, 2008.

(2) Purchase commitments represent supply contracts with third-party manufacturers.

The Company uses interest rate swaps to manage its exposure to fluctuations in the interest rates on its variable-rate debt and has entered into interest rate swap contracts that effectively convert a substantial portion of its variable-rate debt to fixed-rate obligations. At December 31, 2008, the fair value of the debt-related derivatives was \$2.1 million and was classified as a long-term liability.

The Company does not have off-balance sheet financing arrangements other than its operating leases.

*Capital and Other Cash Requirements.* The Company made capital expenditures of \$27.7 million in 2006, \$24.0 million in 2007 and \$7.8 million in 2008, primarily to make process and productivity improvements. The Company currently estimates that its capital expenditures in 2009 will be approximately \$10 million. Capital expenditures in 2009 are expected to be used primarily to make process and productivity improvements and upgrade systems.

The Company believes that cash on hand, cash flow from operations and borrowings expected to be available under the Company's existing revolving credit facility will provide sufficient funds to enable the Company to fund its planned capital expenditures, make scheduled principal and interest payments, fund the warranty reserve, meet its other cash requirements and maintain compliance with terms of its debt agreements for at least the next 12 months. The Company currently expects that it will fund its future capital expenditures from operations and borrowings under its revolving credit facility. The actual amount and timing of the Company's future capital requirements may differ materially from the Company's estimate depending on the demand for Trex and new market developments and opportunities. The Company's ability to meet its cash needs during the next 12 months and thereafter could be adversely affected by various circumstances, including increases in raw materials and product replacement costs, quality control problems, higher than expected product warranty claims, service disruptions and lower than expected collections of accounts receivable. In addition, any failure by the Company to negotiate amendments to its existing debt agreements to resolve any future noncompliance with financial covenants could adversely affect the Company's liquidity by reducing its access to revolving credit

## Edgar Filing: TREX CO INC - Form 10-K/A

borrowings needed primarily to fund its seasonal borrowing needs. The Company may determine that it is necessary or desirable to obtain financing through bank borrowings or the issuance of debt or equity securities to address such contingencies or changes to its business plan. Debt financing would increase the Company's level of indebtedness, while equity financing would dilute the ownership of the Company's stockholders. There can be no assurance as to whether, or as to the terms on which, the Company would be able to obtain such financing, which would be restricted by covenants contained in its existing debt agreements.

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

The financial statements listed in Item 15 and appearing on pages 23 through 49 are incorporated by reference in this Item 8 and are filed as part of this report.

---

## **Table of Contents**

### **Item 9A. Controls and Procedures**

#### **Evaluation of Disclosure Controls and Procedures**

Our management, with the participation of our Chief Executive Officer, who is our principal executive officer, and our Chief Financial Officer, who is our principal financial officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of December 31, 2008. Based upon this evaluation, our Chief Executive Officer and our Chief Financial Officer concluded that, as a result of the material weakness in our internal control over financial reporting as of December 31, 2008 described below under Management's Report on Internal Control Over Financial Reporting, our disclosure controls and procedures were not effective as of December 31, 2008. We have initiated the implementation of measures to remediate this material weakness as described below under Remediation of Material Weakness in Internal Control Over Financial Reporting.

#### **Management's Report on Internal Control Over Financial Reporting**

We, as members of management of Trex Company, Inc. (the Company), are responsible for establishing and maintaining adequate internal control over financial reporting. The Company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

We assessed the Company's internal control over financial reporting as of December 31, 2008, based on criteria for effective internal control over financial reporting established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO Framework). Based on this assessment, management identified a material weakness (as defined by the Public Company Accounting Oversight Board) as of December 31, 2008.

At December 31, 2008, the Company failed to institute procedures to accurately compute the valuation allowance related to the Company's deferred tax assets. As a result, in determining the valuation allowance, the Company considered as a source of future taxable income existing taxable temporary differences related to indefinite-lived intangible assets. Because the timing of reversal of these deferred tax liabilities is unknown, they are not a reliable source of recovery of deferred tax assets. The result of these errors is that the valuation allowance for deferred tax assets was understated at December 31, 2007 and each subsequent financial reporting date through December 31, 2008. As further described in Note 2 to the consolidated financial statements, this error resulted in the restatement of the Company's financial statements for the years ended December 31, 2007 and 2008, including the interim financial statements for these periods. Management has concluded that this control deficiency constitutes a material weakness. Accordingly, management has determined that, because of this material weakness, the Company did not maintain effective internal control over financial reporting as of December 31, 2008 based on the criteria specified in the COSO Framework.

#### **Remediation Efforts Related to Material Weakness in Internal Control Over Financial Reporting**

We intend to remediate the material weakness identified above. Specifically, we intend to improve documentation with respect to our consideration of the four possible sources of taxable income proscribed in paragraph 21 of FAS 109 when considering the need for a valuation allowance against our deferred tax assets. Accordingly, management's assessment that the Company did not maintain effective internal control over financial reporting as of December 31, 2008 remains unchanged. Management has not yet evaluated the effectiveness of our internal control over financial reporting as of December 31, 2009. Our internal control over financial reporting will also be subject to testing by our independent registered public accounting firm. There can be no assurance at this time that the actions taken to date will effectively remediate the material weakness described above. We are continuing to closely monitor the effectiveness of our processes, procedures and controls, and will make any further changes as management determines appropriate.

#### **Changes in Internal Control Over Financial Reporting**

## Edgar Filing: TREX CO INC - Form 10-K/A

Other than the matters described in this Item 9A under Remediation of Material Weakness in Internal Control Over Financial Reporting, during the fourth quarter ended December 31, 2008, there have been no changes in our internal control over financial reporting that have materially affected, or that are reasonably likely to materially affect, our internal control over financial reporting.

**Table of Contents**

Ernst & Young LLP, an independent registered public accounting firm, which audited the Company's consolidated financial statements included in this report, has issued a report on management's assessment of the effectiveness and on the Company's internal control over financial reporting, which is included in this report.

TREX COMPANY, INC.

August 10, 2009

By: /s/ RONALD W. KAPLAN  
Ronald W. Kaplan  
President and Chief Executive Officer  
(Principal Executive Officer)

August 10, 2009

By: /s/ JAMES E. CLINE  
James E. Cline  
Vice President and Chief Financial Officer  
(Principal Financial Officer)

---

**Table of Contents**

**Report of Independent Registered Public Accounting Firm  
on Internal Control over Financial Reporting**

The Board of Directors and Stockholders of

Trex Company, Inc.

We have audited Trex Company, Inc.'s internal control over financial reporting as of December 31, 2008, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Trex Company, Inc.'s management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Report of Management on Trex Company, Inc.'s Internal Control over Financial Reporting. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company's annual or interim financial statements will not be prevented or detected on a timely basis. The following material weakness has been identified and included in management's assessment. Management has identified a material weakness in controls related to the company's income tax accounting process. This material weakness was considered in determining the nature, timing, and extent of audit tests applied in our audit of the 2008 financial statements and this report does not affect our report dated August 7, 2009 on those financial statements.

In our opinion, because of the effect of the material weakness described above on the achievement of the objectives of the control criteria, Trex Company, Inc. has not maintained effective internal control over financial reporting as of December 31, 2008, based on the COSO criteria.

/s/ ERNST & YOUNG LLP

Richmond, Virginia

August 7, 2009

**Table of Contents****PART IV****Item 15. Exhibits and Financial Statement Schedules**

(a)(1) The following restated consolidated financial statements of the company appear on pages 23 through 49 of this report and are incorporated by reference in Part II, Item 8:

<u>Report of Independent Registered Public Accounting Firm</u>	22
Consolidated Financial Statements	
<u>Consolidated Balance Sheets as of December 31, 2007 and 2008</u>	23
<u>Consolidated Statements of Operations for the three years ended December 31, 2008</u>	24
<u>Consolidated Statements of Stockholders' Equity and Comprehensive Income for the three years ended December 31, 2008</u>	25
<u>Consolidated Statements of Cash Flows for the three years ended December 31, 2008</u>	26
<u>Notes to Consolidated Financial Statements</u>	27

(a)(2) All schedules for which provision is made in the applicable accounting regulations of the Securities and Exchange Commission are not required under the related instructions, or are inapplicable or not material and therefore have been omitted.

(a)(3) The following exhibits are either filed with this Form 10-K or are incorporated herein by reference. The company's Securities Exchange Act file number is 001-14649.

**Exhibit**

<b>Number</b>	<b>Exhibit Description</b>
3.1	Restated Certificate of Incorporation of Trex Company, Inc. (the "Company"). Filed as Exhibit 3.1 to the Company's Registration Statement on Form S-1 (No. 333-63287) and incorporated herein by reference.
3.2	Amended and Restated By-Laws of the Company. Filed as Exhibit 3.2 to the Company's Current Report on Form 8-K filed May 7, 2008 and incorporated herein by reference.
4.1	Specimen certificate representing the Company's common stock. Filed as Exhibit 4.1 to the Company's Registration Statement on Form S-1 (No. 333-63287) and incorporated herein by reference.
4.2	Indenture, dated as of June 18, 2007, between Trex Company, Inc. and The Bank of New York, as trustee. Filed as Exhibit 4.1 to the Company's Current Report on Form 8-K filed on June 19, 2007 and incorporated herein by reference.
4.3	Supplemental Indenture, dated as of June 18, 2007, between Trex Company, Inc. and The Bank of New York, as trustee, including the form of 6.00% Convertible Senior Subordinated Note due 2012. Filed as Exhibit 4.2 to the Company's Current Report on Form 8-K filed on June 19, 2007 and incorporated herein by reference.
10.1	Description of Management Compensatory Plans and Arrangements. Filed as Exhibit 10.1 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.
10.2	Trex Company, Inc. 2005 Stock Incentive Plan. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on May 7, 2008 and incorporated herein by reference.
10.3	Trex Company, Inc. Amended and Restated 1999 Incentive Plan for Outside Directors. Filed as Exhibit 10.4 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2007 and incorporated herein by reference.



**Table of Contents**

**Exhibit**

<b>Number</b>	<b>Exhibit Description</b>
10.4	Form of Trex Company, Inc. 2005 Stock Incentive Plan Non-Incentive Stock Option Agreement. Filed as Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005 and incorporated herein by reference.
10.5	Form of Trex Company, Inc. 2005 Stock Incentive Plan Stock Appreciation Rights Agreement. Filed as Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005 and incorporated herein by reference.
10.6	Form of Trex Company, Inc. 2005 Stock Incentive Plan Performance Award Agreement. Filed as Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005 and incorporated herein by reference.
10.7	Form of Trex Company, Inc. 2005 Stock Incentive Plan Restricted Stock Agreement, as amended. Filed as Exhibit 10.8 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and incorporated herein by reference.
10.8	Form of Trex Company, Inc. Amended and Restated 1999 Incentive Plan for Outside Directors Non-Incentive Stock Option Agreement for Directors. Filed as Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006 and incorporated herein by reference.
10.9	Form of Trex Company, Inc. Amended and Restated 1999 Incentive Plan for Outside Directors Stock Appreciation Rights Agreement. Filed as Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006 and incorporated herein by reference.
10.10	Form of Lock-Up Agreement, dated as of December 20, 2005. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on December 21, 2005 and incorporated herein by reference.
10.11	Form of Change in Control Severance Agreement for Officers of Trex Company, Inc. other than the Chief Executive Officer. Filed as Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2007 and incorporated herein by reference.
10.12	Consulting Agreement, dated September 10, 2007, by and between Trex Company, Inc. and Anthony J. Cavanna. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on September 11, 2007 and incorporated herein by reference.
10.13	Amended and Restated Stock Appreciation Rights Agreement, between Trex Company, Inc. and Anthony J. Cavanna dated August 14, 2007. Filed as Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2007 and incorporated herein by reference.
10.14	Amended and Restated Stock Appreciation Rights Agreement, between Trex Company, Inc. and Anthony J. Cavanna dated August 14, 2007. Filed as Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2007 and incorporated herein by reference.
10.15	Amended and Restated Restricted Stock Agreement, between Trex Company, Inc. and Anthony J. Cavanna dated August 14, 2007. Filed as Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2007 and incorporated herein by reference.
10.16	Employment Agreement, dated as of January 1, 2008, between Trex Company, Inc. and Ronald W. Kaplan. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on January 2, 2008 and incorporated herein by reference.
10.17	Change in Control Severance Agreement, dated as of January 1, 2008, between Trex Company, Inc. and Ronald W. Kaplan. Filed as Exhibit 10.2 to the Company's Current Report on Form 8-K filed on January 2, 2008 and incorporated herein by reference.

**Table of Contents**

**Exhibit**

<b>Number</b>	<b>Exhibit Description</b>
10.18	Consulting Agreement, dated February 1, 2008, by and between Trex Company, Inc. and Harold F. Monahan. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on February 1, 2008 and incorporated herein by reference.
10.19	Form of Indemnity Agreement for Directors. Filed as Exhibit 10.19 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.
10.20	Form of Indemnity Agreement for Officers. Filed as Exhibit 10.20 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.
10.21	Form of Indemnity Agreement for Director/Officers. Filed as Exhibit 10.21 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.
10.22	Form of Distributor Agreement of TREX Company, Inc. Filed as Exhibit 10.5 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2001 and incorporated herein by reference.
10.23	Form of Distributor Agreement of TREX Company, Inc. Filed as Exhibit 10.23 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.
10.24	Form of Trex Company, Inc. Fencing Agreement for Installers/Retailers. Filed as Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006 and incorporated herein by reference.
10.25	Deed of Lease, dated June 15, 2000, between TREX Company, LLC and Space, LLC. Filed as Exhibit 10.16 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2000 and incorporated herein by reference.
10.26	Deed of Lease, dated as of July 27, 2005, between the Company and 1 Dulles Town Center, L.L.C. Filed as Exhibit 10.34 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2005 and incorporated herein by reference.*
10.27	Credit Agreement, dated as of June 19, 2002, among TREX Company, LLC, the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.2 to the Company's Current Report on Form 8-K filed on June 25, 2002 (as amended by the Company's Current Report on Form 8-K/A filed on June 28, 2002) and incorporated herein by reference.
10.28	Security Agreement, dated as of March 16, 2007, by and among the Company and Branch Banking and Trust Company, as collateral agent. Filed as Exhibit 10.16 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and incorporated herein by reference.
10.29	First Amendment to Security Agreement, dated as of and effective as of September 30, 2007, with Branch Banking and Trust Company, as Collateral Agent and Senior Secured Party, and JPMorgan Chase Bank, N.A., as Junior Secured Party. Filed as Exhibit 10.26 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2007 and incorporated herein by reference.
10.30	Credit Line Deed of Trust, dated June 19, 2002, by and among TREX Company, LLC, as grantor, BB&T-VA Collateral Service Corporation, as trustee, and Branch Banking and Trust Company of Virginia and Branch Banking and Trust Company, as note holder. Filed as Exhibit 10.5 to the Company's Current Report on Form 8-K filed on June 25, 2002 and incorporated herein by reference.
10.31	First Amendment to Credit Agreement, dated as of August 29, 2003, by and between the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.21 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2005 and incorporated herein by reference.
10.32	Second Amendment to Credit Agreement, dated as of September 30, 2004, among the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2004 and incorporated herein by reference.

**Table of Contents****Exhibit**

<b>Number</b>	<b>Exhibit Description</b>
10.33	Third Amendment to Credit Agreement, dated as of March 31, 2005, by and between the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.6 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005 and incorporated herein by reference.
10.34	Fourth Amendment to Credit Agreement, dated as of July 25, 2005, by and between the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.7 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005 and incorporated herein by reference.
10.35	Fifth Amendment to Credit Agreement, dated as of December 31, 2005, among the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.25 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2005 and incorporated herein by reference.
10.36	Sixth Amendment to Credit Agreement, dated as of November 9, 2006, among the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.24 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and incorporated herein by reference.
10.37	Seventh Amendment to Credit Agreement, dated as of December 31, 2006, among the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.25 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and incorporated herein by reference.
10.38	Eighth Amendment to Credit Agreement, dated as of March 16, 2007, among the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.26 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and incorporated herein by reference.
10.39	Ninth Amendment to Credit Agreement, effective as of June 18, 2007, between Trex Company, Inc. and Branch Banking and Trust Company. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on June 19, 2007 and incorporated herein by reference.
10.40	Tenth Amendment to Credit Agreement, dated as of December 21, 2007, by and between Trex Company, Inc. and Branch Banking and Trust Company. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on December 21, 2007 and incorporated herein by reference.
10.41	Eleventh Amendment to Credit Agreement, dated as of December 31, 2007, by and between Trex Company, Inc. and Branch Banking and Trust Company. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on March 7, 2008 and incorporated herein by reference.
10.42	Twelfth Amendment to Credit Agreement, dated as of June 16, 2008, by and between Trex Company, Inc. and Branch Banking and Trust Company. Filed as Exhibit 10.42 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.
10.43	Thirteenth Amendment to Credit Agreement, dated as of November 10, 2008, by and between Trex Company, Inc. and Branch Banking and Trust Company. Filed as Exhibit 10.43 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.
10.44	Promissory Note (Revolving Note), dated as of December 31, 2006, in the principal amount of \$100,000,000 from the Company payable to the order of Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.27 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and incorporated herein by reference.
10.45	Loan Agreement, dated as of December 1, 2004, between the Company and Mississippi Business Finance Corporation. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on December 20, 2004 and incorporated herein by reference.

**Table of Contents****Exhibit**

<b>Number</b>	<b>Exhibit Description</b>
10.46	Promissory Note, dated as of December 16, 2004, in the principal amount of \$25,000,000 from the Company payable to the order of Mississippi Business Finance Corporation. Filed as Exhibit 10.2 to the Company's Current Report on Form 8-K filed on December 20, 2004 and incorporated herein by reference.
10.47	Reimbursement and Credit Agreement, dated as of December 1, 2004, between the Company and JPMorgan Chase Bank, N.A., as Issuing Bank and Administrative Agent. Filed as Exhibit 10.3 to the Company's Current Report on Form 8-K filed on December 20, 2004 and incorporated herein by reference.
10.48	First Amendment to Reimbursement and Credit Agreement, dated as of July 25, 2005, by and between the Company and JPMorgan Chase Bank, N.A., as Issuing Bank and Administrative Agent. Filed as Exhibit 10.5 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005 and incorporated herein by reference.
10.49	Second Amendment to Reimbursement and Credit Agreement, dated as of December 31, 2005, by and between the Company and JPMorgan Chase Bank, N.A., as Issuing Bank and Administrative Agent. Filed as Exhibit 10.30 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2005 and incorporated herein by reference.
10.50	Third Amendment to Reimbursement and Credit Agreement, dated as of November 21, 2006, by and between the Company and JPMorgan Chase Bank, N.A., as Issuing Bank and Administrative Agent. Filed as Exhibit 10.33 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and incorporated herein by reference.
10.51	Fourth Amendment to Reimbursement and Credit Agreement, dated as of December 31, 2006, by and between the Company and JPMorgan Chase Bank, N.A., as Issuing Bank and Administrative Agent. Filed as Exhibit 10.34 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and incorporated herein by reference.
10.52	Fifth Amendment to Reimbursement and Credit Agreement, effective as of June 18, 2007, between Trex Company, Inc. and JPMorgan Chase Bank, N.A., as Issuing Bank and Administrative Agent. Filed as Exhibit 10.2 to the Company's Current Report on Form 8-K filed on June 19, 2007 and incorporated herein by reference.
10.53	Sixth Amendment to Reimbursement and Credit Agreement, dated as of December 21, 2007, between Trex Company, Inc. and JPMorgan Chase Bank, N.A., as Issuing Bank and Administrative Agent. Filed as Exhibit 10.2 to the Company's Current Report on Form 8-K filed on December 21, 2007 and incorporated herein by reference.
10.54	Seventh Amendment to Reimbursement and Credit Agreement, dated as of December 31, 2007, between Trex Company, Inc. and JPMorgan Chase Bank, N.A., as Issuing Bank and Administrative Agent. Filed as Exhibit 10.2 to the Company's Current Report on Form 8-K filed on March 7, 2008 and incorporated herein by reference.
10.55	Reimbursement Note, dated as of December 1, 2004, in the principal amount of \$25,308,220 from the Company payable to JPMorgan Chase Bank, N.A. Filed as Exhibit 10.4 to the Company's Current Report on Form 8-K filed on December 20, 2004 and incorporated herein by reference.
10.56	Land Deed of Trust, dated as of December 1, 2004, made by the Company to the trustee named therein for the benefit of JPMorgan Chase Bank, N.A. Filed as Exhibit 10.5 to the Company's Current Report on Form 8-K filed on December 20, 2004 and incorporated herein by reference.
10.57	First Amendment to Land Deed of Trust, dated as of and effective as of September 30, 2007, with JPMorgan Chase Bank, N.A., as Beneficiary and Secured Party, and the Trustee therein named for the benefit of such Beneficiary. Filed as Exhibit 10.52 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2007 and incorporated herein by reference.

**Table of Contents**

**Exhibit**

<b>Number</b>	<b>Exhibit Description</b>
10.58	Trust Indenture, dated as of December 1, 2004, between Mississippi Business Finance Corporation and J.P. Morgan Trust Company, National Association, as Trustee, including Form of Variable Rate Series 2004 Bond and Form of Fixed Rate Series 2004 Bond. Filed as Exhibit 10.6 to the Company's Current Report on Form 8-K filed on December 20, 2004 and incorporated herein by reference.
21	Subsidiaries of the Company. Filed herewith.
23	Consent of Ernst & Young LLP, Independent Registered Public Accounting Firm. Filed herewith.
31.1	Certification of Chief Executive Officer of the Company pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934. Filed herewith.
31.2	Certification of Chief Financial Officer of the Company pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934. Filed herewith.
32	Certifications pursuant to Rule 13a-14(b) under the Securities Exchange Act of 1934 and 18 U.S.C. § 1350. Filed herewith.

\* Portions of this exhibit have been omitted and filed separately with the Securities and Exchange Commission pursuant to a request for confidential treatment.

**Table of Contents**

**TREX COMPANY, INC.**

**Index to Consolidated Financial Statements**

	<b>Page</b>
<u>Report of Independent Registered Public Accounting Firm</u>	22
Consolidated Financial Statements	
<u>Consolidated Balance Sheets as of December 31, 2007 and 2008</u>	23
<u>Consolidated Statements of Operations for the three years ended December 31, 2008</u>	24
<u>Consolidated Statements of Changes in Stockholders' Equity and Comprehensive Income for the three years ended December 31, 2008</u>	25
<u>Consolidated Statements of Cash Flows for the three years ended December 31, 2008</u>	26
<u>Notes to Consolidated Financial Statements</u>	27
The following Consolidated Financial Statement Schedule of the Registrant is filed as part of this Report as required to be included in Item 15(a)(2):	

	<b>Page</b>
<u>Schedule II Valuation and Qualifying Accounts and Reserves</u>	50

---

**Table of Contents**

**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders of

Trex Company, Inc.

We have audited the accompanying consolidated balance sheets of Trex Company, Inc. as of December 31, 2008 and 2007, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2008. Our audits also included the financial statement schedule listed in the Index at Item 15. These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Trex Company, Inc. at December 31, 2008 and 2007, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2008, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

As discussed in Note 2, the Company has restated the accompanying consolidated financial statements as of and for the years ended December 31, 2008 and 2007 to correct an error in accounting for income taxes.

Also as discussed in Note 2, the Company on January 1, 2009 retrospectively adopted the provisions of Financial Accounting Standards Board Staff Position APB 14-1, Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement), and changed its method of accounting for certain convertible debt instruments. In addition, as discussed in Note 13, the Company changed its method of accounting for uncertain income tax positions in 2007 to comply with the provisions of Financial Accounting Standards Board Interpretation No. 48, Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Trex Company, Inc.'s internal control over financial reporting as of December 31, 2008, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated August 7, 2009 expressed an adverse opinion thereon.

/s/ ERNST & YOUNG LLP

Richmond, Virginia

August 7, 2009

**Table of Contents****TREX COMPANY, INC.****CONSOLIDATED BALANCE SHEETS**

	<b>December 31,</b>	
	<b>2007</b>	<b>2008</b>
	<b>As Restated</b>	<b>As Restated</b>
	<b>(See Note 2)</b>	<b>(See Note 2)</b>
	<b>(In thousands)</b>	
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 66	\$ 23,189
Accounts receivable (net of allowance for doubtful accounts of \$3.1 million and \$1.5 million in 2007 and 2008, respectively)	6,588	13,555
Inventories	92,569	69,397
Prepaid expenses and other assets	2,617	5,518
Income taxes receivable	2,376	2,554
Deferred income taxes	7,810	2,141
<b>Total current assets</b>	<b>112,026</b>	<b>116,354</b>
Property, plant and equipment, net	193,944	176,336
Goodwill	6,837	6,837
Other assets	7,722	7,557
<b>Total Assets</b>	<b>\$ 320,529</b>	<b>\$ 307,084</b>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Current Liabilities:		
Accounts payable	\$ 19,776	\$ 15,427
Accrued expenses	21,583	22,239
Accrued warranty	21,084	12,310
Current portion of long-term debt	1,198	1,293
<b>Total current liabilities</b>	<b>63,641</b>	<b>51,269</b>
Deferred income taxes	9,178	3,531
Accrued taxes	3,620	2,640
Non-current accrued warranty	18,901	9,546
Debt-related derivatives	1,044	2,069
Long-term debt	95,760	100,201
<b>Total Liabilities</b>	<b>192,144</b>	<b>169,256</b>
Commitments and contingencies (Note 14)		
Stockholders Equity:		
Preferred stock, \$0.01 par value, 3,000,000 shares authorized; none issued and outstanding		
Common stock, \$0.01 par value, 40,000,000 shares authorized; 15,076,738 and 15,310,343 shares issued and outstanding at December 31, 2007 and 2008, respectively	151	153
Additional paid-in capital	90,383	92,825
Accumulated other comprehensive loss	(557)	(1,092)
Retained earnings	38,408	45,942



Edgar Filing: TREX CO INC - Form 10-K/A

Total Stockholders' Equity	128,385	137,828
Total Liabilities and Stockholders' Equity	\$ 320,529	\$ 307,084

See accompanying notes to financial statements.

**Table of Contents****TREX COMPANY, INC.****CONSOLIDATED STATEMENTS OF OPERATIONS**

	Year Ended December 31,		
	2006	2007	2008
		(See Note 2)	As Restated (See Note 2)
	(In thousands, except share and per share data)		
Net sales	\$ 336,956	\$ 328,952	\$ 329,194
Cost of sales	257,671	289,529	240,170
Gross profit	79,285	39,423	89,024
Selling, general, and administrative expenses	73,223	119,439	66,958
Income (loss) from operations	6,062	(80,016)	22,066
Interest expense, net	3,011	11,503	15,282
Income (loss) before provision for income taxes	3,051	(91,519)	6,784
Provision (benefit) for income taxes	708	(26,105)	(750)
Net income (loss)	\$ 2,343	\$ (65,414)	\$ 7,534
Basic earnings (loss) per common share	\$ 0.16	\$ (4.39)	\$ 0.50
Basic weighted average common shares outstanding	14,829,832	14,884,174	14,956,927
Diluted earnings (loss) per common share	\$ 0.16	\$ (4.39)	\$ 0.50
Diluted weighted average common shares outstanding	14,892,966	14,884,174	15,113,083

See accompanying notes to financial statements.

**Table of Contents****TREX COMPANY, INC.****CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS****EQUITY AND COMPREHENSIVE INCOME**

	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Deferred Compensation (Dollars in thousands)	Accumulated Other Comprehensive Loss	Retained Earnings	Total
Balance, December 31, 2005	14,889,674	\$ 149	\$ 61,901	\$ (1,076)	\$ (481)	\$ 104,215	\$ 164,708
Comprehensive income:							
Net income						2,343	2,343
Net unrealized losses on derivatives, net of tax					(344)		(344)
Net derivative losses reclassified to earnings, net of tax					547		547
Total comprehensive income							2,546
Reclassification of deferred compensation upon adoption of SFAS 123(R)			(1,076)	1,076			
Employee stock purchase and option plans	19,131		411				411
Tax benefit of stock options and restricted stock			51				51
Repurchases of common stock	(14,916)		(435)				(435)
Stock based compensation	20,000		2,134				2,134
Balance, December 31, 2006	14,913,889	149	62,986		(278)	106,558	169,415
Comprehensive income:							
Net income as restated (See Note 2)						(65,414)	(65,414)
Net unrealized losses on interest rate swaps, net of tax					(605)		(605)
Net derivative losses reclassified to earnings, net of tax					326		326
Total comprehensive income							(65,693)
Employee stock purchase and option plans	23,132	2	299				301
Tax benefit of stock options and restricted stock			(19)				(19)
Repurchases of common stock	(15,618)		(377)				(377)
Stock-based compensation	162,117		3,634				3,634
Cumulative effect of adoption of FSP APB 14-1			23,860				23,860
Cumulative effect of adoption of FIN 48						(2,736)	(2,736)
Balance, December 31, 2007 as Restated (See Note 2)	15,083,520	151	90,383		(557)	38,408	128,385
Comprehensive income:							
Net income, as restated (See Note 2)						7,534	7,534
Net unrealized losses on interest rate swaps, net of tax					(718)		(718)

Edgar Filing: TREX CO INC - Form 10-K/A

Net derivative losses reclassified to earnings, net of tax					183		183
<b>Total comprehensive income</b>							<b>6,999</b>
Employee stock purchase and option plans	27,298		229				229
Repurchases of common stock	(9,816)	2	(77)				(75)
Stock-based compensation	219,610		2,290				2,290
<b>Balance, December 31, 2008 as Restated (See Note 2)</b>	<b>15,320,612</b>	<b>\$ 153</b>	<b>\$ 92,825</b>	<b>\$</b>	<b>\$ (1,092)</b>	<b>\$ 45,942</b>	<b>\$ 137,828</b>

See accompanying notes to financial statements.

**Table of Contents****TREX COMPANY, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS**

	Year Ended December 31,		
	2006	2007 As Restated (See Note 2) (in thousands)	2008 As Restated (See Note 2)
<b>Operating Activities</b>			
Net income (loss)	\$ 2,343	\$ (65,414)	\$ 7,534
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Depreciation and amortization	20,262	22,491	25,876
Debt discount amortization		2,508	5,730
Deferred income taxes	466	(24,400)	(155)
Derivatives		160	667
Stock-based compensation	2,134	3,634	2,290
Equity method losses (income)	(119)	(363)	40
Other non-cash expense (income)	(225)		
Loss (gain) on disposal of property, plant and equipment	(1)	6,126	500
Changes in operating assets and liabilities:			
Accounts receivable	(5,776)	11,552	(6,967)
Inventories	(54,503)	18,865	23,172
Prepaid expenses and other assets	549	317	(2,665)
Accounts payable	24,667	(20,472)	(4,349)
Accrued expenses	4,445	39,729	(18,453)
Income taxes receivable	1,720	4,104	(178)
Net cash provided by (used in) operating activities	(4,038)	(1,163)	33,042
<b>Investing Activities</b>			
Expenditures for property, plant and equipment	(27,702)	(24,035)	(7,814)
Proceeds from sales of property, plant and equipment			45
Notes receivable, net			(825)
Investment in Denplax	(41)		
Net cash used in investing activities	(27,743)	(24,035)	(8,594)
<b>Financing Activities</b>			
Financing costs		(3,603)	(286)
Proceeds from sales of convertible notes		97,500	
Principal payments under mortgages and notes	(9,031)	(25,077)	(1,194)
Borrowings under line of credit	107,663	86,120	44,178
Principal payments under line of credit	(67,601)	(130,252)	(44,178)
Repurchases of common stock	(435)	(377)	(74)
Proceeds from employee stock purchase and option plans	411	300	229
Excess tax effect from stock-based compensation	51	(19)	
Net cash provided by (used in) financing activities	31,058	24,592	(1,325)
Net increase (decrease) in cash and cash equivalents	(723)	(606)	23,123
Cash and cash equivalents at beginning of year	1,395	672	66

Edgar Filing: TREX CO INC - Form 10-K/A

Cash and cash equivalents at end of year	\$ 672	\$ 66	\$ 23,189
<b>Supplemental disclosures of cash flow information:</b>			
Cash paid for interest, net of capitalized interest	\$ 2,963	\$ 5,059	\$ 7,820
Cash paid (received) for income taxes, net	\$ (961)	\$ (5,056)	\$ 93

See accompanying notes to financial statements.

**Table of Contents****TREX COMPANY, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****1. BUSINESS AND ORGANIZATION**

Trex Company, Inc. (together with its subsidiaries, the Company), a Delaware corporation, was incorporated on September 4, 1998. The Company manufactures and distributes wood/plastic composite products primarily for residential and commercial decking and railing applications. Trex Wood-Polymer® lumber (Trex) is manufactured in a proprietary process that combines waste wood fibers and reclaimed polyethylene (PE material). The Company operates in one business segment.

**2. RESTATEMENT**

The Company has restated its consolidated balance sheets as of December 31, 2007 and 2008, and its consolidated statements of operations, stockholders' equity, and cash flows for the years then ended. On July 26, 2009, the Audit Committee of the Company's Board of Directors concluded, based upon the recommendation of the Company's management, that the Company should restate these financial statements, including the financial statements for affected interim periods in 2007 and 2008, to correct an error in the calculation of the valuation allowance related to its deferred tax assets.

In determining the valuation allowance, the Company considered as a source of future taxable income existing taxable temporary differences related to indefinite-lived intangible assets. Because the timing of reversal of these deferred tax liabilities is unknown, they are not a reliable source of recovery of deferred tax assets. The result of this error is that the valuation allowance for deferred tax assets is understated at December 31, 2007 and each subsequent financial reporting date through December 31, 2008. As a result of the foregoing, the Company understated reported net loss in 2007 by approximately \$1.6 million and overstated net income in 2008 by approximately \$0.3 million.

In May 2008, the Financial Accounting Standards Board issued Staff Position No. APB 14-1, *Accounting for Convertible Debt Instruments that May be Settled in Cash Upon Conversion* (FSP APB 14-1). FSP APB 14-1 requires the proceeds from the issuance of convertible debt instruments that may be settled in cash upon conversion to be allocated between a liability component and an equity component. The resulting debt discount is amortized over the period the convertible debt is expected to be outstanding as non-cash interest expense. The Company adopted FSP APB 14-1, which requires retrospective presentation, effective January 1, 2009. The accompanying restated consolidated financial statements also have been adjusted for the retrospective adoption of FSP APB 14-1. The adoption of FSP APB 14-1 resulted in a decrease to 2007 reported net loss of \$12.1 million and a decrease to 2008 reported net income of \$5.7 million. See Note 3 for additional disclosures related to FSP APB 14-1.

The following tables summarize the effects of the restatement adjustments to correct the income tax accounting error and the adjustments to retrospectively adopt FSP APB 14-1 on the Company's consolidated balance sheets as of December 31, 2007 and 2008 and consolidated statements of operations and consolidated statements of cash flows for the years ended December 31, 2007 and 2008.

**CONSOLIDATED BALANCE SHEET****December 31, 2007****(In thousands)**

	As Previously Reported	(a)	(b)	As Restated
Deferred income taxes - asset	\$ 16,007	\$ (507)	\$ (7,690)	\$ 7,810
Total current assets	120,223	(507)	(7,690)	112,026
Total Assets	328,726	(507)	(7,690)	320,529
Deferred income taxes - liability	15,763	1,105	(7,690)	9,178
Long-term debt	131,730		(35,970)	95,760
Total Liabilities	234,699	1,105	(43,660)	192,144
Additional paid-in capital	66,523		23,860	90,383

Edgar Filing: TREX CO INC - Form 10-K/A

Retained earnings	27,910	(1,612)	12,110	38,408
Total Stockholders' Equity	94,027	(1,612)	35,970	128,385
Total Liabilities and Stockholders' Equity	\$ 328,726	\$ (507)	\$ (7,690)	\$ 320,529



**Table of Contents****CONSOLIDATED BALANCE SHEET****December 31, 2008****(In thousands)**

	As Previously Reported	(a)	(b)	As Restated
Deferred income taxes - asset	\$ 15,578	\$ (397)	\$ (13,040)	\$ 2,141
Total current assets	129,791	(397)	(13,040)	116,354
Total Assets	320,521	(397)	(13,040)	307,084
Deferred income taxes - liability	15,068	1,503	(13,040)	3,531
Long-term debt	130,441		(30,240)	100,201
Total Liabilities	211,033	1,503	(43,280)	169,256
Additional paid-in capital	68,965		23,860	92,825
Retained earnings	41,462	(1,900)	6,380	45,942
Total Stockholders' Equity	109,488	(1,900)	30,240	137,828
Total Liabilities and Stockholders' Equity	\$ 320,521	\$ (397)	\$ (13,040)	\$ 307,084

**CONSOLIDATED STATEMENT OF OPERATIONS****For the year ended December 31, 2007****(in thousands, except per share data)**

	As Previously Reported	(a)	(b)	As Restated
Interest expense, net	\$ 8,995	\$	\$ 2,508	\$ 11,503
Income (loss) before provision for income taxes	(89,011)		(2,508)	(91,519)
Provision (benefit) for income taxes	(13,099)	1,612	(14,618)	(26,105)
Net income (loss)	(75,912)	(1,612)	12,110	(65,414)
Basic earnings (loss) per share	(5.10)	(0.10)	0.81	(4.39)
Diluted earnings (loss) per share	\$ (5.10)	\$ (0.10)	\$ 0.81	\$ (4.39)

**CONSOLIDATED STATEMENT OF OPERATIONS****For the year ended December 31, 2008****(in thousands, except per share data)**

	As Previously Reported	(a)	(b)	As Restated
Cost of sales	\$ 237,808	\$ 2,362	\$	\$ 240,170
Gross profit	91,386	(2,362)		89,024
Selling, general and administrative expenses	69,320	(2,362)		66,958
Interest expense, net	9,552		5,730	15,282
Income before provision for income taxes	12,514		(5,730)	6,784
Provision (benefit) for income taxes	(1,038)	288		(750)
Net income	13,552	(288)	(5,730)	7,534
Basic earnings (loss) per share	0.91	(0.02)	(0.39)	0.50
Diluted earnings (loss) per share	\$ 0.90	\$ (0.01)	\$ (0.39)	\$ 0.50



**Table of Contents****CONSOLIDATED STATEMENT OF CASH FLOWS****For the year ended December 31, 2007****(in thousands, except per share data)**

	As Previously Reported	(a)	(b)	As Restated
Operating activities				
Net income (loss)	\$ (75,912)	\$ (1,612)	\$ 12,110	\$ (65,414)
Adjustments to reconcile net income to net cash provided by operating activities:				
Debt discount amortization			2,508	2,508
Deferred income taxes	\$ (11,394)	\$ 1,612	\$ (14,618)	\$ (24,400)

**CONSOLIDATED STATEMENT OF CASH FLOWS****For the year ended December 31, 2008****(in thousands, except per share data)**

	As Previously Reported	(a)	(b)	As Restated
Operating activities				
Net income (loss)	\$ 13,552	\$ (288)	\$ (5,730)	\$ 7,534
Adjustments to reconcile net income to net cash provided by operating activities:				
Debt discount amortization			5,730	5,730
Deferred income taxes	\$ (443)	\$ 288	\$	\$ (155)

(a) Adjustments to correct accounting for income tax error and certain immaterial reclassification adjustments in 2008.

(b) Adjustments due to the retrospective adoption of FSP APB 14-1.

See Note 16 for the restatement of quarterly financial information for the years ended December 31, 2007 and 2008.

**3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES****Basis of Accounting**

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States and include the accounts of the Company and its wholly-owned subsidiaries, Winchester Capital, Inc., and Trex Wood-Polymer Espana, S.L. ( TWPE ). Intercompany accounts and transactions have been eliminated in consolidation.

TWPE was formed to hold the Company's 35% equity interest in Denplax, S.A. ( Denplax ), a joint venture with a Spanish Company responsible for public environmental programs in southern Spain and with an Italian equipment manufacturer. The joint venture was formed to recycle polyethylene at a facility in El Ejido, Spain. The Company's investment in Denplax is accounted for using the equity method.

**Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and the accompanying notes. Actual results could differ from those estimates.

**Cash and Cash Equivalents**

Cash equivalents consist of highly liquid investments purchased with original maturities of three months or less.

## **Table of Contents**

### **Concentrations and Credit Risk**

The Company's financial instruments that are exposed to concentrations of credit risk consist primarily of cash and cash equivalents, trade accounts receivable and interest rate swap contracts. The Company from time to time may have bank deposits in excess of insurance limits of the Federal Deposit Insurance Corporation. As of December 31, 2008, substantially all deposits are maintained in one financial institution. The Company has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk related to its cash and cash equivalents.

The Company routinely assesses the financial strength of its customers and, as a consequence, believes that its trade receivables credit risk exposure is limited. Trade receivables are carried at the original invoice amount less an estimate made for doubtful accounts. A valuation allowance is provided for known and anticipated credit losses and disputed amounts, as determined by management in the course of regularly evaluating individual customer receivables. This evaluation takes into consideration a customer's financial condition and credit history, as well as current economic conditions.

The Company recorded a decrease to the allowance for doubtful accounts of \$0.7 million in the year ended December 31, 2008 as a result of the collection of amounts previously deemed uncollectible. In the years ended December 31, 2006, 2007 and 2008, sales from certain customers accounted for 10% or more of the Company's total gross sales. For the year ended December 31, 2006, the Company's four largest customers represented 24%, 16%, 15% and 11%, respectively, of the Company's gross sales. For the year ended December 31, 2007, the Company's three largest customers represented 25%, 13% and 11%, respectively, of the Company's gross sales. For the year ended December 31, 2008, the Company's two largest customers represented 26% and 11%, respectively, of the Company's gross sales. As of December 31, 2007, two customers represented 18% and 17%, respectively, of the Company's accounts receivable balance. As of December 31, 2008, three customers represented 26%, 16% and 15%, respectively, of the Company's accounts receivable balance.

Approximately 28%, 32% and 23% of the Company's raw materials purchases for the years ended December 31, 2006, 2007 and 2008, respectively, were purchased from its four largest suppliers.

The Company is also exposed to credit loss in the event of nonperformance by the counter-parties to its interest rate swap agreements, but the Company does not anticipate nonperformance by the counter-parties. The amount of such exposure is limited to the unrealized gains, if any, under such agreements. At December 31, 2008, the Company had no unrealized gains on its interest rate swaps.

### **Inventories**

Inventories are stated at the lower of cost (last-in, first-out, or LIFO method) or market value.

### **Property, Plant and Equipment**

Property, plant and equipment are stated at historical cost. The costs of additions and improvements are capitalized, while maintenance and repairs are expensed as incurred. Depreciation is provided using the straight-line method over the following estimated useful lives:

Buildings	40 years
Machinery and equipment	5-11 years
Furniture and equipment	10 years
Forklifts and tractors	5 years
Computer equipment and software	3-5 years

Leasehold improvements are amortized over the shorter of the lease term or the estimated useful life of the asset.

### **Long-Lived Assets**

In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, the Company reviews its long-lived assets, including property, plant and equipment, whenever events or changes in circumstances indicate that the carrying amount of the assets may not be fully recoverable. To determine the recoverability of its long-lived assets, the Company evaluates the probability that future estimated undiscounted net cash flows will be less than the carrying amount of the long-lived assets. If the estimated cash flows are less than the carrying amount of the long-lived assets, the assets are written down to their fair value. The Company's estimates of anticipated cash flows and the

## Edgar Filing: TREX CO INC - Form 10-K/A

remaining estimated useful lives of long-lived assets could be reduced in the future. As a result, the carrying amount of long-lived assets could be reduced in the future.

Of the Company's \$176.3 million of net property, plant and equipment at December 31, 2008, approximately \$42.7 million is located at the Olive Branch, Mississippi manufacturing facility. The Company suspended manufacturing operations at the Olive Branch facility in the third quarter of 2007 for an indeterminate period. Management believes that as general macroeconomic

---

## **Table of Contents**

conditions improve and demand for the Company's products continues to increase the Company will need to resume operations at the Olive Branch facility. Changes in the plans regarding the future operation of the facility or the expected cash flows generated by the facility in the future may result in material impairment charges and reduced earnings.

### **Contract Termination Costs**

In anticipation of relocating the Company's corporate headquarters, the Company entered into a lease agreement in 2005. The Company reconsidered and decided not to move its headquarters. The lease, which began on January 1, 2006 and extends through June 30, 2019, currently obligates the Company to lease 55,047 square feet and increases to 80,071 square feet in 2012. As of January 10, 2008, the Company had executed subleases for the entire 55,047 square feet it currently leases. The terms of the existing subleases extend through years 2012 to 2015. The Company estimates that the present value of the estimated future sublease rental receipts, net of transaction costs, will be less than the Company's remaining minimum lease payment obligations under its lease for the office space. Accordingly, the Company accounts for the costs associated with the lease as contract termination costs in accordance with SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities*.

To estimate future sublease receipts for the periods beyond the term of the existing subleases and for the additional space the Company is obligated to lease, the Company has assumed that the existing subleases will be renewed or new subleases will be executed at rates consistent with rental rates in the current subleases. However, management cannot be certain that the timing of future subleases or the rental rates contained in future subleases will not differ from current estimates. Factors such as the delivery of a significant amount of new office space or poor economic conditions could have a negative effect on vacancy rates and rental rates in the area. The inability to sublet the office space in the future or unfavorable changes to key management assumptions used in the estimate of the future sublease receipts may result in additional charges to selling, general and administrative expenses in future periods.

### **Goodwill**

Goodwill represents the excess of cost over net assets acquired resulting from the Company's purchase of the Mobil Composite Products Division in 1996. Each year, in accordance with Statement of Financial Accounting Standards (SFAS) No. 142, *Goodwill and Other Intangible Assets*, the Company conducts an impairment test. For the years ended December 31, 2007 and 2008, the Company completed its annual impairment test of goodwill and noted no impairment. The Company performs the annual impairment testing of its goodwill as of October 31 of each year.

### **Product Warranty**

The Company warrants that its products will be free from material defects in workmanship and material and will not check, split, splinter, rot or suffer structural damage from termites or fungal decay. If there is such a defect in any of its products, the Company has an obligation either to replace the defective product or refund the purchase price. The Company establishes warranty reserves to provide for estimated future expenses as a result of product defects that result in claims. Reserve estimates are based on management's judgment, considering such factors as historical experience and other available information. Management reviews and adjusts these estimates, if necessary, on a quarterly basis based on the differences between actual experience and historical estimates.

During the three months ended September 30, 2007, the Company experienced a significant increase in the number of customer claims related to Trex product that exhibited surface defects and which the Company has determined was produced at the Nevada manufacturing facility beginning in 2003. Following a detailed analysis of the additional claims data, production samples, operating data and the incubation period after deck installation and other factors, the Company believes that only a small percentage of the product manufactured from 2003 to mid-2006 at the Nevada plant was affected, and that products manufactured at its other facilities are not affected. The Company believes that changes made to its manufacturing process and quality control procedures have prevented any additional product with this type of defect from reaching the market after mid-2006.

Based on the available data, the Company revised its estimate of expected future product replacement and consumer relations expenses related to the defect and increased its warranty reserve by recording a charge to earnings of \$45.2 million in the three months ended September 30, 2007. In addition, during the three months ended December 31, 2007, the Company elected to alter its handling of future customer claims. As a result of the effect of this change on the estimated cost to settle claims, the Company recorded an additional \$1.5 million increase to its warranty reserve. During 2008, the Company continued to fund payments for product defect claims from the established reserve. Although the Company adjusts the warranty reserve accordingly by recording the best estimate of the expected costs, due to the inherent subjectivity of estimating future claims, it is possible that the ultimate settlement of the claims may exceed the amount recorded and may result in future charges against income. For additional information about product warranties, see Note 14.





---

## **Table of Contents**

### **Revenue Recognition**

The Company recognizes revenue when title is transferred to customers, which is generally upon shipment of the product to the customer. The Company does not grant contractual product return rights to its customers other than pursuant to its product warranty. The Company does not expect future product returns to be material and, consequently, does not maintain an allowance for product returns.

Pursuant to Emerging Issues Task Force ( EITF ) Issue 00-10, *Accounting for Shipping and Handling Fees and Costs*, the Company records all shipping and handling fees in sales and records all of the related costs in cost of sales. The Company offers several sales incentive programs to dealers and distributors, including rebates, pricing discounts, extended terms and cooperative advertising, many of which result in cash consideration made to dealers and distributors. The Company accounts for consideration made pursuant to these programs in accordance with EITF Issue 01-09, *Accounting for Consideration Given by a Vendor to a Customer (Including a Reseller of the Vendor's Products)*. With the exception of cooperative advertising, the Company classifies sales incentives as a reduction in revenue in Net sales. Sales incentives are recorded in the period in which they are earned by customers. The Company's cooperative advertising program meets the requirements of EITF Issue 01-09, paragraph 9 for exclusion from net sales and the costs are recorded as expenses in Selling, general and administrative expenses in the accompanying consolidated statements of operations. Cooperative advertising costs are accrued as incurred.

### **Stock-Based Compensation**

The Company accounts for share-based compensation in accordance with FAS 123(R), *Share-Based Payment*, using the modified prospective transition method. Under the fair value recognition provisions of FAS 123(R), share-based compensation cost is measured at the grant date of the share-based awards based on their fair values, and is recognized on a straight line basis as expense in the accompanying consolidated statements of operations over the vesting periods of the awards, net of an estimated forfeiture rate. In accordance with the modified prospective transition method, share-based compensation expense recognized by the Company beginning January 1, 2006 includes: (a) compensation expense for all share-based payments granted on or after January 1, 2006, based on the grant date fair value estimated in accordance with the provisions of FAS 123(R), and (b) compensation expense for all share-based payments granted prior to, but that were unvested as of, January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS No. 123, *Accounting for Stock-Based Compensation*. Results for prior periods have not been restated. The Company previously recorded share-based compensation expenses in accordance with the provisions of Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* ( APB 25 ), and recorded share-based compensation expense based on the intrinsic value of the share-based award at the date of grant.

Under the provisions of FAS 123(R), the grant date fair value of share-based awards is calculated using the Black-Scholes valuation model for grants subsequent to the adoption of FAS 123(R). Determining the fair value of share-based awards is judgmental in nature and involves the use of significant estimates and assumptions, including the term of the share-based awards, risk-free interest rates over the vesting period, expected dividend rates, the price volatility of shares and forfeiture rates of the awards. Prior to adopting FAS 123(R), the Company recognized forfeitures only as they occurred. The Company bases the fair value estimates on assumptions it believes to be reasonable but that are inherently uncertain. Actual future results may differ from those estimates.

As mandated by FAS 123(R), beginning in the three months ended March 31, 2006, the benefits of tax deductions in excess of recognized compensation expense are reported as a financing cash inflow in the accompanying consolidated statements of cash flows. Prior to the adoption of FAS 123(R), these tax benefits were reported as an operating cash flow.

### **Income Taxes**

The Company accounts for income taxes and the related accounts under SFAS No. 109, *Accounting for Income Taxes*. Deferred tax liabilities and assets are determined based on the difference between the financial statement and tax basis of assets and liabilities using enacted rates expected to be in effect during the year in which the differences reverse. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion, or all, of the deferred tax asset will not be realized. Management periodically assesses the likelihood that the Company will be able to recover its deferred tax assets and reflects any changes in estimates in the valuation allowance.

### **Research and Development Costs**

Research and development costs are expensed as incurred. For the years ended December 31, 2006, 2007 and 2008, research and development costs were \$4.2 million, \$3.9 million and \$3.5 million, respectively, and have been included in Selling, general and administrative expenses in the accompanying consolidated statements of operations.



---

## **Table of Contents**

### **Advertising Costs**

The Company expenses its branding and advertising communication costs as incurred. Significant production costs are deferred and recognized as expense in the period that the related advertisement is first used. At December 31, 2007 and December 31, 2008, \$0.8 million and \$0.1 million, respectively, were included in prepaid expenses for production costs.

For the years ended December 31, 2006, 2007 and 2008, branding expenses, including advertising expenses as described above, were \$19.2 million, \$22.5 million and \$16.9 million, respectively.

### **Fair Value of Financial Instruments**

The Company considers the recorded value of its financial assets and liabilities, consisting primarily of cash and cash equivalents, accounts receivable, accounts payable, accrued expenses and other current liabilities, real estate loans, and promissory note to approximate the fair value of the respective assets and liabilities at December 31, 2007 and 2008. At December 31, 2008, the fair value of the Company's 6.00% Convertible Senior Subordinated Notes due 2012 was estimated at \$66.6 million based on quoted market prices.

### **Derivative Instruments**

The Company uses interest rate swaps to manage its exposure to fluctuations in the interest rates on its variable-rate debt and has entered into interest rate swap contracts that effectively convert a significant portion of its variable-rate debt to fixed-rate obligations. The Company accounts for the interest rate swaps as derivative instruments in accordance with SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended. SFAS No. 133 requires derivative instruments to be measured at fair value in the consolidated balance sheets. Changes in the fair value of the derivative instruments not designated as cash flow hedges or the ineffective portion of derivative instruments designated as cash flow hedges are recorded as a gain or loss in income in the current period. Changes in the fair value of a derivative instrument that qualifies and has been designated as a cash flow hedge of a forecasted transaction are initially recorded, net of tax, in Accumulated other comprehensive loss in the accompanying consolidated balance sheets and are subsequently reclassified to Interest expense, net when the forecasted transaction occurs. If a forecasted transaction is no longer probable, the deferred gain or loss in Accumulated other comprehensive loss in the accompanying consolidated balance sheets is immediately reclassified to income. Gains or losses related to any ineffective portion of cash flow hedges are recognized in income immediately.

### **Comprehensive Income (Loss)**

Comprehensive income (loss) consists of net income (loss) and net unrealized gains and losses on interest rate swap contracts. For the years ended December 31, 2006, 2007 and 2008, comprehensive income (loss) was \$2.5 million, (\$65.7) million and \$7.0 million, respectively.

### **Reclassifications**

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

### **Investment in Denplax**

During 2000, the Company formed a joint venture, Denplax, with a Spanish environmental company and an Italian equipment manufacturer to operate a plant in Spain designed to recycle waste polyethylene. Denplax qualifies as a variable interest entity under FASB Interpretation No. 46, *Consolidation of Variable Interest Entities, an Interpretation of Accounting Research Bulletin No. 51* (FIN 46). The Company adopted FIN 46 during the first quarter of 2004, which did not have a material impact on the Company's financial position or results of operations. Denplax was financed with initial equity contributions from the Company and the other partners and debt financing. The Company is not contingently liable for any of Denplax's obligations. The Company does not control Denplax and records its proportional 35% share of Denplax's operating results using the equity method. The Company expects to purchase up to approximately 8,000 metric tons of the Denplax plant's production next year, if the production meets certain material specifications. In the years ended December 31, 2006, 2007 and 2008, the Company purchased 16,552 metric tons for approximately \$4.2 million, 11,900 metric tons for approximately \$3.3 million, and approximately 10,300 metric tons for approximately \$3.6 million, respectively, excluding freight costs. In each such year, the Company's purchases accounted for substantially all of the Denplax plant's production. The carrying amount of the Company's investment in Denplax at December 31, 2008 was approximately \$1.5 million. In addition, the Company had outstanding loans due from Denplax totaling approximately \$2.0 million and \$1.9 million at December 31, 2007 and 2008, respectively.

### **New Accounting Standards**

## Edgar Filing: TREX CO INC - Form 10-K/A

In September 2006, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Standards ( SFAS ) No. 157, *Fair Value Measurements*, which defines fair value, establishes a framework for measuring fair value in accordance with

**Table of Contents**

generally accepted accounting principles and expands disclosures about fair value measurements. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007. In February 2008, the FASB issued Staff Position (FSP) No. 157-2 which delays the effective date of SFAS 157 one year for all nonfinancial assets and nonfinancial liabilities, except those recognized or disclosed at fair value in the financial statements on a recurring basis. The Company adopted this standard effective January 1, 2008 with no impact on its results of operations and financial position. See Note 7 to the accompanying condensed consolidated financial statements for additional disclosure.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Liabilities*. SFAS No. 159 permits entities to choose to elect to measure eligible financial instruments at fair value, which provides entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without being required to apply complex hedge accounting provisions. SFAS No. 159 applies to fiscal years beginning after November 15, 2007. The Company did not elect to measure any additional assets or liabilities at fair value that are not already measured at fair value under existing standards. Therefore, the adoption of this standard had no impact on the Company's results of operations and financial position.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities - an amendment of FASB Statement No. 133*. SFAS No. 161 requires enhanced disclosure related to derivatives and hedging activities and thereby seeks to improve the transparency of financial reporting. Under SFAS No. 161, entities are required to provide enhanced disclosures relating to: (a) how and why an entity uses derivative instruments; (b) how derivative instruments and related hedge items are accounted for under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, and its related interpretations; and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. SFAS No. 161 must be applied prospectively to all derivative instruments and non-derivative instruments that are designated and qualify as hedging instruments and related hedged items accounted for under SFAS No. 133 for all financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with earlier application encouraged. The Company is evaluating the effect of the adoption of SFAS No. 161, but we do not expect the adoption of this standard to have a material impact on its results of operations or financial position.

In May 2008, the FASB issued FSP APB 14-1, *Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)*. FSP APB 14-1 requires the proceeds from the issuance of convertible debt instruments that may be settled in cash upon conversion to be allocated between a liability component and an equity component. The resulting debt discount will be amortized over the period the convertible debt is expected to be outstanding as non-cash interest expense. The Company adopted FSP APB 14-1 effective January 1, 2009, which was applied retrospectively to prior periods. The Company has outstanding convertible debt instruments issued in June 2007 that are affected by FSP APB 14-1. Upon the original issuance of convertible debt in 2007, the Company recorded the net debt obligation as long-term debt in accordance with applicable accounting standards at that time. To adopt FSP APB 14-1, the Company estimated the fair value, as of the date of issuance, of the convertible debt instruments as if the instruments were issued without the conversion options. The difference between the fair value and the principal amounts of the instruments was \$38.5 million. This amount was retrospectively applied to the Company's financial statements from the issuance date of the debt instruments in 2007, and was retrospectively recorded as a debt discount and as a component of equity. The discount is being amortized over the expected five-year life of the notes resulting in non-cash increase to interest expense in historical and future periods.

The retrospective adoption of FSP APB 14-1 resulted in a \$5.7 million and a \$2.5 million increase to interest expense for the years ended December 31, 2008 and 2007, respectively. Refer to Note 2 for further detail as to the impact of the adoption of FSP APB 14-1 on financial statement amounts.

The following table provides additional information regarding the Company's convertible debt instruments that are subject to FSP APB 14-1 (in thousands, except conversion price):

	December 31, 2007	December 31, 2008
Principal amount of the liability component	\$ 97,500	\$ 97,500
Unamortized discount of liability component	(35,970)	(30,240)
Net carrying amount of liability component	61,530	67,260
Carrying amount of the equity component	23,860	23,860
Remaining amortization period of discount	54 months	42 months
Conversion price	\$ 21.78	\$ 21.78
Effective interest rate on liability component	18.41%	18.41%
Interest expense at coupon rate (6.0%)	\$ 2,925	\$ 5,850

Edgar Filing: TREX CO INC - Form 10-K/A

Additional non-cash interest in accordance with FSP APB 14-1	\$	2,508	\$	5,730
--	----	-------	----	-------

**Table of Contents****4. INVENTORIES**

Inventories (at LIFO value) consist of the following as of December 31 (in thousands):

	2007	2008
Finished goods	\$ 72,916	\$ 48,751
Raw materials	19,653	20,646
<b>Total inventories</b>	<b>\$ 92,569</b>	<b>\$ 69,397</b>

Inventory is stated at the lower of standard cost or net realizable value. The Company periodically reviews its inventory for slow moving or obsolete items and writes down the related products to estimated net realizable value.

During the year ended December 31, 2008, due to the liquidation of certain inventories, a portion of the Company's cost of sales is based on prior year costs rather than current year costs. As a result, the Company recognized a benefit of \$4.2 million.

At December 31, 2007 and 2008, the excess of the replacement cost of inventory over the LIFO value of inventory was approximately \$28.3 million and \$30.3 million, respectively.

**5. PROPERTY, PLANT AND EQUIPMENT**

Property, plant and equipment consist of the following as of December 31 (in thousands):

	2007	2008
Building and improvements	\$ 55,530	\$ 56,214
Machinery and equipment	219,849	223,393
Furniture and equipment	2,533	2,528
Forklifts and tractors	3,920	4,514
Computer equipment	10,212	11,408
Construction in process	3,259	2,608
Land	8,857	8,857
	304,160	309,522
Accumulated depreciation	(110,216)	(133,186)
<b>Total property, plant and equipment, net</b>	<b>\$ 193,944</b>	<b>\$ 176,336</b>

The Company had construction in process as of December 31, 2008 of approximately \$2.6 million. The Company expects that the construction in process will be completed and put into service in the year ending December 31, 2009.

Depreciation expense for the years ended December 31, 2006, 2007 and 2008 totaled \$20.3 million, \$22.5 million and \$24.9 million, respectively.

In connection with the installation of new equipment to improve the Company's manufacturing process and the repurposing of certain assets, the Company disposed of certain equipment that resulted in a \$0.5 million loss recorded in Selling, general and administrative expenses in the accompanying consolidated statements of operations for the year ended December 31, 2008.

**6. ACCRUED EXPENSES**

Accrued expenses consist of the following (in thousands):

Edgar Filing: TREX CO INC - Form 10-K/A

	2007	2008
Accrued compensation and benefits	\$ 5,157	\$ 9,996
Accrued interest	4,637	4,734
Accrued rent obligations	1,996	2,268
Accrued sales and marketing costs	3,615	2,023
Accrued taxes and penalties	837	1,144
Accrued manufacturing expenses	1,088	607
Accrued freight	461	386
Accrued customer relations costs	1,844	345
Accrued professional and legal costs	564	258
Other	1,384	478
<b>Total accrued expenses</b>	<b>\$ 21,583</b>	<b>\$ 22,239</b>



---

## **Table of Contents**

### **7. DEBT**

*Indebtedness.* At December 31, 2008, the Company's indebtedness, including the fair value of its interest rate swaps, totaled \$133.8 million and the annualized overall weighted average interest rate of such indebtedness, including the effect of the Company's interest rate swaps, was approximately 5.57%.

*Convertible Notes Offering.* On June 18, 2007, the Company issued \$85.0 million principal amount of its 6.00% Convertible Senior Subordinated Notes due 2012 (the "Notes") through an underwritten public offering. The Company used a portion of net proceeds of \$82.1 million from the sale of the Notes to repay in full \$24.0 million principal amount of its 8.32% senior secured notes due July 19, 2009 and \$45.7 million principal amount of borrowings outstanding under its revolving credit facility. The Company paid a prepayment penalty of \$0.6 million in connection with the retirement of the senior secured notes. On July 12, 2007, the underwriters of the Notes offering exercised their over-allotment option to purchase an additional \$12.5 million principal amount of Notes. The Company received net proceeds of \$12.1 million from the sale of the additional Notes, which it issued on July 17, 2007.

Holders may convert the Notes into the Company's common stock at their option before the close of business on any business day prior to April 1, 2012 only under the following circumstances:

during any fiscal quarter of the Company commencing after September 30, 2007, if the last reported sale price of the Company's common stock for at least 20 trading days during a period of 30 consecutive trading days ending on the last trading day of the preceding fiscal quarter is greater than or equal to 130% of the applicable conversion price on each applicable trading day;

during the five business-day period after any ten consecutive trading-day period in which the trading price per Note for each day of that measurement period is less than 98% of the product of the last reported sale price of the common stock and the applicable Note conversion rate on each such day; or

upon the occurrence of specified corporate events.

On and after April 1, 2012, until the close of business on the third business day immediately preceding the maturity date, holders may convert their Notes at any time, regardless of the foregoing circumstances.

Upon conversion of any Notes, the Company will pay cash up to the principal amount of the Notes converted and deliver shares of its common stock to the extent the daily conversion value exceeds the proportionate principal amount of such Notes based on a 40 trading-day observation period. The conversion rate will be 45.9116 shares of common stock per \$1,000 principal amount of Notes, which is equivalent to a conversion price of approximately \$21.78 per share of common stock. The conversion rate will be subject to adjustment in some events. In addition, following specified corporate transactions that occur before the maturity date, the conversion rate will be increased for a holder who elects to convert the holder's Notes in connection with such a corporate transaction in certain circumstances. Shares issued as a result of the conversion of any Notes would have a dilutive effect on earnings per share.

The Company may not redeem the Notes. If the Company undergoes a fundamental change, as defined in the Notes, holders may require the Company to purchase the Notes in whole or in part for cash at a price equal to 100% of the principal amount of the Notes to be purchased, plus any accrued and unpaid interest.

The Notes are the Company's direct, senior subordinated, unsecured obligations and rank equally in right of payment with all of the Company's existing and future senior subordinated indebtedness, senior in right of payment to all of the Company's existing and future subordinated indebtedness and junior in right of payment to all of the Company's existing and future senior indebtedness.

*Revolving Credit Facility.* Amounts drawn under the revolving credit facility are subject to a borrowing base consisting of accounts receivable and finished goods inventories. At December 31, 2008, there were no borrowings outstanding under the revolving credit facility and the borrowing base totaled approximately \$63.8 million.

*Compliance With Debt Covenants.* Effective January 1, 2009, financial covenants related to the credit agreement and reimbursement agreement with BB&T and JPMorgan reset to the following so that:

## Edgar Filing: TREX CO INC - Form 10-K/A

the Company's senior debt ratio, or ratio of consolidated senior debt to consolidated EBITDA (as defined for purposes of the agreements), may not be greater than (a) 3.0 to 1 for the period commencing January 1, 2009 to and including March 31, 2009 and (b) thereafter (A) 2.5 to 1 for any measurement period ending June 30 or September 30, and (B) 3.0 to 1 for any measurement period ending December 31 or March 31;

the Company's fixed charge coverage ratio, or ratio of consolidated EBITDA to fixed charges (as defined for purposes of the agreements), may not be less than (a) 1.4 to 1 for any measurement period commencing after January 1, 2009;

The Company's ratio of total consolidated debt to total consolidated capitalization (as defined for purposes of the agreements) may not be greater than (a) 60% for the period commencing January 1, 2009 to and including March 31, 2009, and (b) thereafter (A) 50% for each period commencing April 1 of a calendar year to and including September 30 of such calendar year, and (B) 60% for each period commencing October 1 of a calendar year to and including March 31 of the immediately succeeding calendar year; and

**Table of Contents**

the Company's consolidated tangible net worth (as defined for purposes of the agreements) may not be less than the sum of (a) \$85 million, (b) 100% of the net proceeds of all stock issued after January 1, 2008, plus (c) 50% of consolidated net income after December 31, 2007 (taken as one accounting period), but excluding from such calculation of consolidated net income for purposes of (c) any quarter in which consolidated net income is negative.

The Company was in compliance with all covenants contained in its loan agreements at December 31, 2008.

*Long-Term Debt.* The Company's Notes have been reduced by debt discounts of \$30.2 million and \$36.0 million as of December 31, 2008 and 2007, respectively, in accordance with the terms of FSP APB 14-1, which is discussed in more detail in Note 3 to the Consolidated Financial Statements.

Long-term debt consists of the following as of December 31 (in thousands):

	2007	2008
Real estate loans	\$ 10,428	\$ 9,234
Convertible notes	97,500	97,500
Promissory note	25,000	25,000
Total long-term debt	132,928	131,734
Less unamortized debt discount	(35,970)	(30,240)
	96,958	101,494
Less current portion	(1,198)	(1,293)
Long-term debt, excluding current portion	\$ 95,760	\$ 100,201

Future debt maturities are as follows (in thousands):

Years ending December 31,	
2009	\$ 1,293
2010	1,405
2011	4,581
2012	98,142
2013	692
Thereafter	25,621
Total long-term debt	\$ 131,734

The Company uses interest rate swap contracts to manage its exposure to fluctuations in the interest rates on its variable-rate debt. At December 31, 2008, the fair value of the debt-related derivatives was \$2.1 million and was classified as a long-term liability in the accompanying consolidated balance sheets.

During the years ended December 31, 2006, 2007 and 2008, the Company capitalized approximately \$1.8 million, \$1.0 million and \$0.2 million of interest, respectively.

**Interest Rate Swaps**

The Company uses interest rate swaps to manage its exposure to fluctuations in the interest rates on its variable-rate debt and has entered into interest rate swap contracts that effectively convert a significant portion of its variable-rate debt to fixed-rate obligations. The Company had outstanding debt of \$131.7 million at December 31, 2008, \$97.5 million of which is fixed-rate debt. Of the remaining \$34.2 million, \$27.1 million was effectively converted to a fixed rate through the use of fixed-for-floating interest rate swaps. The remaining \$7.1 million, 5.4% of the Company's total debt outstanding at December 31, 2008, is variable-rate debt, \$2.1 million of which is LIBOR-based and \$5.0 million of which is based on auction rates and is reset weekly.

## Edgar Filing: TREX CO INC - Form 10-K/A

The Company accounts for the interest rate swaps as derivative instruments in accordance with SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended. SFAS No. 133 requires derivative instruments to be measured at fair value in the consolidated balance sheets. At December 31, 2008 the fair value of the Company's interest rate swaps was \$2.1 million and was classified as a long term liability in the accompanying consolidated balance sheets. Interest rate swap instruments representing \$1.3 million of the total \$2.1 million qualify for and were designated as cash flow hedges of forecasted transactions in accordance with SFAS No. 133 and the changes in fair value of these instruments were recorded, net of tax, in Accumulated other comprehensive loss in the accompanying consolidated balance sheets. At December 31, 2008, \$1.1 million of unrealized losses, net of tax, were recorded in Accumulated other comprehensive loss in the accompanying consolidated balance sheets. The Company

**Table of Contents**

expects approximately \$0.4 million to be reclassified into Interest expense, net over the next twelve months. Interest rate swap instruments representing the remaining \$0.8 million of the total \$2.1 million do not qualify as cash flow hedges per SFAS No. 133 and changes in the fair value of these instruments in the amount of \$0.2 million and \$0.7 million of expense were recorded in Interest expense, net in the accompanying consolidated statements of operations in the years ended December 31, 2007 and 2008, respectively.

**8. FAIR VALUE MEASUREMENT**

The Company adopted SFAS 157 on January 1, 2008, which defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles and expands disclosures about fair value measurements. The Company's adoption was limited to financial assets and liabilities, which primarily relate to derivative contracts.

SFAS 157 requires the categorization of financial assets and liabilities based upon the level of judgments associated with the inputs used to measure their fair value. Hierarchical levels, defined by SFAS 157 and directly related to the amount of subjectivity associated with the inputs used to determine the fair value of financial assets and liabilities, are as follows:

Level 1 Inputs are unadjusted, quoted prices in active markets for identical assets or liabilities at the measurement date

Level 2 Inputs (other than quoted prices included in Level 1) are either directly or indirectly observable for the assets or liability through correlation with market data at the measurement date and for the duration of the instrument's anticipated life

Level 3 Inputs reflect management's best estimate of what market participants would use in pricing the asset or liability at the measurement date. Consideration is given to the risk inherent in the valuation technique and the risk inherent in the inputs to the model.

The determination of the fair value level within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the assets or liabilities.

The following table presents the financial assets and liabilities we measure at fair value on a recurring basis, based on the fair value hierarchy as of December 31, 2008 (in thousands):

	Total Fair Value Measurement December 31, 2008	Quoted Prices in Active Markets for Identical Asset (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Debt-related derivative liability	\$ 2,069	\$	\$ 2,069	\$

The Company uses interest-rate swap contracts to manage its exposure to fluctuations in the interest rates under its variable-rate debt.

**9. STOCKHOLDERS' EQUITY**

The following table sets forth the computation of basic and diluted earnings per share (in thousands, except share and per share data):

	Year Ended December 31,	
	2007	2008
	As Restated (See Note 2)	As Restated (See Note 2)
2006		

Edgar Filing: TREX CO INC - Form 10-K/A

<b>Numerator:</b>			
Net income (loss)	\$	2,343	\$ (65,414) \$ 7,534
<b>Denominator:</b>			
Basic weighted average shares outstanding		14,829,832	14,884,174 14,956,927
<b>Effect of dilutive securities:</b>			
Stock options		21,529	38,623
Restricted stock		41,605	117,533
Diluted weighted average shares outstanding		14,892,966	14,884,174 15,113,083
Basic earnings (loss) per share	\$	0.16	\$ (4.39) \$ 0.50
Diluted earnings (loss) per share	\$	0.16	\$ (4.39) \$ 0.50

The Company has excluded 15,943 restricted shares from the calculation of diluted earnings per share for the year ended December 31, 2008 as these represent anti-dilutive stock options.

**Table of Contents****10. STOCK-BASED COMPENSATION**

Effective January 1, 2006, the Company adopted the fair value recognition provisions of SFAS No. 123(R), *Share-Based Payment*, using the modified prospective transition method. Under that transition method, compensation cost includes (a) compensation cost for all share-based payments granted prior to, but not yet vested as of, January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS No. 123; and (b) compensation cost for all share-based payments granted subsequent to January 1, 2006, based on the grant date fair value estimated in accordance with the provisions of SFAS No. 123(R).

The Company has one stock-based compensation plan, the 2005 Stock Incentive Plan (the 2005 Plan), which was amended by its shareholders on May 7, 2008. The 2005 Plan is administered by the Compensation Committee of the Company's Board of Directors. Stock-based compensation is granted to officers, directors and certain key employees in accordance with the provisions of the 2005 Plan. The 2005 Plan provides for grants of stock options, stock appreciation rights (SARs), restricted stock and performance share awards. The total aggregate number of shares of the Company's common stock that may be issued under the 2005 Plan is 3,150,000 shares. For the years ended December 31, 2006, 2007 and 2008, SFAS 123(R) compensation expense related to awards under the 2005 Plan was \$2.1 million, \$3.6 million and \$2.3 million, respectively. This expense was included in Selling, general and administrative expenses in the accompanying consolidated statements of operations.

*Stock Options and Stock Appreciation Rights*

The 2005 Plan authorizes the grant of stock options and SARs. Stock options are granted with an exercise price and SARs are granted with a grant price equal to the closing market price of the Company's common stock on the date of grant. These awards have ten-year contractual terms and vest based on the terms of the individual awards. The options and SARs are generally forfeitable upon termination of a holder's service as an employee or director. The Company recognizes compensation cost on a straight-line basis over the vesting period for the award. Prior to 2006, the Company granted stock options and all stock options outstanding at December 31, 2008 are fully vested. In 2006, the Company began the use of SARs instead of stock options.

As of December 31, 2008, there was \$2.8 million of unrecognized compensation cost related to SARs expected to be recognized over a weighted-average period of approximately 2.0 years. In the years ended December 31, 2006 and 2007, as a result of the excess tax effects of stock-based compensation, the Company reflected cash in-flows of \$51 thousand and cash out-flows of \$19 thousand, respectively, in the accompanying consolidated statements of cash flows. The fair value of each stock option award and SAR is estimated on the date of grant using a Black-Scholes option-pricing model. For SARs issued in the years ended December 31, 2007 and 2008, respectively, the assumptions shown in the following table were used:

	<b>Year Ended December 31,</b>	
	<b>2007</b>	<b>2008</b>
Dividend yield	0%	0%
Average risk-free interest rate	4.7%	2.9%
Expected term (years)	5	5
Volatility	41.4%	45.0%

*Expected Volatility.* Volatility is a measure of the amount by which a financial variable such as a share price has fluctuated (historical volatility) or is expected to fluctuate (expected volatility) during a period. The Company has used the historical volatility over the average expected term of the options granted as the expected volatility.

*Risk-Free Interest Rate.* This is the U.S. Treasury rate having a term that most closely resembles the expected term of the option.

*Expected Term.* The expected term is the period of time that the SARs granted is expected to remain unexercised. SARs granted during the year ended December 31, 2008 had a maximum term of ten years. The Company used historical exercise behavior with further consideration given to the class of employees to whom the equity awards were granted to estimate the expected term of the SAR.

The forfeiture rate is the estimated percentage of equity awards granted that are expected to be forfeited or canceled before becoming fully vested. The Company estimates forfeitures based on historical experience with further consideration given to the class of employees to whom the equity awards were granted.

Edgar Filing: TREX CO INC - Form 10-K/A

The weighted-average grant date fair value of SARs granted during the year ended December 31, 2008 was \$3.88.



**Table of Contents**

Stock option activity under the 2005 Plan and a predecessor stock incentive plan is as follows:

	Options	Weighted-Average Exercise Price Per Share	Weighted-Average Remaining Contractual Life	Aggregate Intrinsic Value as of December 31, 2008
Outstanding at December 31, 2006	587,406	\$ 35.19		
Granted		\$		
Exercised	(1,733)	\$ 22.59		
Canceled	(60,221)	\$ 36.64		
Outstanding at December 31, 2007	525,452	\$ 35.10		
Granted		\$		
Exercised		\$		
Canceled	(298,862)	\$ 37.11		
Outstanding at December 31, 2008	226,590	\$ 32.45	4.3	\$ 11,862
Vested and expected to vest at December 31, 2008	226,590	\$ 32.45	4.3	\$ 11,862
Exercisable at December 31, 2008	226,590	\$ 32.45	4.3	\$ 11,862

At December 31, 2008, the price range of options outstanding was as follows:

	Options Outstanding	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Life (Years)	Options Exercisable	Weighted-Average Exercise Price
\$ 0.00 - 19.99	18,289	\$ 17.91	2.6	18,289	\$ 17.91
20.00 - 29.99	88,372	\$ 24.68	3.4	88,372	\$ 24.68
30.00 - 39.99	72,742	\$ 36.81	4.6	72,742	\$ 36.81
40.00 and over	47,187	\$ 45.95	6.0	47,187	\$ 45.95
Total	226,590	\$ 32.45	4.3	226,590	\$ 32.45

SAR activity under the 2005 Plan is as follows:

	SARs	Weighted-Average Grant Price Per Share
Outstanding at December 31, 2006	300,360	\$ 24.21
Granted	209,665	\$ 24.42
Canceled	(37,499)	\$ 24.79
Vested and expected to vest at December 31, 2007	403,513	\$ 24.21
Exercisable at December 31, 2007	134,571	\$ 23.01
Outstanding at December 31, 2007	472,526	\$ 24.26
Granted	732,648	\$ 9.01
Canceled	(254,038)	\$ 22.23
Outstanding at December 31, 2008	951,136	\$ 13.07
Vested and expected to vest at December 31, 2008	848,014	\$ 12.31
Exercisable at December 31, 2008	219,387	\$ 19.90

*Performance Share Awards*

In the years ended December 31, 2005 and December 31, 2006, the Company granted performance share awards ( PSAs ) to certain of the Company s officers and other employees under the 2005 Plan. The PSAs consist of a right to receive shares of the Company s common stock if the Company meets specified performance criteria over a three-year performance period.

Prior to January 1, 2006, PSAs were accounted for under APB 25 by charging a portion of compensation expense during each accounting period based on the probable number of shares to be issued. Beginning January 1, 2006, all PSAs are accounted for in accordance with the provisions of SFAS 123R. The fair value of the PSAs is determined based on the closing price of the Company s shares on the date of grant. At December 31, 2008, there were 37,806 performance share awards outstanding with a weighted-average grant fair value of \$24.79 per share. As a result of Company performance, no compensation expense was recognized related to PSAs during the years ended December 31, 2006, 2007, and 2008.

**Table of Contents**

Performance share awards activity under the 2005 Plan is as follows:

	<b>Performance Share Awards</b>	<b>Weighted-Average Grant Price Per Share</b>
Nonvested at December 31, 2006	124,704	\$ 30.36
Granted	7,213	\$ 25.37
Forfeited	(25,276)	\$ 32.25
Nonvested at December 31, 2007	106,641	\$ 29.56
Granted		\$
Forfeited	(68,835)	\$ 32.19
Nonvested at December 31, 2008	37,806	\$ 24.79

*Restricted Stock*

The fair value of the restricted stock is determined based on the closing price of the Company's shares on the grant date. Shares of restricted stock vest based on the terms of the awards. In the years ended December 31, 2006, 2007 and 2008, 20,000, 188,331 and 325,202 restricted shares were granted at \$26.65, \$23.44 and \$8.59 per share, respectively. In the years ended December 31, 2006, 2007 and 2008, \$0.6 million, \$1.4 million and \$1.2 million of compensation expense, respectively, was recognized related to restricted stock awards. At December 31, 2008, there was \$4.0 million of total compensation expense related to unvested restricted stock remaining to be recognized over a weighted-average period of approximately 1.8 years. Compensation expense related to restricted stock is included in Selling, general and administrative expenses in the accompanying consolidated statements of operations.

Restricted stock activity under the 2005 Plan is as follows:

	<b>Restricted Stock</b>	<b>Weighted-Average Grant Price Per Share</b>
Nonvested at December 31, 2006	66,311	\$ 26.77
Granted	188,331	\$ 23.44
Vested	(49,767)	\$ 24.07
Forfeited	(27,738)	\$ 23.90
Nonvested at December 31, 2007	177,137	\$ 24.03
Granted	325,202	\$ 8.59
Vested	(50,439)	\$ 7.59
Forfeited	(105,592)	\$ 16.87
Nonvested at December 31, 2008	346,308	\$ 11.69

*Employee Stock Purchase Plan*

The Company has an employee stock purchase plan ( ESPP ) that permits eligible employees to purchase shares of common stock of the Company at a purchase price which is the lesser of 85% of the market price on the first day of the calendar quarter or 85% of the market price on the last day of the calendar quarter. Eligible employees may elect to participate in the plan by authorizing payroll deductions from 1% to 15% of gross compensation for each payroll period. On the last day of each quarter, each participant's contribution account is used to purchase the maximum number of whole shares of common stock determined by dividing the contribution account's balance by the purchase price. The aggregate number of shares of common stock that may be purchased under the plan is 300,000. Through December 31, 2008, employees had purchased approximately 131,926 shares under the plan. In the years ended December 31, 2006, 2007 and 2008, compensation expense of \$67.5 thousand, \$49.2 thousand and \$67.9 thousand, respectively, was recognized related to the discount on ESPP purchases. Compensation expense related to ESPP purchases is included in Selling, general and administrative expenses in the accompanying consolidated statements of operations.



**Table of Contents****11. LEASES**

The Company leases office space (also see Note 14), storage warehouses and certain office and plant equipment under various operating leases. Minimum annual payments under these non-cancelable leases as of December 31, 2008 were as follows (in thousands):

Year Ending December 31,	
2009	\$ 7,792
2010	7,540
2011	5,727
2012	5,280
2013	4,174
Thereafter	17,044
<b>Total minimum lease payments</b>	<b>\$ 47,557</b>

For the years ended December 31, 2006, 2007 and 2008, the Company recognized rental expenses of approximately \$13.7 million, \$12.2 million and \$10.1 million, respectively.

**12. EMPLOYEE BENEFIT PLANS**

Through December 31, 2007, the Company had a 401(k) Profit Sharing Plan and a Money Purchase Pension Plan for the benefit of all employees who meet certain eligibility requirements. These plans covered substantially all of the Company's full-time employees. The plan documents provide for the Company to make defined contributions as well as matching and other discretionary contributions, as determined by the Board of Directors. At December 31, 2007, the Company merged the two plans together and subsequently administers post-retirement benefits to employees through the prevailing 401(k) Profit Sharing Plan. The Company's contributions to the plans totaled \$1.7 million, \$1.8 million and \$1.3 million for the years ended December 31, 2006, 2007 and 2008.

**13. INCOME TAXES**

Income tax provision (benefit) for the years ended December 31, 2006, 2007 and 2008 consists of the following (in thousands):

	Year Ended December 31,		
	2006	2007 As Restated (See Note 2)	2008 As Restated (See Note 2)
<b>Current income tax provision (benefit):</b>			
Federal	\$	\$ (1,617)	\$ (238)
State	242	(88)	(357)
	242	(1,705)	(595)
<b>Deferred income tax provision (benefit):</b>			
Federal	803	(23,912)	(131)
State	(337)	(488)	(24)
	466	(24,400)	(155)
<b>Total income tax provision (benefit)</b>	<b>\$ 708</b>	<b>\$ (26,105)</b>	<b>\$ (750)</b>

## Edgar Filing: TREX CO INC - Form 10-K/A

The income tax provision (benefit) differs from the amount of income tax determined by applying the U.S. federal statutory rate to income before taxes as a result of the following (in thousands):

	Year Ended December 31,		
		2007	2008
	2006	As Restated (See Note 2)	As Restated (See Note 2)
U.S. federal statutory taxes	\$ 1,037	\$ (31,117)	\$ 2,307
State and local taxes, net of U.S. federal benefit	80	(2,740)	567
State tax charges (credits)	(1,129)	(637)	913
Research and development credits	(201)	(189)	(168)
Non-deductible expenses	94	125	89
Change in deferred state rate		549	
Increase (decrease) in valuation allowance	875	7,352	(4,118)
Federal credits			(234)
Other	(48)	552	(106)
 Total income tax provision (benefit)	 \$ 708	 \$ (26,105)	 \$ (750)

**Table of Contents**

Deferred tax assets and liabilities as of December 31, 2007 and 2008 consist of the following (in thousands):

	As of December 31,	
	2007	2008
	As Restated (See Note 2)	As Restated (See Note 2)
<b>Deferred tax assets:</b>		
Net operating losses	\$ 13,526	\$ 21,527
Warranty reserve	15,190	8,389
Stock-based compensation	1,795	2,203
Accruals not currently deductible and other	5,526	5,382
Inventories	2,452	1,853
State tax credit carryforwards	4,337	3,424
Gross deferred tax assets, before valuation allowance	42,826	42,778
Valuation allowance	(9,581)	(5,596)
Gross deferred tax assets, after valuation allowance	33,245	37,182
<b>Deferred tax liabilities:</b>		
Inventories		(2,783)
Debt discount	(13,665)	(11,466)
Depreciation and other	(20,948)	(24,323)
Gross deferred tax liabilities	(34,613)	(38,572)
Net deferred tax asset (liability)	\$ (1,368)	\$ (1,390)

The valuation allowance as of December 31, 2008 of \$5.6 million is primarily attributable to the uncertainty related to the realizability of the Company's excess deferred tax assets. The Company has considered all available evidence, both positive and negative, in determining the need for a valuation allowance. Based upon this analysis, including a consideration of the Company's cumulative loss history in the three-year period ended December 31, 2008, management determined that it is not more likely than not that its excess deferred tax assets will be realized. The Company's future realization of its excess deferred tax assets ultimately depends on the existence of sufficient taxable income in the carry-forward periods under the tax laws. The Company will analyze its position in subsequent reporting periods, considering all available positive and negative evidence, in determining the expected realization of its excess deferred tax assets.

The Company has federal net operating losses of \$60.5 million at December 31, 2008 which expire starting 2028.

The Company adopted FIN 48 on January 1, 2007. As a result of the implementation of FIN 48, the Company recognized a charge of \$2.7 million to the January 1, 2007 Retained earnings balance in the accompanying consolidated balance sheets. A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows (in thousands):

	Year Ended December 31,	
	2007	2008
Unrecognized tax benefits balance at January 1	\$ 2,929	\$ 3,620
Gross increases related to prior year tax positions	1,479	
Gross decreases related to prior year tax positions	(545)	
Gross increases related to current year tax positions		34
Settlements		(63)
Lapse of statute of limitations	(243)	(521)

## Edgar Filing: TREX CO INC - Form 10-K/A

Unrecognized tax benefits balance at December 31	\$ 3,620	\$ 3,070
--	----------	----------

The total liabilities associated with unrecognized tax benefits that, if recognized, would affect the effective tax rates were \$2.5 million and \$2.5 million at December 31, 2007 and December 31, 2008, respectively.

The Company recognizes interest and penalties related to tax matters as a component of Selling, general and administrative expenses in the accompanying consolidated statements of operations. As of December 31, 2007 and December 31, 2008, the Company had accrued interest related to uncertain tax positions of \$1.4 million and \$1.7 million, respectively, and accrued penalties related to uncertain tax positions of \$0.8 million and \$0.7 million, respectively, in the accompanying consolidated balance sheets.



---

## **Table of Contents**

The Company operates in multiple tax jurisdictions and, in the normal course of business, its tax returns are subject to examination by various taxing authorities. Such examinations may result in future assessments by these taxing authorities and the Company has accrued a liability when it believes that it is not more likely than not that it will realize the benefits of tax positions that it has taken or for the amount of any tax benefit that exceeds the cumulative probability threshold in accordance with FIN 48. The Company believes that adequate provisions have been made for all tax returns subject to examination. As of December 31, 2008, tax years 2004 through 2008 remain subject to examination by federal and certain state tax jurisdictions.

The Company has taken tax positions in certain taxing jurisdictions for which it is reasonably possible that the total amounts of unrecognized tax benefits may decrease within the year ending December 31, 2009. The possible decrease could result from the closing of the statutes for federal tax purposes in some taxing jurisdictions and would be approximately \$0.4 million.

## **14. COMMITMENTS AND CONTINGENCIES**

### **Legal Matters**

On October 16, 2006, Ron Nystrom commenced a lawsuit against the Company in the United States District Court for the Eastern District of Virginia, Norfolk Division, which also named Home Depot, Inc. and Snavely Forest Products, Inc. as defendants. Mr. Nystrom alleges that the Company's Accen<sup>®</sup> product and other new products introduced after the commencement of a prior patent infringement action infringe his patent. Mr. Nystrom also alleges that the Company's Contour<sup>®</sup> product infringes a second patent owned by him and that the Company is engaged in contributory infringement by recommending third party hidden fastening systems that infringe such patent. In January 2008, Mr. Nystrom added an additional allegation that the Company's Trex Hideaway hidden fastening system also infringes such patent. On May 16, 2008, the District Court granted summary judgment to the Company with respect to Mr. Nystrom's claims on the first patent. On April 29, 2008, the District Court issued an order severing all claims associated with the second patent and consolidating them into a separate case. The Company believes that all of Mr. Nystrom's claims are without merit, and, in addition, are barred by a prior judgment and patent claim construction.

On September 25, 2008, the Company commenced a lawsuit against Mr. Nystrom in Virginia Circuit Court for various causes of action, including defamation. On September 26, 2008, Mr. Nystrom filed a Notice of Appeal to the United States Court of Appeals for the Federal Circuit appealing the District Court's grant of summary judgment to the Company with respect to Mr. Nystrom's claims on the first patent. On October 16, 2008, the Company and Mr. Nystrom signed a Dismissal and Tolling Agreement which provided that the Federal District Court action relating to the second patent and the Company's action in Virginia Circuit Court would both be dismissed without prejudice pending the decision of the Federal Court of Appeals on the District Court's decision relating to the first patent.

On January 19, 2009, a purported class action case was commenced against the Company in the Superior Court of California, Santa Cruz County, by Eric Ross and Bradley S. Hureth generally alleging certain product defects in the Company's products, and that the Company has failed to provide adequate remedies for defective products. On February 13, 2009, the Company removed this case to the United States District Court, Northern District of California. On January 21, 2009, a purported class action case was commenced against the Company in the United States District Court, Western District of Washington by Mark Okano making similar allegations. The Company believes that both lawsuits are without merit.

### **Purchase Commitments**

The Company fulfills requirements for raw materials under both purchase orders and supply contracts. In the year ended December 31, 2008, the Company purchased substantially all of its waste wood fiber requirements under purchase orders, which do not involve long-term supply commitments. Substantially all of the Company's PE material purchases are under short-term supply contracts that average two years, for which pricing is negotiated as needed. The PE material supply contracts have not had a material adverse effect on the Company's business.

The waste wood and PE material supply contracts generally provide that the Company is obligated to purchase all of the waste wood or PE material a supplier provides, if the waste wood or PE material meets certain specifications. The amount of waste wood and PE material the Company is required to purchase under these contracts varies with the production of its suppliers and, accordingly, is not fixed or determinable.

The Company outsources the production of certain products to third-party manufacturers under supply contracts that commit the Company to purchase minimum levels for each year extending through 2011. The Company has purchase commitments under the third-party manufacturing contracts of \$32.8 million, \$33.6 million and \$33.6 million for the years ended December 31, 2009, 2010 and 2011, respectively, and is subject to monetary penalties if it fails to purchase the minimum volumes specified in the contracts.

**Contract Termination Costs**

In anticipation of relocating the Company's corporate headquarters, the Company entered into a lease agreement in 2005. The Company reconsidered and decided not to move its headquarters. The lease, which began on January 1, 2006 and extends through June 30, 2019, currently obligates the Company to lease 55,047 square feet and increases to 80,071 square feet in 2012. As of January 10, 2008, the Company had executed subleases for the entire 55,047 square feet it currently leases. The terms of the existing subleases extend through years 2012 to 2015. The Company estimates that the present value of the estimated future sublease rental

**Table of Contents**

receipts, net of transaction costs, will be less than the Company's remaining minimum lease payment obligations under its lease for the office space. Accordingly, the Company accounts for the costs associated with the lease as contract termination costs in accordance with SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities*.

To estimate future sublease receipts for the periods beyond the term of the existing subleases and for the additional space the Company is obligated to lease, the Company has assumed that the existing subleases will be renewed or new subleases will be executed at rates consistent with rental rates in the current subleases. However, management cannot be certain that the timing of future subleases or the rental rates contained in future subleases will not differ from current estimates. Factors such as the delivery of a significant amount of new office space or poor economic conditions could have a negative effect on vacancy rates and rental rates in the area. The inability to sublet the office space in the future or unfavorable changes to key management assumptions used in the estimate of the future sublease receipts may result in additional charges to selling, general and administrative expenses in future periods.

As of December 31, 2008, the minimum payments remaining under the Company's lease over the years ending December 31, 2009, 2010, 2011, 2012 and 2013 are \$1.6 million, \$1.6 million, \$1.6 million, \$2.0 million and \$2.5 million, respectively, and \$14.2 million thereafter. The minimum receipts remaining under the Company's existing subleases over the years ending December 31, 2009, 2010, 2011, 2012 and 2013 are \$1.5 million, \$1.6 million, \$1.6 million, \$1.6 million and \$1.3 million, respectively, and \$1.0 million thereafter. During the three months ended June 30, 2008, the Company recorded a \$0.4 million charge related to a change in the estimated future sublease cash flows. The following table provides information about the Company's liability under the lease (in thousands):

	2007	2008
Balance as of January 1,	\$ 1,765	\$ 925
Less: cash payments	(1,392)	(847)
Accretion of discount	110	55
Add: charge for minimum lease payments in excess of estimated sublease receipts, net	442	391
Balance as of December 31,	\$ 925	\$ 524

**Product Warranty**

The Company warrants that its products will be free from material defects in workmanship and material and will not check, split, splinter, rot or suffer structural damage from termites or fungal decay. If there is such a defect in any of its products, the Company has an obligation either to replace the defective product or refund the purchase price. The Company establishes warranty reserves to provide for estimated future expenses as a result of product defects that result in claims. Reserve estimates are based on management's judgment, considering such factors as historical experience and other available information. Management reviews and adjusts these estimates, if necessary, on a quarterly basis based on the differences between actual experience and historical estimates.

During the three months ended September 30, 2007, the Company experienced a significant increase in the number of customer claims related to Trex product that exhibited surface defects and which the Company has determined was produced at the Nevada manufacturing facility beginning in 2003. Following a detailed analysis of the additional claims data, production samples, operating data and the incubation period after deck installation and other factors, the Company believes that only a small percentage of the product manufactured from 2003 to mid-2006 at the Nevada plant was affected, and that products manufactured at its other facilities are not affected. The Company believes that changes made to its manufacturing process and quality control procedures have prevented any additional product with this type of defect from reaching the market after mid-2006.

Based on the available data, the Company revised its estimate of expected future product replacement and consumer relations expenses related to the defect and increased its warranty reserve by recording a charge to earnings of \$45.2 million in the three months ended September 30, 2007. In addition, during the three months ended December 31, 2007, the Company elected to alter its handling of future customer claims. As a result of the effect of this change on the estimated cost to settle claims, the Company recorded an additional \$1.5 million increase to its warranty reserve. During 2008, the Company continued to fund payments for product defect claims from the established reserve. Although the Company adjusts the warranty reserve accordingly by recording the best estimate of the expected costs, due to the inherent subjectivity of estimating future claims, it is possible that the ultimate settlement of the claims may exceed the amount recorded and may result in future charges against income.

The following is a reconciliation of the Company's warranty reserve (in thousands):

Edgar Filing: TREX CO INC - Form 10-K/A

	2007	2008
Beginning balance, January 1	\$ 2,467	\$ 39,985
Provision for estimated warranties	65,496	
Settlements made during the period	(27,978)	(18,129)
Ending balance, December 31	\$ 39,985	\$ 21,856

**Table of Contents****15. RELATED PARTY TRANSACTIONS**

Anthony J. Cavanna retired as Chief Executive Officer of the Company effective August 15, 2007. Effective September 10, 2007, Mr. Cavanna was appointed as the interim Chief Financial Officer of the Company. In connection with Mr. Cavanna's service as interim Chief Financial Officer, the Company and Mr. Cavanna entered into a consulting agreement. Under the terms of the consulting agreement, which was terminated on March 17, 2008, Mr. Cavanna received consulting fees of \$71,500 in the year ended December 31, 2008 in connection with his performance of services under the agreement.

On February 1, 2008, the Company entered into a consulting agreement with Harold F. Monahan, Executive Vice President, Materials and Engineering, whose last day of employment with the Company was March 10, 2008. Under the terms of the consulting agreement, Mr. Monahan provided services to the Company between March 11, 2008 and December 31, 2008 relating to manufacturing, engineering, and raw materials. Mr. Monahan received consulting fees of \$86,000 in the year ended December 31, 2008 in connection with his performance of services under the agreement. Mr. Monahan's consulting agreement terminated on December 31, 2008.

**16. INTERIM FINANCIAL DATA (Unaudited)**

The selected interim financial data presented below for 2007 and 2008 has been restated to correct an error in income tax expense and adjust the financial data for the retrospective adoption of FSP APB 14-1. This error correction and accounting changes are discussed more fully in Notes 2 and 3 to the accompanying consolidated financial statements.

The accompanying financial data for the quarter ended March 31, 2008 was previously restated for the adoption of FSP APB 14-1 in connection with the Company's filing of its Quarterly Report on Form 10-Q for the quarter ended March 31, 2009 on May 8, 2009. Accordingly, the amounts in the column as previously reported for the quarter ended March 31, 2008 were previously adjusted for the retrospective adoption of FSP APB 14-1.

(In thousands, except share and per share data)

	First Quarter				Second Quarter				
	As		As		As		As		
	Previously Reported	(a) (b)	Restated	Previously Reported	(a) (b)	Restated	Previously Reported	(a) (b)	
<b>2007</b>									
Net sales	\$ 115,913	\$ \$	\$ 115,913	\$ 118,779	\$ \$	\$ 118,779	\$ \$	\$ 118,779	\$ \$
Cost of sales	91,284		91,284	89,615		89,615		89,615	
Gross profit (loss)	24,629		24,629	29,164		29,164		29,164	
Selling, general and administrative expenses	17,039		17,039	22,860		22,860		22,860	
Income (loss) from operations	7,590		7,590	6,304		6,304		6,304	
Interest expense, net	1,694		1,694	2,526	166	2,692		2,692	
Income (loss) before provision for income taxes	5,896		5,896	3,778	(166)	3,612		3,612	
Provision (benefit) for income taxes	2,171		2,171	1,190	(15)	1,175		1,175	
Net income (loss)	\$ 3,725	\$ \$	\$ 3,725	\$ 2,588	\$ \$	\$ 2,588	\$ \$	\$ 2,588	\$ \$
Basic earnings (loss) per common share	\$ 0.25	\$ \$	\$ 0.25	\$ 0.17	\$ \$	\$ 0.17	\$ \$	\$ 0.17	\$ \$
Basic weighted average common shares outstanding	14,856,315		14,856,315	14,887,632		14,887,632		14,887,632	
Diluted earnings (loss) per common share	\$ 0.25	\$ \$	\$ 0.25	\$ 0.17	\$ \$	\$ 0.17	\$ \$	\$ 0.17	\$ \$

## Edgar Filing: TREX CO INC - Form 10-K/A

Diluted weighted average common shares outstanding	14,898,851	14,898,851	14,916,648	14,916,648	14,916,648
--	------------	------------	------------	------------	------------

The Company's net sales, gross profit and income from operations have historically varied from quarter to quarter. Such variations are principally attributable to seasonal trends in the demand for Trex. The Company has historically experienced lower net sales during the fourth quarter because holidays and adverse weather conditions in certain regions reduce the level of home improvement and new construction activity.

- (a) Adjustments to correct accounting for income tax error and certain immaterial reclassification adjustments.
- (b) Adjustments due to the retrospective adoption of FSP APB 14-1.

**Table of Contents**

(In thousands, except share and per share data)

2007	Third Quarter (1)				Fourth Quarter (2)			
	As Previously Reported	(a)	(b)	As Restated	As Previously Reported	(a)	(b)	As Restated
Net sales	\$ 63,971	\$	\$	\$ 63,971	\$ 30,289	\$	\$	\$ 30,289
Cost of sales	73,631			73,631	34,999			34,999
Gross profit (loss)	(9,660)			(9,660)	(4,710)			(4,710)
Selling, general and administrative expenses	52,074			52,074	27,466			27,466
Income (loss) from operations	(61,734)			(61,734)	(32,176)			(32,176)
Interest expense, net	2,021		1,171	3,192	2,754		1,171	3,925
Income (loss) before provision for income taxes	(63,755)		(1,171)	(64,926)	(34,930)		(1,171)	(36,101)
Provision (benefit) for income taxes	(22,528)		(439)	(22,967)	6,068	1,612	(14,164)	(6,484)
Net income (loss)	\$ (41,227)	\$	\$ (732)	\$ (41,959)	\$ (40,998)	\$ (1,612)	\$ 12,993	\$ (29,617)
Basic earnings (loss) per common share	\$ (2.77)	\$	\$ (0.05)	\$ (2.82)	\$ (2.75)	\$ (0.11)	\$ 0.87	\$ (1.99)
Basic weighted average common shares outstanding	14,892,507		14,892,507	14,892,507	14,899,675	14,899,675	14,899,675	14,899,675
Diluted earnings (loss) per common share	\$ (2.77)	\$	\$ (0.05)	\$ (2.82)	\$ (2.75)	\$ (0.11)	\$ 0.87	\$ (1.99)
Diluted weighted average common shares outstanding	14,892,507		14,892,507	14,892,507	14,899,675	14,899,675	14,899,675	14,899,675

The Company's net sales, gross profit and income from operations have historically varied from quarter to quarter. Such variations are principally attributable to seasonal trends in the demand for Trex. The Company has historically experienced lower net sales during the fourth quarter because holidays and adverse weather conditions in certain regions reduce the level of home improvement and new construction activity.

- (a) Adjustments to correct accounting for income tax error and certain immaterial reclassification adjustments.
- (b) Adjustments due to the retrospective adoption of FSP APB 14-1.
- (1) Three months ended September 30, 2007 materially affected by an increase in the warranty reserve and inventory valuation adjustments as disclosed in the Company's previous filings.
- (2) Three months ended December 31, 2007 materially affected by an increase in the warranty reserve, fixed asset disposal charges, inventory valuation adjustments and tax valuation allowance as disclosed in the Company's previous filings.





**Table of Contents**

(In thousands, except share and per share data)

2008	First Quarter				Second Quarter			
	As Previously Reported	(a)	(b)	As Restated	As Previously Reported	(a)	(b)	As Restated
Net sales	\$ 119,529	\$	\$	\$ 119,529	\$ 94,998	\$	\$	\$ 94,998
Cost of sales	87,253			87,253	66,881	499		67,380
Gross profit (loss)	32,276			32,276	28,117	(499)		27,618
Selling, general and administrative expenses	20,308			20,308	18,330	(499)		17,831
Income (loss) from operations	11,968			11,968	9,787			9,787
Interest expense, net	4,347			4,347	1,882		1,370	3,252
Income (loss) before provision for income taxes	7,621			7,621	7,905		(1,370)	6,535
Provision (benefit) for income taxes	86	134		220	17	34		51
Net income (loss)	\$ 7,535	\$ (134)	\$	\$ 7,401	\$ 7,888	\$ (34)	\$ (1,370)	\$ 6,484
Basic earnings (loss) per common share	\$ 0.50	\$	\$	\$ 0.50	\$ 0.53	\$	\$ (0.10)	\$ 0.43
Basic weighted average common shares outstanding	14,936,235	14,936,235		14,936,235	14,956,154	14,956,154	14,956,154	14,956,154
Diluted earnings (loss) per common share	\$ 0.50	\$ (0.01)	\$	\$ 0.49	\$ 0.52	\$	\$ (0.09)	\$ 0.43
Diluted weighted average common shares outstanding	14,955,837	14,955,837		14,955,837	15,044,943	15,044,943	15,044,943	15,044,943

The Company's net sales, gross profit and income from operations have historically varied from quarter to quarter. Such variations are principally attributable to seasonal trends in the demand for Trex. The Company has historically experienced lower net sales during the fourth quarter because holidays and adverse weather conditions in certain regions reduce the level of home improvement and new construction activity.

- (a) Adjustments to correct accounting for income tax error and certain immaterial reclassification adjustments.  
(b) Adjustments due to the retrospective adoption of FSP APB 14-1.

**Table of Contents**

(In thousands, except share and per share data)

2008	Third Quarter				Fourth Quarter			
	As Previously Reported	(a)	(b)	As Restated	As Previously Reported	(a)	(b)	As Restated
Net sales	\$ 85,379	\$	\$	\$ 85,379	\$ 29,288	\$	\$	\$ 29,288
Cost of sales	61,827	579		62,406	22,435	696		23,131
Gross profit (loss)	23,552	(579)		22,973	6,853	(696)		6,157
Selling, general and administrative expenses	15,112	(579)		14,533	14,982	(696)		14,286
Income (loss) from operations	8,440			8,440	(8,129)			(8,129)
Interest expense, net	2,041		1,495	3,536	2,651		1,496	4,147
Income (loss) before provision for income taxes	6,399		(1,495)	4,904	(10,780)		(1,496)	(12,276)
Provision (benefit) for income taxes	(318)	57		(261)	(823)	63		(760)
Net income (loss)	\$ 6,717	\$ (57)	\$ (1,495)	\$ 5,165	\$ (9,957)	\$ (63)	\$ (1,496)	\$ (11,516)
Basic earnings (loss) per common share	\$ 0.45	\$	\$ (0.10)	\$ 0.35	\$ (0.67)	\$	\$ (0.10)	\$ (0.77)
Basic weighted average common shares outstanding	14,964,110	14,964,110	14,964,110	14,964,110	14,970,975	14,970,975	14,970,975	14,970,975
Diluted earnings (loss) per common share	\$ 0.44	\$	\$ (0.10)	\$ 0.34	\$ (0.67)	\$	\$ (0.10)	\$ (0.77)
Diluted weighted average common shares outstanding	15,253,680	15,253,680	15,253,680	15,253,680	14,970,975	14,970,975	14,970,975	14,970,975

## Edgar Filing: TREX CO INC - Form 10-K/A

The Company's net sales, gross profit and income from operations have historically varied from quarter to quarter. Such variations are principally attributable to seasonal trends in the demand for Trex. The Company has historically experienced lower net sales during the fourth quarter because holidays and adverse weather conditions in certain regions reduce the level of home improvement and new construction activity.

- (a) Adjustments to correct accounting for income tax error and certain immaterial reclassification adjustments.
- (b) Adjustments due to the retrospective adoption of FSP APB 14-1.

**Table of Contents****TREX COMPANY, INC.****SCHEDULE II VALUATION AND QUALIFYING ACCOUNTS AND RESERVES****(In Thousands)**

<b>Descriptions</b>	<b>Balance at Beginning of Period</b>	<b>Additions (Reductions) Charged to Cost and Expenses</b>	<b>Other</b>	<b>Deductions</b>	<b>Balance at End of Period</b>
<b>Year ended December 31, 2008:</b>					
Allowance for doubtful accounts (a)	\$ 3,074	\$ (701)	\$	\$ (884)	\$ 1,489
Warranty reserve	\$ 39,985	\$	\$	\$ (18,129)	\$ 21,856
Income tax valuation allowance (as restated see Note 2)	\$ 9,581	\$ (4,118)	\$ 133	\$	\$ 5,596
<b>Year ended December 31, 2007:</b>					
Allowance for doubtful accounts (a)	\$ 1,059	\$ 2,130	\$	\$ (115)	\$ 3,074
Warranty reserve	\$ 2,467	\$ 65,496	\$	\$ (27,978)	\$ 39,985
Income tax valuation allowance (as restated see Note 2)	\$ 2,229	\$ 7,352	\$	\$	\$ 9,581
<b>Year ended December 31, 2006:</b>					
Allowance for doubtful accounts (a)	\$ 627	\$ 570	\$	\$ (138)	\$ 1,059
Warranty reserve	\$	\$ 12,268	\$	\$ (9,801)	\$ 2,467
Income tax valuation allowance	\$ 1,354	\$ 875	\$	\$	\$ 2,229

(a) Reserve related to accounts receivable

**Table of Contents**

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

**Trex Company, Inc.**

Date: August 10, 2009

By: **/s/ RONALD W. KAPLAN**  
**Ronald W. Kaplan**  
**President and Chief Executive Officer**

**(Duly Authorized Officer)**

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed as of August 10, 2009 by the following persons on behalf of the registrant and in the capacities indicated.

Signature	Title
<i>/s/ RONALD W. KAPLAN</i> <b>Ronald W. Kaplan</b>	President and Chief Executive Officer (Principal Executive Officer); Director
<i>/s/ JAMES E. CLINE</i> <b>James E. Cline</b>	Vice President and Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)
<i>/s/ ANDREW U. FERRARI</i> <b>Andrew U. Ferrari</b>	Chairman
<i>/s/ WILLIAM F. ANDREWS</i> <b>William F. Andrews</b>	Director
<i>/s/ PAUL A. BRUNNER</i> <b>Paul A. Brunner</b>	Director
<i>/s/ JAY M. GRATZ</i> <b>Jay M. Gratz</b>	Director
<i>/s/ FRANK H. MERLOTTI, JR.</i> <b>Frank H. Merlotti, Jr.</b>	Director
<i>/s/ RICHARD E. POSEY</i> <b>Richard E. Posey</b>	Director
<i>/s/ PATRICIA B. ROBINSON</i> <b>Patricia B. Robinson</b>	Director

**Table of Contents**

**EXHIBIT INDEX**

<b>Exhibit Number</b>	<b>Exhibit Description</b>
3.1	Restated Certificate of Incorporation of Trex Company, Inc. (the Company). Filed as Exhibit 3.1 to the Company's Registration Statement on Form S-1 (No. 333-63287) and incorporated herein by reference.
3.2	Amended and Restated By-Laws of the Company. Filed as Exhibit 3.2 to the Company's Current Report on Form 8-K filed May 7, 2008 and incorporated herein by reference.
4.1	Specimen certificate representing the Company's common stock. Filed as Exhibit 4.1 to the Company's Registration Statement on Form S-1 (No. 333-63287) and incorporated herein by reference.
4.2	Indenture, dated as of June 18, 2007, between Trex Company, Inc. and The Bank of New York, as trustee. Filed as Exhibit 4.1 to the Company's Current Report on Form 8-K filed on June 19, 2007 and incorporated herein by reference.
4.3	Supplemental Indenture, dated as of June 18, 2007, between Trex Company, Inc. and The Bank of New York, as trustee, including the form of 6.00% Convertible Senior Subordinated Note due 2012. Filed as Exhibit 4.2 to the Company's Current Report on Form 8-K filed on June 19, 2007 and incorporated herein by reference.
10.1	Description of Management Compensatory Plans and Arrangements. Filed as Exhibit 10.1 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.
10.2	Trex Company, Inc. 2005 Stock Incentive Plan. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on May 7, 2008 and incorporated herein by reference.
10.3	Trex Company, Inc. Amended and Restated 1999 Incentive Plan for Outside Directors. Filed as Exhibit 10.4 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2007 and incorporated herein by reference.
10.4	Form of Trex Company, Inc. 2005 Stock Incentive Plan Non-Incentive Stock Option Agreement. Filed as Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005 and incorporated herein by reference.
10.5	Form of Trex Company, Inc. 2005 Stock Incentive Plan Stock Appreciation Rights Agreement. Filed as Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005 and incorporated herein by reference.
10.6	Form of Trex Company, Inc. 2005 Stock Incentive Plan Performance Award Agreement. Filed as Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005 and incorporated herein by reference.
10.7	Form of Trex Company, Inc. 2005 Stock Incentive Plan Restricted Stock Agreement, as amended. Filed as Exhibit 10.8 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and incorporated herein by reference.
10.8	Form of Trex Company, Inc. Amended and Restated 1999 Incentive Plan for Outside Directors Non-Incentive Stock Option Agreement for Directors. Filed as Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006 and incorporated herein by reference.
10.9	Form of Trex Company, Inc. Amended and Restated 1999 Incentive Plan for Outside Directors Stock Appreciation Rights Agreement. Filed as Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006 and incorporated herein by reference.
10.10	Form of Lock-Up Agreement, dated as of December 20, 2005. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on December 21, 2005 and incorporated herein by reference.

**Table of Contents**

**Exhibit**

**Number Exhibit Description**

- 10.11 Form of Change in Control Severance Agreement for Officers of Trex Company, Inc. other than the Chief Executive Officer. Filed as Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2007 and incorporated herein by reference.
- 10.12 Consulting Agreement, dated September 10, 2007, by and between Trex Company, Inc. and Anthony J. Cavanna. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on September 11, 2007 and incorporated herein by reference.
- 10.13 Amended and Restated Stock Appreciation Rights Agreement, between Trex Company, Inc. and Anthony J. Cavanna dated August 14, 2007. Filed as Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2007 and incorporated herein by reference.
- 10.14 Amended and Restated Stock Appreciation Rights Agreement, between Trex Company, Inc. and Anthony J. Cavanna dated August 14, 2007. Filed as Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2007 and incorporated herein by reference.
- 10.15 Amended and Restated Restricted Stock Agreement, between Trex Company, Inc. and Anthony J. Cavanna dated August 14, 2007. Filed as Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2007 and incorporated herein by reference.
- 10.16 Employment Agreement, dated as of January 1, 2008, between Trex Company, Inc. and Ronald W. Kaplan. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on January 2, 2008 and incorporated herein by reference.
- 10.17 Change in Control Severance Agreement, dated as of January 1, 2008, between Trex Company, Inc. and Ronald W. Kaplan. Filed as Exhibit 10.2 to the Company's Current Report on Form 8-K filed on January 2, 2008 and incorporated herein by reference.
- 10.18 Consulting Agreement, dated February 1, 2008, by and between Trex Company, Inc. and Harold F. Monahan. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on February 1, 2008 and incorporated herein by reference.
- 10.19 Form of Indemnity Agreement for Directors. Filed as Exhibit 10.19 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.
- 10.20 Form of Indemnity Agreement for Officers. Filed as Exhibit 10.20 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.
- 10.21 Form of Indemnity Agreement for Director/Officers. Filed as Exhibit 10.21 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.
- 10.22 Form of Distributor Agreement of TREX Company, Inc. Filed as Exhibit 10.5 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2001 and incorporated herein by reference.
- 10.23 Form of Distributor Agreement of TREX Company, Inc. Filed as Exhibit 10.23 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.
- 10.24 Form of Trex Company, Inc. Fencing Agreement for Installers/Retailers. Filed as Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2006 and incorporated herein by reference.
- 10.25 Deed of Lease, dated June 15, 2000, between TREX Company, LLC and Space, LLC. Filed as Exhibit 10.16 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2000 and incorporated herein by reference.
- 10.26 Deed of Lease, dated as of July 27, 2005, between the Company and 1 Dulles Town Center, L.L.C. Filed as Exhibit 10.34 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2005 and incorporated herein by reference.\*

**Table of Contents**

<b>Exhibit Number</b>	<b>Exhibit Description</b>
10.27	Credit Agreement, dated as of June 19, 2002, among TREX Company, LLC, the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.2 to the Company's Current Report on Form 8-K filed on June 25, 2002 (as amended by the Company's Current Report on Form 8-K/A filed on June 28, 2002) and incorporated herein by reference.
10.28	Security Agreement, dated as of March 16, 2007, by and among the Company and Branch Banking and Trust Company, as collateral agent. Filed as Exhibit 10.16 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and incorporated herein by reference.
10.29	First Amendment to Security Agreement, dated as of and effective as of September 30, 2007, with Branch Banking and Trust Company, as Collateral Agent and Senior Secured Party, and JPMorgan Chase Bank, N.A., as Junior Secured Party. Filed as Exhibit 10.26 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2007 and incorporated herein by reference.
10.30	Credit Line Deed of Trust, dated June 19, 2002, by and among TREX Company, LLC, as grantor, BB&T-VA Collateral Service Corporation, as trustee, and Branch Banking and Trust Company of Virginia and Branch Banking and Trust Company, as note holder. Filed as Exhibit 10.5 to the Company's Current Report on Form 8-K filed on June 25, 2002 and incorporated herein by reference.
10.31	First Amendment to Credit Agreement, dated as of August 29, 2003, by and between the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.21 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2005 and incorporated herein by reference.
10.32	Second Amendment to Credit Agreement, dated as of September 30, 2004, among the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.4 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended September 30, 2004 and incorporated herein by reference.
10.33	Third Amendment to Credit Agreement, dated as of March 31, 2005, by and between the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.6 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005 and incorporated herein by reference.
10.34	Fourth Amendment to Credit Agreement, dated as of July 25, 2005, by and between the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.7 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005 and incorporated herein by reference.
10.35	Fifth Amendment to Credit Agreement, dated as of December 31, 2005, among the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.25 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2005 and incorporated herein by reference.
10.36	Sixth Amendment to Credit Agreement, dated as of November 9, 2006, among the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.24 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and incorporated herein by reference.
10.37	Seventh Amendment to Credit Agreement, dated as of December 31, 2006, among the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.25 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and incorporated herein by reference.
10.38	Eighth Amendment to Credit Agreement, dated as of March 16, 2007, among the Company and Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.26 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and incorporated herein by reference.



**Table of Contents**

<b>Exhibit Number</b>	<b>Exhibit Description</b>
10.39	Ninth Amendment to Credit Agreement, effective as of June 18, 2007, between Trex Company, Inc. and Branch Banking and Trust Company. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on June 19, 2007 and incorporated herein by reference.
10.40	Tenth Amendment to Credit Agreement, dated as of December 21, 2007, by and between Trex Company, Inc. and Branch Banking and Trust Company. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on December 21, 2007 and incorporated herein by reference.
10.41	Eleventh Amendment to Credit Agreement, dated as of December 31, 2007, by and between Trex Company, Inc. and Branch Banking and Trust Company. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on March 7, 2008 and incorporated herein by reference.
10.42	Twelfth Amendment to Credit Agreement, dated as of June 16, 2008, by and between Trex Company, Inc. and Branch Banking and Trust Company. Filed as Exhibit 10.42 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.
10.43	Thirteenth Amendment to Credit Agreement, dated as of November 10, 2008, by and between Trex Company, Inc. and Branch Banking and Trust Company. Filed as Exhibit 10.43 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2008 and incorporated herein by reference.
10.44	Promissory Note (Revolving Note), dated as of December 31, 2006, in the principal amount of \$100,000,000 from the Company payable to the order of Branch Banking and Trust Company of Virginia. Filed as Exhibit 10.27 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and incorporated herein by reference.
10.45	Loan Agreement, dated as of December 1, 2004, between the Company and Mississippi Business Finance Corporation. Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on December 20, 2004 and incorporated herein by reference.
10.46	Promissory Note, dated as of December 16, 2004, in the principal amount of \$25,000,000 from the Company payable to the order of Mississippi Business Finance Corporation. Filed as Exhibit 10.2 to the Company's Current Report on Form 8-K filed on December 20, 2004 and incorporated herein by reference.
10.47	Reimbursement and Credit Agreement, dated as of December 1, 2004, between the Company and JPMorgan Chase Bank, N.A., as Issuing Bank and Administrative Agent. Filed as Exhibit 10.3 to the Company's Current Report on Form 8-K filed on December 20, 2004 and incorporated herein by reference.
10.48	First Amendment to Reimbursement and Credit Agreement, dated as of July 25, 2005, by and between the Company and JPMorgan Chase Bank, N.A., as Issuing Bank and Administrative Agent. Filed as Exhibit 10.5 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2005 and incorporated herein by reference.
10.49	Second Amendment to Reimbursement and Credit Agreement, dated as of December 31, 2005, by and between the Company and JPMorgan Chase Bank, N.A., as Issuing Bank and Administrative Agent. Filed as Exhibit 10.30 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2005 and incorporated herein by reference.
10.50	Third Amendment to Reimbursement and Credit Agreement, dated as of November 21, 2006, by and between the Company and JPMorgan Chase Bank, N.A., as Issuing Bank and Administrative Agent. Filed as Exhibit 10.33 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and incorporated herein by reference.
10.51	Fourth Amendment to Reimbursement and Credit Agreement, dated as of December 31, 2006, by and between the Company and JPMorgan Chase Bank, N.A., as Issuing Bank and Administrative Agent. Filed as Exhibit 10.34 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and incorporated herein by reference.

**Table of Contents**

<b>Exhibit Number</b>	<b>Exhibit Description</b>
10.52	Fifth Amendment to Reimbursement and Credit Agreement, effective as of June 18, 2007, between Trex Company, Inc. and JPMorgan Chase Bank, N.A., as Issuing Bank and Administrative Agent. Filed as Exhibit 10.2 to the Company's Current Report on Form 8-K filed on June 19, 2007 and incorporated herein by reference.
10.53	Sixth Amendment to Reimbursement and Credit Agreement, dated as of December 21, 2007, between Trex Company, Inc. and JPMorgan Chase Bank, N.A., as Issuing Bank and Administrative Agent. Filed as Exhibit 10.2 to the Company's Current Report on Form 8-K filed on December 21, 2007 and incorporated herein by reference.
10.54	Seventh Amendment to Reimbursement and Credit Agreement, dated as of December 31, 2007, between Trex Company, Inc. and JPMorgan Chase Bank, N.A., as Issuing Bank and Administrative Agent. Filed as Exhibit 10.2 to the Company's Current Report on Form 8-K filed on March 7, 2008 and incorporated herein by reference.
10.55	Reimbursement Note, dated as of December 1, 2004, in the principal amount of \$25,308,220 from the Company payable to JPMorgan Chase Bank, N.A. Filed as Exhibit 10.4 to the Company's Current Report on Form 8-K filed on December 20, 2004 and incorporated herein by reference.
10.56	Land Deed of Trust, dated as of December 1, 2004, made by the Company to the trustee named therein for the benefit of JPMorgan Chase Bank, N.A. Filed as Exhibit 10.5 to the Company's Current Report on Form 8-K filed on December 20, 2004 and incorporated herein by reference.
10.57	First Amendment to Land Deed of Trust, dated as of and effective as of September 30, 2007, with JPMorgan Chase Bank, N.A., as Beneficiary and Secured Party, and the Trustee therein named for the benefit of such Beneficiary. Filed as Exhibit 10.52 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2007 and incorporated herein by reference.
10.58	Trust Indenture, dated as of December 1, 2004, between Mississippi Business Finance Corporation and J.P. Morgan Trust Company, National Association, as Trustee, including Form of Variable Rate Series 2004 Bond and Form of Fixed Rate Series 2004 Bond. Filed as Exhibit 10.6 to the Company's Current Report on Form 8-K filed on December 20, 2004 and incorporated herein by reference.
21	Subsidiaries of the Company. Filed herewith.
23	Consent of Ernst & Young LLP, Independent Registered Public Accounting Firm. Filed herewith.
31.1	Certification of Chief Executive Officer of the Company pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934. Filed herewith.
31.2	Certification of Chief Financial Officer of the Company pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934. Filed herewith.
32	Certifications pursuant to Rule 13a-14(b) under the Securities Exchange Act of 1934 and 18 U.S.C. § 1350. Filed herewith.

\* Portions of this exhibit have been omitted and filed separately with the Securities and Exchange Commission pursuant to a request for confidential treatment.