

WESCO INTERNATIONAL INC

Form 10-Q

November 09, 2006

**Table of Contents**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM 10-Q**

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

**For the quarterly period ended September 30, 2006**

**or**

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

**FOR THE TRANSITION PERIOD from \_\_\_\_\_ to \_\_\_\_\_**

**Commission file number 001-14989**

**WESCO International, Inc.**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of  
incorporation or organization)

**25-1723342**

(IRS Employer Identification No.)

**225 West Station Square Drive**

**Suite 700**

**Pittsburgh, Pennsylvania 15219**

(Address of principal executive offices)

**(412) 454-2200**

(Registrant's telephone number, including area code)

**N/A**

(Former name or former address, if changed since last report)

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 at least the past 90 days. Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):  
Large accelerated filer  Accelerated filer  Non-accelerated filer

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

As of October 31, 2006, WESCO International, Inc. had 49,163,972 shares common stock outstanding.

**Table of Contents**

**WESCO INTERNATIONAL, INC. AND SUBSIDIARIES  
QUARTERLY REPORT ON FORM 10-Q  
Table of Contents**

	Page
<b>PART I FINANCIAL INFORMATION</b>	
<b>Item 1.</b> Financial Statements	
<u>Condensed Consolidated Balance Sheets as of September 30, 2006 and December 31, 2005 (unaudited)</u>	2
<u>Condensed Consolidated Statements of Income for the three months and nine months ended September 30, 2006 and 2005 (unaudited)</u>	3
<u>Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2006 and 2005 (unaudited)</u>	4
<u>Notes to Condensed Consolidated Financial Statements (unaudited)</u>	5
<b>Item 2.</b> <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	20
<b>Item 3.</b> <u>Quantitative and Qualitative Disclosures About Market Risk</u>	28
<b>Item 4.</b> <u>Controls and Procedures</u>	28
<b>PART II OTHER INFORMATION</b>	
<b>Item 1.</b> <u>Legal Proceedings</u>	29
<b>Item 6.</b> <u>Exhibits</u>	29
<u>Signatures and Certifications</u>	30
<u>EX-23.1</u>	
<u>EX-31.1</u>	
<u>EX-31.2</u>	
<u>EX-32.1</u>	
<u>EX-32.2</u>	

**Table of Contents**

**WESCO INTERNATIONAL, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(unaudited)

<i>Amounts in thousands, except share data</i>	<b>September 30, 2006</b>	<b>December 31, 2005</b>
<b>Assets</b>		
<b>Current Assets:</b>		
Cash and cash equivalents	\$ 59,273	\$ 22,125
Trade accounts receivable, net of allowance for doubtful accounts of \$13,089 and \$12,609 in 2006 and 2005, respectively ( <b>Note 5</b> )	460,966	315,594
Other accounts receivable	31,191	36,235
Inventories, net	542,244	500,798
Current deferred income taxes	16,984	13,399
Income taxes receivable		12,814
Prepaid expenses and other current assets	9,554	7,898
<b>Total current assets</b>	<b>1,120,212</b>	<b>908,863</b>
Property, buildings and equipment, net	104,771	103,083
Intangible assets, net ( <b>Note 6</b> )	79,134	83,892
Goodwill ( <b>Note 6</b> )	550,338	542,217
Other assets	13,644	13,104
<b>Total assets</b>	<b>\$1,868,099</b>	<b>\$1,651,159</b>
<b>Liabilities and Stockholders Equity</b>		
<b>Current Liabilities:</b>		
Accounts payable	\$ 605,919	\$ 572,467
Accrued payroll and benefit costs	51,318	51,220
Short-term debt related to revolving credit facility		14,500
Current portion of long-term debt	5,856	36,825
Deferred acquisition payable	3,936	2,680
Bank overdrafts	17,123	3,695
Other current liabilities	50,354	38,499
<b>Total current liabilities</b>	<b>734,506</b>	<b>719,886</b>
Long-term debt	348,816	352,232
Long-term deferred acquisition payable		4,346
Other noncurrent liabilities	12,396	9,507
Deferred income taxes	77,200	73,738
<b>Total liabilities</b>	<b>1,172,918</b>	<b>1,159,709</b>
Commitments and contingencies ( <b>Note 8</b> )		

**Stockholders Equity:**

Preferred stock, \$.01 par value; 20,000,000 shares authorized, no shares issued or outstanding		
Common stock, \$.01 par value; 210,000,000 shares authorized, 53,252,805 and 51,790,725 shares issued in 2006 and 2005, respectively	533	518
Class B nonvoting convertible common stock, \$.01 par value; 20,000,000 shares authorized, 4,339,431 issued in 2006 and 2005; no shares outstanding	43	43
Additional capital	755,894	707,407
Retained deficit	(9,319)	(168,332)
Treasury stock, at cost; 8,549,323 and 8,418,607 shares in 2006 and 2005, respectively	(68,599)	(61,821)
Accumulated other comprehensive income	16,629	13,635
Total stockholders equity	695,181	491,450
Total liabilities and stockholders equity	\$1,868,099	\$1,651,159

*The accompanying notes are an integral part of the condensed consolidated financial statements.*

**Table of Contents**

**WESCO INTERNATIONAL, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME**  
(unaudited)

<i>Amounts in thousands, except share data</i>	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Net sales	\$1,343,066	\$1,131,449	\$3,944,550	\$3,184,381
Cost of goods sold (excluding depreciation and amortization below)	1,067,406	923,136	3,145,231	2,596,300
Gross profit	275,660	208,313	799,319	588,081
Selling, general and administrative expenses	168,830	157,300	508,240	441,968
Depreciation and amortization	6,653	3,707	19,249	11,330
Income from operations	100,177	47,306	271,830	134,783
Interest expense	5,094	6,450	17,100	22,425
Loss on debt extinguishment				10,051
Other expenses ( <b>Note 5</b> )	5,814	3,796	17,137	8,814
Income before income taxes	89,269	37,060	237,593	93,493
Provision for income taxes	29,884	12,052	78,580	29,702
Net income	\$ 59,385	\$ 25,008	\$ 159,013	\$ 63,791
Earnings per share:				
Basic:	\$ 1.21	\$ 0.53	\$ 3.27	\$ 1.36
Diluted	\$ 1.13	\$ 0.51	\$ 3.04	\$ 1.30

*The accompanying notes are an integral part of the condensed consolidated financial statements.*

**Table of Contents**

**WESCO INTERNATIONAL, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(unaudited)

<i>Amounts in thousands</i>	<b>Nine Months Ended September 30,</b>	
	<b>2006</b>	<b>2005</b>
<b>Operating Activities:</b>		
Net income	\$ 159,013	\$ 63,791
Adjustments to reconcile net income to net cash provided by operating activities:		
Loss on debt extinguishment (excluding premium of \$8,168 in 2005)		1,883
Depreciation and amortization	19,249	11,330
Accretion of original issue and amortization of purchase discounts		873
Amortization of debt issuance costs	1,677	744
Deferred income taxes	143	6,360
Amortization of gain on interest rate swap		(684)
Stock-based compensation expense	8,487	5,586
Loss (gain) on the sale of property, buildings and equipment	(3,328)	(29)
Excess tax benefit from stock-based compensation ( <b>Note 3</b> )	(26,741)	
Changes in assets and liabilities		
Change in receivables facility	(82,000)	102,000
Trade and other receivables	(54,562)	(110,531)
Inventories	(38,704)	(14,326)
Prepaid expenses and other current assets	37,748	2,726
Accounts payable	30,494	98,441
Accrued payroll and benefit costs	98	(7,292)
Other current and noncurrent liabilities	13,496	5,185
Net cash provided by operating activities	65,070	166,114
<b>Investing Activities:</b>		
Capital expenditures	(14,872)	(10,997)
Acquisition payments	(10,872)	(278,270)
Proceeds from sale of building	4,500	
Other investing activities	(337)	1,192
Net cash used by investing activities	(21,581)	(288,075)
<b>Financing Activities:</b>		
Proceeds from issuance of long-term debt	265,404	471,000
Repayments of long-term debt	(315,358)	(321,278)
Debt issuance costs	(564)	(7,844)
Proceeds from the exercise of stock options	6,496	6,003
Excess tax benefit from stock-based compensation ( <b>Note 3</b> )	26,741	
Increase in bank overdrafts	13,428	
Real estate defeasance	(1,692)	
Payments on capital lease obligations	(778)	

Net cash (used) provided by financing activities	(6,323)	147,881
Effect of exchange rate changes on cash and cash equivalents	(18)	423
Net change in cash and cash equivalents	37,148	26,343
Cash and cash equivalents at the beginning of period	22,125	34,523
Cash and cash equivalents at the end of period	\$ 59,273	\$ 60,866

**Supplemental disclosures:**

Non-cash investing activities:

Property, plant and equipment acquired through capital leases \$ 1,438

Increase in deferred acquisition payable 500

Non-cash financing activities:

Decrease in fair value of outstanding interest rate swaps \$ 1,223

Note payable issued in connection with acquisition 3,000

*The accompanying notes are an integral part of the condensed consolidated financial statements.*



**Table of Contents**

**WESCO INTERNATIONAL, INC. AND SUBSIDIARIES**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
(unaudited)

**1. ORGANIZATION**

WESCO International, Inc. and its subsidiaries (collectively, WESCO ), headquartered in Pittsburgh, Pennsylvania, are a full-line distributor of electrical supplies and equipment and are a provider of integrated supply procurement services with operations in the United States, Canada, Mexico, Puerto Rico, Guam, the United Kingdom, Nigeria, United Arab Emirates and Singapore. WESCO currently operates approximately 365 branch locations and seven distribution centers (five in the United States and two in Canada.)

**2. ACCOUNTING POLICIES**

*Basis of Presentation*

The unaudited condensed consolidated financial statements of WESCO have been prepared in accordance with Rule 10-01 of Regulation S-X of the Securities and Exchange Commission (the SEC ). The unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in WESCO 's 2005 Annual Report on Form 10-K filed with the SEC. The December 31, 2005 condensed balance sheet data was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America.

The unaudited condensed consolidated balance sheet as of September 30, 2006, the unaudited condensed consolidated statements of income for the three months and nine months ended September 30, 2006 and 2005, respectively, and the unaudited condensed consolidated statements of cash flows for the nine months ended September 30, 2006 and 2005, respectively, in the opinion of management, have been prepared on the same basis as the audited consolidated financial statements and include all adjustments necessary for the fair statement of the results of the interim periods. All adjustments reflected in the unaudited condensed consolidated financial statements are of a normal recurring nature unless indicated. Results for the interim periods presented are not necessarily indicative of the results to be expected for the full year.

*Recent Accounting Pronouncements*

In March 2006, the FASB issued SFAS No. 156, *Accounting for Servicing of Financial Assets-an amendment of FASB Statement No. 140* ( SFAS 156 ) which amends FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, with respect to the accounting for separately recognized servicing assets and servicing liabilities. This statement clarifies when servicing rights should be separately accounted for, requires companies to account for separately recognized servicing rights initially at fair value, and gives companies the option of subsequently accounting for those servicing rights at either fair value or under the amortization method. SFAS 156 is effective for fiscal years beginning after September 15, 2006. Consistent with its requirements, WESCO will adopt SFAS 156 on January 1, 2007. WESCO does not anticipate that the adoption of SFAS 156 will have a material impact on its financial position, results of operations and cash flows.

In July 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109* ( FIN 48 ) which clarifies the accounting for uncertainty in income taxes recognized in an entity 's financial statements in accordance with SFAS No. 109, *Accounting for Income Taxes*. It prescribes a recognition threshold and measurement attribute for financial statement disclosure of tax positions taken or expected to be taken on a tax return. FIN 48 is effective for fiscal years beginning after December 15, 2006. Consistent with its requirements, WESCO will adopt FIN 48 on January 1, 2007. WESCO is currently evaluating the effect that implementation of FIN 48 will have on its financial position, results of operations and cash flows.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* ( SFAS 157 ) which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS 157 is effective for fiscal years beginning after November 15, 2007. WESCO is currently evaluating the effect that implementation of SFAS 157 will have on its financial position, results of operations, and cash flows.

**3. STOCK-BASED COMPENSATION**

WESCO has sponsored four stock option plans: the 1999 Long-Term Incentive Plan ( LTIP ), the 1998 Stock Option Plan, the Stock Option Plan for Branch Employees and the 1994 Stock Option Plan. The LTIP was designed to be the successor plan to all prior plans.

**Table of Contents**

Outstanding options under prior plans will continue to be governed by their existing terms, which are substantially similar to the LTIP. Any remaining shares reserved for future issuance under the prior plans are available for issuance under the LTIP. The LTIP and predecessor plans are administered by the Compensation Committee of the Board of Directors.

An initial reserve of 6,936,000 shares of common stock has been authorized for issuance under the LTIP. This reserve automatically increases by (i) the number of shares of common stock covered by unexercised options granted under prior plans that are canceled or terminated after the effective date of the LTIP, and (ii) the number of shares of common stock surrendered by employees to pay the exercise price and/or minimum withholding taxes in connection with the exercise of stock options granted under our prior plans. All awards under WESCO's stock incentive plans are designed to be issued at fair market value.

Awards granted vest and become exercisable once criteria based on time or financial performance are achieved. If the financial performance criteria are not met, all the awards will vest after nine years and nine months. All awards vest immediately in the event of a change in control. Each award terminates on the tenth anniversary of its grant date unless terminated sooner under certain conditions.

Beginning January 1, 2006, WESCO adopted the provisions of SFAS No. 123 (revised 2004) ( SFAS 123R ), *Share-Based Payment* and SEC Staff Accounting Bulletin No. 107 ( SAB 107 ), *Share-Based Payment*, requiring the measurement and recognition of all stock-based compensation under the fair value method.

During the year ended December 31, 2003, WESCO adopted the measurement provisions of SFAS No. 123 ( SFAS 123 ), *Accounting for Stock-Based Compensation*. Stock options awarded prior to 2003 were accounted for under the intrinsic value method (i.e. the difference between the market price on the exercise date and the price paid by the employee to exercise the options) under Accounting Principles Board Opinion No. 25 ( APB 25 ), *Accounting for Stock Issued to Employees*. Beginning January 1, 2006, WESCO adopted SFAS 123R using the modified prospective method, which requires measurement of compensation cost for all stock-based awards at fair value on date of grant and recognition of compensation cost, net of estimated forfeitures, over the service period for awards expected to vest. The fair value of stock-based awards is determined using the Black-Scholes valuation model, which is consistent with the valuation techniques previously utilized for stock-based awards in footnote disclosures required under SFAS 123. The forfeiture assumption is 5% per year and is based on WESCO's historical employee behavior that is reviewed on an annual basis. No dividends are assumed.

Prior to the adoption of SFAS 123R, WESCO presented all tax benefits of deductions resulting from the exercise of stock options as operating cash flows in the Consolidated Statements of Cash Flows. SFAS 123R requires the tax benefits resulting from deductions in excess of the compensation cost recognized for those options ( excess tax benefits ) to be classified as financing cash flows.

WESCO recognized \$3.4 million and \$2.5 million of non-cash stock-based compensation expense, which is included in selling, general and administrative expenses, for the three months ended September 30, 2006 and 2005, respectively. WESCO recognized \$8.5 million (including \$0.1 million due to the adoption of SFAS 123R and related to the vesting in 2006 of options granted prior to January 1, 2003) and \$5.7 million of non-cash stock-based compensation expense, which is included in selling, general and administrative expenses, for the nine months ended September 30, 2006 and 2005, respectively.

During the three months ended September 30, 2006 and 2005 and the nine months ended September 30, 2006 and 2005, WESCO granted the following stock-settled appreciation rights at the following weighted average assumptions:

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Stock-settled appreciation rights granted	457,750	888,500	463,132	892,200
Risk free interest rate	4.9	3.0%	4.9%	3.0%
Expected life	4 years	4 years	4 years	4 years
Expected volatility	50%	59%	50%	59%

Edgar Filing: WESCO INTERNATIONAL INC - Form 10-Q

As of September 30, 2006, there was \$23.5 million of total unrecognized compensation expense related to non-vested stock-based compensation arrangements for all awards previously made of which approximately \$3.2 million is expected to be recognized over the remainder of 2006, \$11.7 million is expected to be recognized in 2007, \$6.5 million in 2008 and \$2.1 million in 2009.

**Table of Contents**

During the nine months ended September 30, 2006 and 2005, the total intrinsic value of options exercised was \$78.9 million and \$13.5 million, respectively, and the total amount of cash received from the exercise of these options was \$12.9 million and \$6.2 million, respectively. The tax benefit recorded for tax deductions associated with stock-based compensation plans for the nine months ended September 30, 2006 and 2005 totaled \$27.1 million and \$8.0 million, respectively, and was recorded as a credit to additional paid-in capital.

The following table sets forth a summary of both stock options and stock appreciation rights and related information for the nine months ended September 30, 2006:

	<b>Awards</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Remaining Contractual Life</b>
Outstanding at December 31, 2005	6,303,936	\$ 14.02	5.9
Granted	466,732	\$68.84	
Exercised	1,527,560	\$ 11.13	
Forfeited	66,333	\$ 19.13	
Outstanding at September 30, 2006	5,176,775	\$ 19.71	6.0
Exercisable at September 30, 2006	2,134,626	\$ 14.28	6.0
Unvested at September 30, 2006	3,042,149	\$ 23.52	6.0

As of September 30, 2006, the intrinsic value of awards exercisable and awards unvested was \$30.5 million and \$71.6 million, respectively.

As of September 30, 2006, 4.3 million shares of common stock were reserved under the 1999 Long Term Incentive Plan for future equity award grants.

The following table sets forth exercise prices for equity awards outstanding as of September 30, 2006:

	<b>Awards Outstanding</b>	<b>Awards Exercisable</b>	<b>Weighted Average Remaining Contractual Life</b>
Range of exercise price			
\$ 0.00 - \$10.00	1,843,216	1,052,532	5.3
\$10.00 - \$20.00	1,365,025	445,942	2.8
\$20.00 - \$30.00	678,960	409,129	8.0
\$30.00 - \$40.00	811,653	227,023	8.8
\$40.00 - \$50.00	17,139	0	9.2
\$50.00 - \$60.00	2,650	0	9.4
\$60.00 - \$70.00	458,132	0	9.8
	5,176,775	2,134,626	6.0

For the three months ending September 30, 2005 and the nine months ending September 30, 2005, WESCO's pro forma net income and earnings per share would have been adjusted to the amounts indicated below to reflect the additional fair value compensation, net of tax, as if the fair-value based method of accounting for stock-based awards had been applied to all outstanding awards:

	<b>Three Months Ended September 30, 2005</b>	<b>Nine Months Ended September 30, 2005</b>
<i>Amounts in thousands, except per share amounts</i>		
Net income reported	\$ 25,008	\$ 63,791
Add: Stock-based compensation expense included in reported net income, net of related tax	1,624	3,704
Deduct: Stock based employee compensation expense determined under fair value based methods for all awards, net of related tax	1,715	3,886
Pro forma net income	\$ 24,917	\$ 63,609
Earnings per share:		
Basic as reported	\$ 0.53	\$ 1.36
	<b>Three Months Ended September 30, 2005</b>	<b>Nine Months Ended September 30, 2005</b>
<i>Amounts in thousands, except per share amounts</i>		
Basic pro forma	\$ 0.53	\$ 1.35
Diluted as reported	\$ 0.51	\$ 1.30
Diluted pro forma	\$ 0.50	\$ 1.29

**Table of Contents****4. EARNINGS PER SHARE**

The following table sets forth the details of basic and diluted earnings per share:

<i>Amounts in thousands, except per share amounts</i>	<b>Three Months Ended September 30,</b>	
	<b>2006</b>	<b>2005</b>
Net income reported	\$ 59,385	\$ 25,008
Weighted average common shares outstanding used in computing basic earnings per share	48,971,225	47,170,417
Common shares issuable upon exercise of dilutive stock options	2,412,261	2,262,767
Common shares issuable from contingently convertible debentures (see note below for basis of calculation)	1,118,928	
Weighted average common shares outstanding and common share equivalents used in computing diluted earnings per share	52,502,414	49,433,184
Earnings per share:		
Basic	\$ 1.21	\$ 0.53
Diluted	\$ 1.13	\$ 0.51

<i>Amounts in thousands, except per share amounts</i>	<b>Nine Months Ended September 30,</b>	
	<b>2006</b>	<b>2005</b>
Net income reported	\$ 159,013	\$ 63,791
Weighted average common shares outstanding used in computing basic earnings per share	48,549,104	46,950,762
Common shares issuable upon exercise of dilutive stock options	2,610,185	2,190,755
Common shares issuable from contingently convertible debentures (see note below for basis of calculation)	1,130,119	
Weighted average common shares outstanding and common share equivalents used in computing diluted earnings per share	52,289,408	49,141,517
Earnings per share:		
Basic	\$ 3.27	\$ 1.36
Diluted	\$ 3.04	\$ 1.30

Stock-settled stock appreciation rights to purchase 0.1 million and 1.7 million shares of common stock at a weighted average exercise price of \$60.87 and \$28.00 per share that were outstanding as of September 30, 2006 and 2005, respectively, were not included in the computation of diluted earnings per share because to do so would have been antidilutive for the three- and nine-month periods ending September 30, 2006 and 2005. In addition, to the extent that the average share price during the three-month or year-to-date periods ending September 30, 2006 exceeds the 2.625% Convertible Senior Debentures due 2025 (the 2025 Debentures) conversion price of \$41.86 per share, an incremental number of up to 3,583,080 shares are to be included in determining diluted earnings per share using the treasury stock method of accounting as represented in the table below. Since the average stock price for the three-month and nine-month periods ended September 30, 2006 was approximately \$61 per share, 1,118,928 shares

and 1,130,119 shares, respectively, underlying the 2025 Debentures were included in the diluted weighted average shares outstanding for the three-month and nine-month periods ended September 30, 2006, under the treasury stock method of accounting, as required by the FASB Emerging Issues Task Force ( EITF ) Issue No. 90-19, *Convertible Bonds with Issuer Option to Settle for Cash upon Conversion ( EITF 90-19 )*.

Under EITF Issue No. 04-8 *The Effect of Contingently Convertible Instruments on Diluted Earnings Per Share*, and EITF 90-19, and because of WESCO's obligation to settle the par value of the 2025 Debentures in cash, WESCO is not required to include any shares underlying the 2025 Debentures in its diluted weighted average shares outstanding until the average stock price per share for the three- and nine-month periods ending September 30, 2006 exceeds the \$41.86 conversion price and only to the extent of the additional shares WESCO may be required to issue in the event WESCO's conversion obligation exceeds the principal amount of the 2025 Debentures converted. At such time, only the number of shares that would be issuable (under the treasury stock method of accounting for share dilution) will be included, which is based upon the amount by which the average stock price exceeds the conversion price. For the first \$1 per share that WESCO's average stock price exceeds the \$41.86 conversion price of the 2025 Debentures, WESCO will include approximately 83,000 additional



**Table of Contents**

shares in WESCO's diluted share count. For the second \$1 per share that WESCO's average stock price exceeds the \$41.86 conversion price, WESCO will include approximately 80,000 additional shares, for a total of approximately 163,000 shares, in WESCO's diluted share count, and so on, with the additional shares' dilution decreasing for each \$1 per share that WESCO's average stock price exceeds \$41.86 if the stock price rises further above \$41.86 (see table, below).

**TREASURY STOCK METHOD OF ACCOUNTING FOR SHARE DILUTION**

<b>Conversion Price:</b>	<b>\$ 41.86</b>
<b>Number of Underlying Shares:</b>	<b>0 to 3,583,080</b>
<b>Principal Amount</b>	<b>\$ 150,000,000</b>

**Formula:** Number of extra dilutive shares created  

$$= ((\text{Stock Price} * \text{Underlying Shares}) - \text{Principal}) / \text{Stock Price}$$

**Condition:** Only applies when share price exceeds \$41.86

<b>Stock Price</b>	<b>Conversion Price</b>	<b>Price Difference</b>	<b>Include in Share Count</b>	<b>Share Dilution Per \$1.00 Share Price Difference</b>
\$41.86	\$41.86	\$ 0	0	0
\$42.86	\$41.86	\$ 1	83,313	83,313
\$51.86	\$41.86	\$ 10	690,677	69,068
\$61.86	\$41.86	\$ 20	1,158,249	57,912
\$71.86	\$41.86	\$ 30	1,495,687	49,856
\$81.86	\$41.86	\$ 40	1,750,683	43,767

Share dilution is limited to a maximum of 3,583,080 shares.

**5. ACCOUNTS RECEIVABLE SECURITIZATION**

WESCO maintains an accounts receivable securitization program (the "Receivables Facility") that had a total purchase commitment of \$400 million as of September 30, 2006 and December 31, 2005. The Receivables Facility has a term of three years and is subject to renewal in May 2008. Under the Receivables Facility, WESCO sells, on a continuous basis, an undivided interest in all domestic accounts receivable to WESCO Receivables Corporation, a wholly owned, special purpose entity ("SPE"). The SPE sells, without recourse, to a third-party conduit all the eligible receivables while maintaining a subordinated interest, in the form of overcollateralization, in a portion of the receivables. WESCO has agreed to continue servicing the sold receivables for the financial institution at market rates; accordingly, no servicing asset or liability has been recorded.

As of September 30, 2006 and December 31, 2005, accounts receivable eligible for securitization totaled approximately \$534 million and \$525 million, respectively, of which the subordinated retained interest was approximately \$219 million and \$128 million, respectively. Accordingly, approximately \$315 million and \$397 million of accounts receivable balances were removed from the consolidated balance sheets at September 30, 2006 and December 31, 2005, respectively. Costs associated with the Receivables Facility totaled \$5.8 million and \$3.8 million for the three months ended September 30, 2006 and September 30, 2005, respectively. Costs associated with the Receivables Facility totaled \$17.1 million and \$8.8 million for the nine months ended September 30, 2006 and September 30, 2005, respectively. These amounts are recorded as other expenses in the consolidated statements of income and are primarily related to interest and the discount and loss on the sale of accounts receivables, partially offset by related servicing revenue.

The key economic assumptions used to measure the retained interest at the date of the securitization for securitizations completed in 2006 were a discount rate of 4.6% and an estimated life of 1.5 months. At September 30, 2006, an immediate adverse change in the discount rate or estimated life of 10% and 20% would result in a reduction

in the fair value of the retained interest of \$0.3 million and \$0.6 million, respectively. These sensitivities are hypothetical and should be used with caution. Changes in fair value based on a 10% variation in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, in this example, the effect of a variation in a particular assumption on the fair value of the retained interest is calculated without changing any other assumption. In reality, changes in one factor may result in changes in another.

**Table of Contents****6. ACQUISITIONS**

Acquisitions were accounted for under the purchase method of accounting in accordance with SFAS No. 141, *Business Combinations*. Accordingly, the purchase price has been allocated based on an independent appraisal of the fair value of intangible assets and management's estimate of the fair value of tangible assets acquired and liabilities assumed with the excess being recorded primarily as goodwill as of the effective date of the acquisition.

The allocation of assets acquired and liabilities assumed for the 2005 acquisitions is summarized below.

<i>Amounts in thousands</i>	<b>Fastec Industrial Corp.</b>	<b>Carlton-Bates Company</b>
Assets Acquired		
Cash and equivalents	\$ 281	\$ 1,763
Trade accounts receivable	4,675	37,628
Inventories	11,944	40,709
Deferred income taxes short-term		2,128
Other accounts receivable		840
Prepaid expenses	161	762
Income taxes receivable		2,789
Property, buildings and equipment	2,168	5,159
Intangible assets	11,134	74,444
Goodwill	5,422	137,589
Total assets acquired	35,785	303,811
Liabilities Assumed		
Accounts payable	2,663	16,901
Accrued and other current liabilities	767	9,275
Deferred income taxes long-term		19,607
Other noncurrent liabilities		136
Total liabilities assumed	3,430	45,919
Fair value of net assets acquired, including intangible assets	\$ 32,355	\$ 257,892

**Acquisition of Carlton-Bates Company**

On September 29, 2005, WESCO acquired Carlton-Bates Company ( Carlton-Bates ), headquartered in Little Rock, Arkansas. The original purchase price was \$248.5 million, net of \$1.8 million cash acquired, of which \$25.0 million of the purchase price was held in escrow to address up to \$5.0 million of post-closing adjustments relating to working capital and up to \$20.0 million of potential indemnification claims, with all distributions from the escrow to be made by March 2008. Distributions of \$2.0 million and \$3.0 million were made from the escrow in November 2005 and February 2006, respectively, in accordance with terms set forth in the purchase agreement. During the three months ended March 31, 2006, WESCO completed its evaluation of the calculation of the acquired working capital resulting in an increase in the purchase price in the amount of \$5.5 million which amount was paid on April 6, 2006.

Carlton-Bates operates as a traditional branch-based distributor and includes its LADD division, the sole U.S. distributor of engineered connecting devices for the industrial products division of Deutsch Company ECD. Carlton-Bates is a regional distributor of electrical and electronic components with a special emphasis on automation

and electromechanical applications for the original equipment manufacturer markets. Carlton-Bates adds new capabilities for WESCO including new product categories, new supplier relationships, kitting and light assembly services for WESCO customers and sales opportunities resulting from value-added services.

The purchase price allocation resulted in intangible assets of \$74.4 million and goodwill of \$137.6 million, of which \$58.4 million is deductible for tax purposes. The intangible assets include customer relationships of \$45.3 million amortized over a range of 13 to 19 years, distribution agreements of \$12.0 million and non-compete agreements of \$0.2 million, both of which are amortized over five years, and trademarks of \$16.9 million. Trademarks have an indefinite life and are not being amortized. The intangible assets were valued by American Appraisal Associates, Inc., an independent appraiser. No residual value is estimated for these intangible assets.

**Table of Contents**

The operating results of Carlton-Bates have been included in WESCO's consolidated financial statements since September 29, 2005. The following summary of the unaudited pro forma results of operations for the three months ended September 30, 2005 and nine months ended September 30, 2005 is included below as if the acquisition occurred on the first day of 2005 and is not necessarily indicative of what WESCO's results of operations would have been had Carlton-Bates been acquired at the beginning of the period. Seasonality of sales is not a significant factor to the pro forma combined results of operations.

<i>Amounts in thousands, except per share amounts</i>	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2005
Net Sales	\$ 1,209,021	\$ 3,414,065
Net Income	\$ 24,221	\$ 69,429
Earnings per common share:		
Basic	\$ 0.51	\$ 1.48
Diluted	\$ 0.49	\$ 1.41

As part of the acquisition of Carlton-Bates, WESCO developed a plan for the integration of Carlton-Bates into the WESCO operations. This plan was finalized during the three-month period ending September 30, 2006. Pursuant to EITF Issue No. 95-3, *Recognition of Liabilities in Connection with a Purchase Business Combination*, all certain charges related to the Carlton-Bates acquisition integration within one year of the date of acquisition have been recognized as a part of the purchase price allocation. A summary of these charges for the three-month period ending September 30, 2006 is as follows:

<i>Amounts in thousands</i>	Balance at June 30, 2006	Cash Payments	Adjustments	Balance at September 30, 2006
Termination Benefits	\$ 25	\$ 81	\$ 125	\$ 69
Cost of closing redundant facilities	\$ 2,204	\$ 180	\$ (604)	\$ 1,420
Other	\$ 277	\$ 291	\$ 118	\$ 104
Total	\$ 2,506	\$ 552	\$ (361)	\$ 1,593

**Acquisition of Fastec Industrial Corp.**

On July 29, 2005, WESCO acquired the assets and business of Fastec Industrial Corp. (Fastec Industrial). Fastec Industrial was a nationwide importer and distributor of industrial fasteners, cabinet and locking and latching products. The original purchase price WESCO paid was \$28.7 million, net of \$0.3 million cash acquired, and WESCO also issued a \$3.0 million promissory note to consummate this acquisition. In accordance with the terms of the purchase, a net working capital valuation was performed subsequent to the closing date of the acquisition, resulting in an increase to the purchase price and the note payable in the amount of \$0.3 million.

The purchase price allocation resulted in intangible assets of \$11.1 million and goodwill of \$5.4 million, which is expected to be fully deductible for tax purposes. The intangible assets include customer relationships of \$9.4 million, trademarks of \$1.5 million and non-compete agreements of \$0.2 million. Trademarks have an indefinite life and are not being amortized. Non-compete agreements are being amortized over five years and customer relationships over 15 years. The intangible assets were valued by American Appraisal Associates, Inc., an independent appraiser. No residual value is estimated for the intangible assets.

The operating results of Fastec Industrial have been included in WESCO's operating results since July 29, 2005. Pro forma comparative results of WESCO, assuming the acquisition of Fastec Industrial had been made at the beginning of fiscal 2005, would not have been materially different from the reported results or the pro forma results presented above.

Other Acquisition

Another previously completed acquisition agreement contains contingent consideration for the final acquisition payment which management has estimated to be \$5.0 million. During the three months ended June 30, 2006, \$3.9 million was paid, with the estimated remaining \$1.1 million is to be paid during 2007, and is reported as deferred acquisition payable.

**Table of Contents**

**7. EMPLOYEE BENEFIT PLANS**

A majority of WESCO's employees are covered by defined contribution retirement savings plans for their services rendered subsequent to WESCO's formation. For U.S. participants, WESCO will make contributions in an amount equal to 50% of the participant's total monthly contributions up to a maximum of 6% of eligible compensation. For Canadian participants, WESCO will make contributions in an amount ranging from 1% to 7% of the participant's eligible compensation based on years of continuous service. In addition, employer contributions may be made at the discretion of the Board of Directors. For the nine months ended September 30, 2006 WESCO contributed \$16.3 million to all such plans. Contributions are made in cash to employee retirement savings plan accounts. Employees then have the option to transfer balances allocated to their accounts into any of the available investment options, including WESCO stock.

**8. COMMITMENTS AND CONTINGENCIES**

WESCO is a defendant in a lawsuit in a state court in Florida in which a former supplier alleges that WESCO failed to fulfill its commercial obligations to purchase product and seeks monetary damages in excess of \$17 million. WESCO believes that it has meritorious defenses. Neither the outcome nor the monetary impact of this litigation can be predicted at this time. A trial is scheduled for March 2007.

On March 3, 2006, Dana Corporation ( Dana ) and forty of its domestic subsidiaries filed voluntary petitions for reorganization under Chapter 11 of the United States Bankruptcy Code. The Dana petitions applied to its U.S. domestic entities only. Dana represented \$48.5 million of WESCO sales in 2005.

As of March 3, 2006, the amount of accounts receivable due WESCO from Dana's U.S. domestic entities was \$11.1 million, of which \$10.6 million related to 2006 sales. As of June 30, 2006, a reserve in the amount of \$2.0 million was maintained by WESCO based on management's evaluation of the collectibility of this balance. In September 2006, in accordance with a court approved settlement, WESCO sold \$10.8 million of the \$11.1 million Dana accounts receivable, resulting in a loss of \$1.7 million. As of September 30, 2006, the remaining \$0.3 million Dana pre-petition accounts receivable are fully reserved.

**Table of Contents****9. COMPREHENSIVE INCOME**

The following table sets forth comprehensive income and its components:

<i>Amounts In thousands</i>	<b>Three Months Ended September 30,</b>	
	<b>2006</b>	<b>2005</b>
Net income	\$ 59,385	\$ 25,008
Foreign currency translation adjustment	87	3,401
Comprehensive income	\$ 59,472	\$ 28,409

<i>Amounts In thousands</i>	<b>Nine Months Ended September 30,</b>	
	<b>2006</b>	<b>2005</b>
Net income	\$ 159,013	\$ 63,791
Foreign currency translation adjustment	2,995	2,596
Comprehensive income	\$ 162,008	\$ 66,387

**10. INCOME TAXES**

The following table sets forth the reconciliation between the federal statutory income tax rate and the effective rate:

	<b>Three Months Ended September 30,</b>	
	<b>2006</b>	<b>2005</b>
Federal statutory rate	35.0%	35.0%
State taxes, net of federal tax benefit	3.4	1.8
Nondeductible expenses	0.4	0.8
Domestic tax benefit from foreign operations	(2.8)	(1.9)
Foreign tax rate differences <sup>(1)</sup>	(2.4)	(3.2)
Domestic production activity deduction	(0.1)	
	33.5%	32.5%

	<b>Nine Months Ended September 30,</b>	
	<b>2006</b>	<b>2005</b>
Federal statutory rate	35.0%	35.0%
State taxes, net of federal tax benefit	2.7	1.6
Nondeductible expenses	0.4	0.8
Domestic tax benefit from foreign operations	(2.3)	(1.6)
Foreign tax rate differences <sup>(1)</sup>	(2.7)	(2.9)
Federal tax credits <sup>(2)</sup>		(1.1)
Domestic production activity deduction	(0.1)	
Other	0.1	



33.1%

31.8%

- (1) Includes a benefit of \$2.1 million and \$1.2 million for the three months ended September 30, 2006 and 2005, respectively, and \$6.1 million and \$2.8 million for the nine months ended September 30, 2006 and 2005, respectively, from the recapitalization of our Canadian operations.
- (2) Represents a benefit of \$1 million for the nine months ended September 30, 2005 from research and development credits.

**Table of Contents**

**11. OTHER FINANCIAL INFORMATION (Unaudited)**

WESCO Distribution, Inc. ( WESCO Distribution ) has issued \$150 million in aggregate principal amount of 7.50% Senior Subordinated Notes due 2017 (the 2017 Notes ). The 2017 Notes are fully and unconditionally guaranteed by WESCO International, Inc. ( WESCO International ) on a subordinated basis to all existing and future senior indebtedness of WESCO International. Pursuant to an Exchange and Registration Rights Agreement with respect to the 2017 Notes and WESCO International's guarantee of the 2017 Notes (the 2017 Notes Guarantee ), WESCO International and WESCO Distribution filed a registration statement with the Securities and Exchange Commission to register an exchange enabling holders of the 2017 Notes to exchange the 2017 Notes and 2017 Notes Guarantee for publicly registered senior subordinated notes, and a similar unconditional guarantee of those notes by WESCO International, with substantially identical terms (except for terms relating to additional interest and transfer restrictions). All of the original \$150 million in aggregate principal amount of the 2017 Notes were exchanged in the exchange offer. WESCO International and WESCO Distribution completed the exchange offer on July 12, 2006.

WESCO International has issued \$150 million in aggregate principal amount of 2025 Debentures. The 2025 Debentures are fully and unconditionally guaranteed by WESCO Distribution on a senior subordinated basis to all existing and future senior indebtedness of WESCO Distribution. Pursuant to a Registration Rights Agreement, with respect to the 2025 Debentures, WESCO Distribution's guarantee of the 2025 Debentures (the Debentures Guarantee ) and the common stock of WESCO International into which the 2025 Debentures are convertible (the Conversion Shares ), WESCO Distribution and WESCO International filed a resale shelf registration statement to register the 2025 Debentures, the Debentures Guarantee and the Conversion Shares. The resale shelf registration statement became effective on June 23, 2006.

WESCO Distribution issued \$300 million in aggregate principal amount of 9 1/8% Senior Subordinated Notes due 2008 (the 2008 Notes ) in June 1998 and \$100 million in aggregate principal amount of the 2008 Notes in August 2001 and repurchased all amounts outstanding during 2005, 2004 and 2003. There was no outstanding balance remaining related to the 2008 Notes as of December 31, 2005. The 2008 Notes were fully and unconditionally guaranteed by WESCO International on a subordinated basis.

Condensed consolidating financial information for WESCO International, WESCO Distribution and the non-guarantor subsidiaries are as follows:

**Table of Contents****WESCO INTERNATIONAL, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATING BALANCE SHEETS****September 30, 2006  
(In thousands)**

	WESCO International, Inc.	WESCO Distribution, Inc.	Non-Guarantor Subsidiaries	Consolidating and Eliminating Entries	Consolidated
Cash and cash equivalents	\$	\$ 26,814	\$ 32,459	\$	\$ 59,273
Trade accounts receivable			460,966		460,966
Inventories		407,419	134,826		542,245
Other current assets	65	30,502	27,161		57,728
Total current assets	65	464,735	655,412		1,120,212
Intercompany receivables, net		(407,211)	388,917	18,294	
Property, buildings and equipment, net		35,022	69,749		104,771
Intangible assets, net		11,538	67,596		79,134
Goodwill and other intangibles, net		374,027	176,311		550,338
Investments in affiliates and other noncurrent assets	826,822	1,125,243	4,385	(1,942,806)	13,644
Total assets	\$826,887	\$1,603,354	\$1,362,370	\$(1,924,512)	\$1,868,099
Accounts payable	\$	\$ 479,171	\$ 126,748	\$	\$ 605,919
Other current liabilities		83,353	45,234		128,587
Total current liabilities		562,524	171,982		734,506
Intercompany payables, net	(18,294)			18,294	
Long-term debt	150,000	152,867	45,949		348,816
Other noncurrent liabilities		64,916	24,680		89,596
Stockholders' equity	695,181	823,047	1,119,759	(1,942,806)	695,181
Total liabilities and stockholders' equity	\$826,887	\$1,603,354	\$1,362,370	\$(1,924,512)	\$1,868,099

**December 31, 2005  
(In thousands)**

	WESCO International, Inc.	WESCO	Non-Guarantor Subsidiaries	Consolidating and Eliminating Entries	Consolidated
--	---------------------------------	-------	-------------------------------	--	--------------

Edgar Filing: WESCO INTERNATIONAL INC - Form 10-Q

		Distribution, Inc.			
Cash and cash equivalents	\$	\$ 18,088	\$ 4,037	\$	\$ 22,125
Trade accounts receivable			315,594		315,594
Inventories		380,227	120,571		500,798
Other current assets		40,049	50,971	(20,674)	70,346
Total current assets		438,364	491,173	(20,674)	908,863
Intercompany receivables, net		(161,534)	206,253	(44,719)	
Property, buildings and equipment, net		31,712	71,371		103,083
Intangible assets, net		11,140	72,752		83,892
Goodwill and other intangibles, net		374,000	168,217		542,217
Investments in affiliates and other noncurrent assets	686,169	806,818	3,045	(1,482,928)	13,104
Total assets	\$686,169	\$1,500,500	\$1,012,811	\$(1,548,321)	\$1,651,159
Accounts payable	\$	\$ 453,101	\$ 119,366	\$	\$ 572,467
Short-term debt		14,500			14,500
Other current liabilities		133,478	20,115	(20,674)	132,919
Total current liabilities		601,079	139,481	(20,674)	719,886
Intercompany payables, net	44,719			(44,719)	
Long-term debt	150,000	154,024	48,208		352,232
Other noncurrent liabilities		63,491	24,100		87,591
Stockholders' equity	491,450	681,906	801,022	(1,482,928)	491,450
Total liabilities and stockholders' equity	\$686,169	\$1,500,500	\$1,012,811	\$(1,548,321)	\$1,651,159

**Table of Contents**

**WESCO INTERNATIONAL, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATING STATEMENTS OF INCOME**

**Three Months Ended September 30, 2006**  
**(In thousands)**

	WESCO International, Inc.	WESCO Distribution, Inc.	Non-Guarantor Subsidiaries	Consolidating and Eliminating Entries	Consolidated
Net sales	\$	\$ 1,056,813	\$ 286,253	\$	\$ 1,343,066
Cost of goods sold		849,990	217,416		1,067,406
Selling, general and administrative expenses	4	121,975	46,851		168,830
Depreciation and amortization		3,236	3,417		6,653
Results of affiliates operations	52,300	15,697		(67,997)	
Interest (income) expense, net	(10,395)	10,138	5,351		5,094
Other expense (income)		13,612	(7,798)		5,814
Provision for income taxes	3,306	21,259	5,319		29,884
Net income	\$ 59,385	\$ 52,300	\$ 15,697	\$(67,997)	\$ 59,385

**Three Months Ended September 30, 2005**  
**(In thousands)**

	WESCO International, Inc.	WESCO Distribution, Inc.	Non-Guarantor Subsidiaries	Consolidating and Eliminating Entries	Consolidated
Net sales	\$	\$ 953,453	\$ 177,996	\$	\$ 1,131,449
Cost of goods sold		780,144	142,992		923,136
Selling, general and administrative expenses	1	149,614	7,685		157,300
Depreciation and amortization		2,960	747		3,707
Results of affiliates operations	21,254	11,345		(32,599)	
Interest (income) expense, net	(6,068)	10,217	2,301		6,450
Other (income) expense		(2,304)	6,100		3,796
Provision for income taxes	2,313	2,913	6,826		12,052
Net income	\$ 25,008	\$ 21,254	\$ 11,345	\$(32,599)	\$ 25,008

**Table of Contents**

**WESCO INTERNATIONAL, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATING STATEMENTS OF INCOME**

**Nine Months Ended September 30, 2006**  
**(In thousands)**

	WESCO International, Inc.	WESCO Distribution, Inc.	Non-Guarantor Subsidiaries	Consolidating and Eliminating Entries	Consolidated
Net sales	\$	\$3,094,241	\$850,309	\$	\$3,944,550
Cost of goods sold		2,496,907	648,324		3,145,231
Selling, general and administrative expenses	7	402,953	105,280		508,240
Depreciation and amortization		9,859	9,390		19,249
Results of affiliates operations	138,146	68,437		(206,583)	
Interest (income) expense, net	(29,283)	29,865	16,518		17,100
Other expense (income)		40,089	(22,952)		17,137
Provision for income taxes	8,409	44,859	25,312		78,580
 Net income	 \$ 159,013	 \$ 138,146	 \$ 68,437	 \$(206,583)	 \$ 159,013

**Nine Months Ended September 30, 2005**  
**(In thousands)**

	WESCO International, Inc.	WESCO Distribution, Inc.	Non-Guarantor Subsidiaries	Consolidating and Eliminating Entries	Consolidated
Net sales	\$	\$2,686,186	\$498,195	\$	\$3,184,381
Cost of goods sold		2,195,597	400,703		2,596,300
Selling, general and administrative expenses	4	395,462	46,502		441,968
Depreciation and amortization		9,217	2,113		11,330
Results of affiliates operations	52,156	32,459		(84,615)	
Interest (income) expense, net	(17,066)	32,765	6,726		22,425
Loss on debt extinguishment		10,051			10,051
Other expense (income)		15,252	(6,438)		8,814
Provision for income taxes	5,427	8,145	16,130		29,702
 Net income	 \$ 63,791	 \$ 52,156	 \$ 32,459	 \$(84,615)	 \$ 63,791

**Table of Contents**

**WESCO INTERNATIONAL, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS**

**Nine Months Ended September 30, 2006**  
**(In thousands)**

	WESCO International, Inc.	WESCO Distribution, Inc.	Non-Guarantor Subsidiaries	Consolidating and Eliminating Entries	Consolidated
Net cash provided (used) by operating activities	\$ 29,776	\$ (1,844)	\$ 37,138	\$	\$ 65,070
Investing activities:					
Capital expenditures		(13,515)	(1,357)		(14,872)
Acquisition payments		(5,372)	(5,500)		(10,872)
Proceeds from sale of building			4,500		4,500
Other		(337)			(337)
Net cash used by investing activities		(19,224)	(2,357)		(21,581)
Financing activities:					
Net borrowings (repayments)	(63,013)	31,136	(4,649)		(36,526)
Equity transactions	33,237				33,237
Real estate defiance			(1,692)		(1,692)
Other		(1,342)			(1,342)
Net cash (used) provided by financing activities	(29,776)	29,794	(6,341)		(6,323)
Effect of exchange rate changes on cash and cash equivalents			(18)		(18)
Net change in cash and cash equivalents		8,726	28,422		37,148
Cash and cash equivalents at the beginning of year		18,088	4,037		22,125
Cash and cash equivalents at the end of period	\$	\$ 26,814	\$ 32,459	\$	\$ 59,273

**Nine Months Ended September 30, 2005**  
**(In thousands)**

	WESCO International, Inc.	WESCO Distribution, Inc.	Non-Guarantor Subsidiaries	Consolidating and Eliminating Entries	Consolidated
	\$ 24,619	\$ 132,619	\$ 8,876	\$	\$ 166,114

Edgar Filing: WESCO INTERNATIONAL INC - Form 10-Q

Net cash provided by operating activities				
Investing activities:				
Capital expenditures		(10,492)	(505)	(10,997)
Acquisitions and other investing activities		(277,078)		(277,078)
Net cash used by investing activities		(287,570)	(505)	(288,075)
Financing activities:				
Net borrowings (repayments)	(26,870)	177,476	(884)	149,722
Equity transactions	6,003			6,003
Debt issuance costs	(3,750)	(3,588)	(506)	(7,844)
Net cash (used) provided by financing activities	(24,617)	173,888	(1,390)	147,881
Effect of exchange rate changes on cash and cash equivalents			423	423
Net change in cash and cash equivalents	2	18,937	7,404	26,343
Cash and cash equivalents at the beginning of year	1	15,974	18,548	34,523
Cash and cash equivalents at the end of period	\$ 3	\$ 34,911	\$ 25,952	\$ 60,866



**Table of Contents****12. SUBSEQUENT EVENTS****1.75% Convertible Senior Debentures due 2026**

On November 2, 2006, WESCO International issued \$300 million in aggregate principal amount of 1.75% Convertible Senior Debentures due 2026 (the 2026 Debentures). The 2026 Debentures were issued by WESCO International under an indenture dated as of November 2, 2006 with The Bank of New York, as Trustee, and are unconditionally guaranteed on an unsecured senior subordinated basis by WESCO Distribution. The 2026 Debentures accrue interest at the rate of 1.75% per annum and are payable in cash semi-annually in arrears on each May 15 and November 15, commencing May 15, 2007. Beginning with the six-month interest period commencing November 15, 2011, WESCO International also will pay contingent interest in cash during any six-month interest period in which the trading price of the 2026 Debentures for each of the five trading days ending on the second trading day immediately preceding the first day of the applicable six-month interest period equals or exceeds 120% of the principal amount of the 2026 Debentures. During any interest period when contingent interest shall be payable, the contingent interest payable per \$1,000 principal amount of 2026 Debentures will equal 0.25% of the average trading price of \$1,000 principal amount of the 2026 Debentures during the five trading days immediately preceding the first day of the applicable six-month interest period.

The 2026 Debentures are convertible into cash and, in certain circumstances, shares of WESCO International's common stock, \$0.01 par value, at any time on or after November 15, 2024, or prior to November 15, 2024 in certain circumstances. The 2026 Debentures will be convertible based on an initial conversion rate of 11.3437 shares of common stock per \$1,000 principal amount of the 2026 Debentures (equivalent to an initial conversion price of approximately \$88.15 per share). The conversion rate and the conversion price may be adjusted under certain circumstances.

At any time on or after November 15, 2011, WESCO International may redeem all or a part of the 2026 Debentures at a redemption price equal to 100% of the principal amount of the 2026 Debentures plus accrued and unpaid interest (including contingent interest and additional interest, if any) to, but not including, the redemption date. Holders of 2026 Debentures may require WESCO International to repurchase all or a portion of their 2026 Debentures on November 15, 2011, November 15, 2016 and November 15, 2021 at a cash repurchase price equal to 100% of the principal amount of the 2026 Debentures, plus accrued and unpaid interest (including contingent interest and additional interest, if any) to, but not including, the repurchase date. If WESCO International undergoes certain fundamental changes prior to maturity, holders of 2026 Debentures will have the right, at their option, to require WESCO International to repurchase for cash some or all of their 2026 Debentures at a repurchase price equal to 100% of the principal amount of the 2026 Debentures being repurchased, plus accrued and unpaid interest (including contingent interest and additional interest, if any) to, but not including, the repurchase date.

**Amended and Restated Revolving Credit Facility**

On November 1, 2006, WESCO Distribution entered into an amended and restated \$440 million revolving credit facility (the Revolving Credit Facility), which includes a letter of credit subfacility of up to \$50 million. The Revolving Credit Facility matures in November 2012 and is collateralized by substantially all assets of WESCO Distribution other than its real property and by substantially all assets of WESCO Distribution Canada, Inc. WESCO Distribution's obligations under the Revolving Credit Facility have been guaranteed by WESCO International and by certain of WESCO Distribution's subsidiaries. The Revolving Credit Facility consists of two separate sub-facilities: (i) a U.S. sub-facility with a borrowing limit of up to \$375 million and (ii) a Canadian sub-facility with a borrowing limit of up to \$65 million. Availability under the Revolving Credit Agreement is limited to the amount of eligible inventory and Canadian inventory and receivables applied against certain advance rates. Interest on the Revolving Credit Facility is at LIBOR plus a margin that will range from 1.00% to 1.75%, depending upon the amount of excess availability under the Revolving Credit Facility.

**Acquisition of Communications Supply**

On November 3, 2006, WESCO International completed its acquisition of Communications Supply Holdings, Inc. (Communications Supply). On that day, a wholly-owned subsidiary of WESCO Distribution merged with and into Communications Supply, which became a wholly-owned subsidiary of WESCO Distribution. The Company paid at closing a cash merger price of approximately \$525 million, of which \$17 million is held in escrow to address

post-closing adjustments relating to working capital and potential indemnification claims, with all amounts in escrow to be eligible for release after January 31, 2008. To fund the merger price paid at closing, WESCO Distribution borrowed \$105 million under its accounts receivable securitization facility and \$102 million under the Revolving Credit Facility together with the net proceeds from the offering of the 2026 Debentures and available cash.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

*The following discussion should be read in conjunction with the information in the unaudited condensed consolidated financial statements and notes thereto included herein and WESCO International Inc.'s Financial Statements and Management's Discussion and Analysis of Financial Condition and Results of Operations included in its 2005 Annual Report on Form 10-K.*

**Company Overview**

We are a full-line distributor of electrical supplies and equipment and a provider of integrated supply procurement services. We have more than 365 full service branches and seven distribution centers located in the United States, Canada, Mexico, Puerto Rico, Guam, the United Kingdom, Nigeria, United Arab Emirates and Singapore. We serve over 100,000 customers worldwide, offering over 1,000,000 products from over 24,000 suppliers. Our diverse customer base includes a wide variety of industrial companies; contractors for industrial, commercial and residential projects; utility companies, and commercial, institutional and governmental customers. Approximately 86% of our net sales are generated from operations in the U.S., 11% from Canada and the remainder from other countries.

Sales increases attributed to growth in our served markets and from the two acquisitions completed in 2005, along with positive impact from our productivity initiatives, contributed to improved financial results for the first nine months of 2006. Sales increased \$760.2 million, or 23.9%, over the same period last year. Gross margin was 20.3% and 18.5% for the first nine months of 2006 and 2005, respectively. During the first nine months of 2006, sales from our acquisitions, both of which were completed in the third quarter of 2005, were \$317.4 million in the aggregate and accounted for 10% of the improved sales versus 2005. Favorable exchange rates accounted for approximately 1% of the higher revenues. The remainder of the 2006 sales increase was the result of a combination of market and share growth, higher commodity prices and hurricane rebuilding activity. Operating income improved by \$137.0 million, or 101.7% primarily from organic growth of the base business along with income from operations acquired in the third quarter of 2005. Operating income improvement was due mainly to sales growth, gross margin expansion, acquisitions, gain on sale of fixed assets and cost containment. The net income for the nine months ending September 30, 2006 and 2005 was \$159.0 million and \$63.8 million, respectively.

**Cash Flow**

We generated \$65.1 million in operating cash flow for the first nine months of 2006. Included in this amount was an \$82 million reduction in the amount outstanding under our accounts receivables securitization facility, whereby we sell, on a continuous basis, an undivided interest in all domestic accounts receivable to WESCO Receivables Corp., a wholly owned, special purpose entity. Investing activities in the first nine months of 2006 included \$14.9 million in capital expenditures and acquisition payments of \$10.9 million. Financing activities during the first nine months of 2006 consisted of borrowings of \$265.4 million related to our revolving credit facility and repayments of \$294.4 million related to our revolving credit facility, \$20 million related to the Bruckner Note Payable and \$0.9 million related our mortgage financing facility.

**Financing Availability**

As of September 30, 2006, we had approximately \$275 million in available borrowing capacity under our revolving credit facility, of which \$225 million is the U.S sub-facility borrowing limit and \$50 million is the Canadian sub-facility borrowing limit.

**Outlook**

We believe that acquisitions and improvements in operations and our capital structure made in 2005 and 2006 have positioned us well for the remainder of 2006. We continue to see macroeconomic data that reflects good activity levels in our major end markets. We continue to focus on selling and marketing initiatives to increase market share and pricing and procurement initiatives to achieve margin expansion and cost containment as we drive towards continued improvement in our operating performance for the last quarter of 2006.

**Critical Accounting Policies and Estimates**

During the first quarter of 2006, we adopted Statement of Financial Accounting Standard No. 123 (revised 2004) ( SFAS 123R ) *Share-Based Payment* which did not have a material impact on our financial position or results of operations and resulted in the reporting of \$26.7 million excess tax benefit being classified as a financing cash inflow in the Consolidated Statements of Cash Flows for the nine months ended September 30, 2006. There were no other

significant changes to our Critical Accounting Policies and Estimates referenced in the 2005 Annual Report on Form 10-K.

**Table of Contents****Results of Operations***Third Quarter of 2006 versus Third Quarter of 2005*

The following table sets forth the percentage relationship to net sales of certain items in our condensed consolidated statements of income for the periods presented:

	<b>Three Months Ended September</b>	
	<b>2006</b>	<b>2005</b>
Net sales	100.0%	100.0%
Gross profit	20.5	18.4
Selling, general and administrative expenses	12.5	13.9
Depreciation and amortization	0.5	0.3
Income from operations	7.5	4.2
Interest expense	0.4	0.6
Other expense	0.5	0.3
Income before income taxes	6.6	3.3
Provision for income taxes	2.2	1.1
Net income	4.4%	2.2%

Sales increases attributed to growth in our markets served and from the two acquisitions completed in 2005, along with positive impact from gross margin improvements and our cost improvement initiatives, contributed to improved financial results for the third quarter of 2006. Net sales in the third quarter of 2006 totaled \$1,343 million versus \$1,131.4 million in the comparable period for 2005, an increase of \$211.6 million or 18.7% over the same period last year. Third quarter 2006 net sales from our acquisitions, both of which were completed in the third quarter of 2005, were \$103.4 million. Favorable exchange rates accounted for approximately 1% of the higher sales. The remainder of the third quarter 2006 sales increase was the result of a combination of market and share growth and higher pricing.

Gross profit for the third quarter of 2006 was \$275.7 million versus \$208.3 million for the comparable period in 2005, and gross margin percentage of net sales was 20.5% in 2006 versus 18.4% in 2005. The increase was attributable primarily to the combination of continued margin improvement initiatives and the higher margins from the acquisitions completed in the second half of 2005.

Selling, general and administrative ( SG&A ) expenses in the third quarter of 2006 totaled \$168.8 million versus \$157.3 million in last year's comparable quarter. As a percentage of net sales, SG&A expenses were 12.5% in the third quarter of 2006 compared to 13.9% in the third quarter in 2005, reflecting the positive impact of cost containment initiatives and the leverage of higher sales volume.

SG&A payroll expenses for the third quarter of 2006 of \$121.6 million increased by \$20.7 million compared to the same quarter in 2005, of which \$9.9 million resulted from the 2005 acquisitions. Of the remaining \$10.8 million increase in payroll expenses, \$10.8 million was from increased salaries and variable commissions and incentive compensation costs resulting from increased sales and related gross margins, \$0.9 million was from increased stock option expense, and \$0.9 million was from decreased other SG&A related payroll expenses.

The remaining SG&A expenses for the third quarter of 2006 of \$47.2 million decreased by approximately \$9.2 million compared to same quarter in 2005. Contributing to the decrease in the SG&A expenses for the third quarter of 2006 compared to the same period in 2005 was the decrease of \$9.0 million in expenses related to a legal settlement and associated litigation expenses in 2005 that were not incurred in 2006. Further, the decrease in SG&A expenses during the third quarter of 2006 resulted from a gain in the amount of \$3.4 million from the sale of a property. SG&A expenses in the third quarter of 2006 increased by \$4.2 million resulting from the 2005 acquisitions.

Other SG&A expenses in the third quarter of 2006 netted to a decrease of \$1.0 million.

Depreciation and amortization for the third quarter of 2006 was \$6.7 million versus \$3.7 million in last year's comparable quarter. Of the \$3.0 million increase, \$2.3 million is related to the two acquisitions in 2005, of which \$1.5 million is due to the amortization expense of the intangible assets acquired and \$0.8 million is due to the depreciation of the fixed assets acquired.

Interest expense totaled \$5.1 million for the third quarter of 2006 versus \$6.5 million in last year's comparable quarter, a decrease of 21.5%. This decrease was due primarily to lower interest on debt in 2006 resulting from the redemption of higher interest rate notes, which were replaced with lower interest rates on both the 2017 Notes and the 2025 Debentures.

**Table of Contents**

Other expense during the third quarter of 2006 increased to \$5.8 million versus \$3.8 million in 2005, reflecting costs associated with the accounts receivables securitization facility resulting from an increase in the average of the accounts receivable sold for the third quarter of 2006 to \$358.3 million versus \$336.7 million in last year's comparable quarter and higher discount rates.

Income tax expense totaled \$29.9 million in the third quarter of 2006 and the effective tax rate was 33.5% compared to 32.5% in the same quarter in 2005. The current quarter's effective tax rate differed from the statutory rate primarily as a result of the domestic tax benefit from foreign operations and from the increase in state taxes in 2006 as compared to 2005.

For the third quarter of 2006, net income increased by \$34.4 million to \$59.4 million, or \$1.13 per diluted share, compared with \$25 million and \$0.51 per diluted share for the third quarter of 2005. The increase in net income was primarily attributable to increased sales, gross margin expansion, decreases in the SG&A expenses as a percent of net sales, decrease in interest expense and increases in depreciation and amortization and other expense and an increase in the effective tax rate of 1%.

*Nine Months Ended September 30, 2006 versus Nine Months Ended September 30, 2005*

The following table sets forth the percentage relationship to net sales of certain items in our condensed consolidated statements of income for the periods presented:

	<b>Nine Months Ended September 30,</b>	
	<b>2006</b>	<b>2005</b>
Net sales	100.0%	100.0%
Gross profit	20.3	18.5
Selling, general and administrative expenses	12.9	13.9
Depreciation and amortization	0.5	0.4
Income from operations	6.9	4.2
Interest expense	0.5	0.7
Loss on debt extinguishment		0.3
Other expense	0.4	0.3
Income before income taxes	6.0	2.9
Provision for income taxes	2.0	0.9
Net income	4.0%	2.0%

Sales increases attributed to growth in our markets served and from the two acquisitions completed in 2005, along with positive impact from gross margin improvements and our cost improvement initiatives, contributed to improved financial results for the first nine months of 2006. Net sales in the first nine months of 2006 totaled \$3,944.6 million versus \$3,184.4 million in the comparable period for 2005, an increase of \$760.2 million, or 23.9%, over the same period last year. First nine months 2006 sales from our acquisitions, both of which were completed in the third quarter of 2005, were \$317.4 million in the aggregate. Favorable exchange rates accounted for approximately 1% of the higher sales. The remainder of the 2006 sales increase was the result of a combination of market and share growth, higher pricing and hurricane rebuilding activity.

Gross profit for the first nine months of 2006 was \$799.3 million versus \$588.1 million for the comparable period in 2005, and gross margin percentage of net sales was 20.3% in 2006 versus 18.5% in 2005. The increase was attributable primarily to the combination of continued margin improvement initiatives and the higher margins from the acquisitions completed in the second half of 2005.

SG&A expenses in the first nine months of 2006 totaled \$508.2 million versus \$442 million in last year's comparable period. As a percentage of net sales, SG&A expenses were 12.9% in the first nine months of 2006 compared to 13.9% in the first nine months of 2005, reflecting the positive impact of cost containment initiatives and the leverage of higher sales volume.

SG&A payroll expenses for the first nine months of 2006 of \$360.6 million increased by \$67.6 million compared to the same period in 2005, of which \$32.5 million resulted from the 2005 acquisitions. Of the remaining \$35.1 million increase in payroll expenses, \$28.1 million was from increased salaries and variable commissions and incentive compensation costs resulting from increased sales and related gross margins, \$1.9 million was from increased employee benefit costs, \$2.3 million from other SG&A payroll related expenses, and \$2.8 million was from increased stock option expense (\$.1 million attributable to the implementation of SFAS 123R).



**Table of Contents**

The remaining SG&A expenses for the first nine months of 2006 of \$147.6 million decreased by approximately \$1.3 million compared to same period in 2005. Contributing to the decrease in the SG&A expenses for the first nine months of 2006 compared to the same period in 2005 was the net decrease of \$7.3 million (\$9.9 million in expenses reduced by \$2.6 million from the settlement of a related insurance claim) in expenses related to a legal settlement and associated litigation expenses in 2005 that were not incurred in 2006. Further, the decrease in the SG&A expenses during the first nine months of 2006 resulted from a gain in the amount of \$3.4 million from the sale of a property. Other SG&A expenses for the first nine months of 2006 increased by \$15.0 million resulting from the 2005 acquisitions and an increase of \$2.0 million in bad debt expense related to the write-down of accounts receivable from a major customer which filed for bankruptcy in the first three months of 2006.

Depreciation and amortization for first nine months of 2006 was \$19.2 million versus \$11.3 million in last year's comparable period. Of the \$7.9 million increase, \$7.2 million is related to the two acquisitions in 2005, of which \$5.2 million is due to the amortization expense of the intangible assets acquired and \$2.0 million is due to the depreciation of the fixed assets acquired.

Interest expense totaled \$17.1 million for the first nine months of 2006 versus \$22.4 million in last year's comparable period, a decrease of 23.7%. This decrease was due primarily to lower interest on debt in 2006 resulting from the redemption of higher interest rate notes, which were replaced with lower interest rates on both the 2017 Notes and the 2025 Debentures.

On March 1, 2005, we redeemed \$123.8 million in aggregate principal amount of our 9.125% Senior Subordinated Notes due 2008 and incurred a pretax loss of \$10.1 million resulting from the payment of the call premium and the write-off of the unamortized original issue discount and debt issue costs.

Other expense during the first nine months of 2006 increased to \$17.1 million versus \$8.8 million in 2005, reflecting costs associated with the Receivables Facility resulting from an increase in the average of the accounts receivable sold for the first nine months of 2006 to \$376.8 million versus \$305.9 million in last year's comparable period and higher discount rates.

Income tax expense totaled \$78.6 million in the first nine months of 2006, and the effective tax rate was 33.1% compared to 31.8% in the same period in 2005. The current period's effective tax rate differed from the statutory rate primarily as a result of the domestic tax benefit from foreign operations and the increase in state taxes in 2006 compared to 2005.

For the first nine months of 2006, net income increased by \$95.2 million to \$159 million, or \$3.04 per diluted share, compared with \$63.8 million and \$1.30 per diluted share for the first nine months of 2005. The increase in net income was primarily attributable to increased sales, gross margin expansion, decreases in the SG&A expenses as a percent of net sales, decrease in interest expense, the 2005 loss on debt extinguishment somewhat offset by increases in depreciation and amortization and other expense and an increase in the effective tax rate of 1.3%.

***Liquidity and Capital Resources***

Total assets at September 30, 2006 and December 31, 2005 were \$1.9 billion and \$1.7 billion, respectively, for an increase of \$.2 billion. Contributing to the increase in total assets was an increase in accounts receivable of \$147.4 million from an increase of \$82 million in the subordinated retained interest in accounts receivable related to the accounts receivable securitization program and from an increase in the level of accounts receivable as a result of increased sales, and a \$41.4 million increase in inventory as a result of the increased level of sales. Total liabilities at September 30, 2006 compared to December 31, 2005 increased by \$13.2 million to \$1.2 billion. Contributing to the increase in total liabilities was an increase in accounts payable of \$33.5 million as a result of increased cost of sales and inventory; increase in bank overdrafts of \$13.4 million; and, the increase in accrued income taxes of \$14.8 million related to the increase in taxable income. Decreases in total liabilities were primarily from decreases in short-term and long term debt of \$48.9 million related to the \$29 million payment of the revolving credit facility and the \$20 million payment of the Bruckner note.

Our liquidity needs arise from working capital requirements, capital expenditures, acquisitions and debt service obligations. In addition, an acquisition agreement to which we are a party contains contingent consideration for the final acquisition payment which management has estimated will be \$1.1 million and paid in 2007 and is included in the current portion of deferred acquisition payable of \$4.6 million at September 30, 2006.



**Table of Contents**

We finance our operating and investing needs, as follows:

*Revolving Credit Facility*

The revolving credit facility matures in June 2010 and provides for an aggregate borrowing limit of up to \$275 million. During the nine months ended September 30, 2006, borrowings were \$215.9 million and repayments were \$244.9 million, with no outstanding balance at September 30, 2006, and, consequently, we were not subject to any covenants in the agreement governing the revolving credit facility.

*Mortgage Financing Facility*

In February 2003, we finalized a \$51 million mortgage financing facility, \$47.3 million of which was outstanding as of September 30, 2006. Borrowings under the mortgage financing are collateralized by 75 domestic properties and are subject to a 22-year amortization schedule with a balloon payment due at the end of the 10-year term. Interest rates on borrowings under this facility are fixed at 6.5%.

*Bruckner Note Payable*

Pursuant to the Bruckner purchase agreement and in accordance with the terms of a promissory note, the remaining payment of \$20 million was paid in June 2006.

*7.50% Senior Subordinated Notes due 2017*

At September 30, 2006, \$150 million in aggregate principal amount of the 7.50% Senior Subordinated Notes due 2017 (the 2017 Notes ) were outstanding. The 2017 Notes were issued by WESCO Distribution under an indenture dated as of September 27, 2005 with The Bank of New York (as successor to J.P. Morgan Trust Company, National Association), as Trustee, and are unconditionally guaranteed on an unsecured basis by WESCO International. The 2017 Notes accrue interest at the rate of 7.50% per annum and are payable in cash semi-annually in arrears on each April 15 and October 15.

*2.625% Convertible Senior Debentures due 2025*

At September 30, 2006, \$150 million in aggregate principle amount of the 2.625% Convertible Senior Debentures due 2025 (the 2025 Debentures ) was outstanding. The 2025 Debentures were issued by WESCO International under an indenture dated as of September 27, 2005 with The Bank of New York (as successor to J.P. Morgan Trust Company, National Association), as Trustee, and are unconditionally guaranteed on an unsecured senior subordinated basis by WESCO Distribution. The 2025 Debentures accrue interest at the rate of 2.625% per annum and are payable in cash semi-annually in arrears on each April 15 and October 15. Beginning with the six-month interest period commencing October 15, 2010, we also will pay contingent interest in cash during any six-month interest period in which the trading price of the 2025 Debentures for each of the five trading days ending on the second trading day immediately preceding the first day of the applicable six-month interest period equals or exceeds 120% of the principal amount of the 2025 Debentures. During any interest period when contingent interest shall be payable, the contingent interest payable per \$1,000 principal amount of 2025 Debentures will equal 0.25% of the average trading price of \$1,000 principal amount of the 2025 Debentures during the five trading days immediately preceding the first day of the applicable six-month interest period. As defined in SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities* the contingent interest feature of the 2025 Debentures is an embedded derivate that is not considered clearly and closely related to the host contract. The contingent interest component had a nominal value at issuance and at September 30, 2006.

The 2025 Debentures are convertible into cash and, in certain circumstances, shares of WESCO International, Inc. s common stock, \$0.01 par value, at any time on or after October 15, 2023, or prior to October 15, 2023 in certain circumstances. The 2025 Debentures will be convertible based on an initial conversion rate of 23.8872 shares of common stock per \$1,000 principal amount of the 2025 Debentures (equivalent to an initial conversion price of approximately \$41.86 per share). The conversion rate and the conversion price may be adjusted under certain circumstances.

At any time on or after October 15, 2010, we may redeem all or a part of the 2025 Debentures at a redemption price equal to 100% of the principal amount of the 2025 Debentures plus accrued and unpaid interest (including contingent interest and additional interest, if any) to, but not including, the redemption date. Holders of 2025 Debentures may require us to repurchase all or a portion of their 2025 Debentures on October 15, 2010, October 15, 2015 and October 15, 2020 at a cash repurchase price equal to 100% of the principal amount of the 2025 Debentures,

plus accrued and unpaid interest (including contingent interest and additional interest, if any) to, but not including, the repurchase date. If we undergo certain fundamental changes prior to maturity, holders of 2025 Debentures will have the right, at their option, to require us to repurchase for cash some or all of their 2025 Debentures at a repurchase price equal to 100% of the principal amount of the 2025 Debentures being repurchased, plus accrued and unpaid interest (including contingent interest and additional interest, if any) to, but not including, the repurchase date.

**Table of Contents***Cash Flow*

*Operating Activities-2006.* Cash provided by operating activities for the first nine months of 2006 totaled \$65.1 million primarily as the result of net income of \$159 million, adjusted for, among other items, depreciation and amortization of \$19.3 million of which \$7.4 million is related to two acquisitions in the second half of 2005, stock-based compensation of \$8.5 million and the reclassification of \$26.7 million related to the excess tax benefit from stock-based compensation expense. Cash provided by operating activities in the first nine months of 2006 included \$37.7 million from prepaid expenses and \$30.5 million in accounts payable related to increased sales and inventory. Additionally, \$13.5 million was provided from other current and noncurrent liabilities of which \$14.8 million is related to an increase in accrued income taxes related to increased taxable income and \$1.6 million increase in accrued acquisition related expenses related to the Carlton-Bates acquisition. Cash used by operating activities in the first nine months of 2006 included: \$82 million reduction in the receivables facility; \$51.8 million increase in trade and other receivables resulting from higher sales volume; and, \$38.7 million increase in inventories to accommodate increased sales demand.

*Operating Activities-2005.* Cash provided by operating activities during the first nine months of 2005 totaled \$166.1 million as the result of net income of \$63.8 million, adjusted for, among other items, \$1.9 million related to the loss on debt extinguishment, \$11.3 million of depreciation and amortization and \$5.6 million of stock-based compensation. Cash provided by operating activities in the first nine months of 2005 included: \$102.0 million related to the receivables facility; \$2.7 million related to prepaid and other current assets and \$98.4 million related to accounts payable from increased inventory purchases related to increased sales. Cash used in the first nine months of 2005 for operating activities included: \$110.5 million in trade and accounts receivable resulting from higher sales volume; \$14.3 million in inventories to accommodate increased sales demand and \$7.3 million in accrued payroll and benefit costs primarily related to incentive compensation.

*Investing Activities.* Net cash used in investing activities for the first nine months of 2006 and 2005 was \$21.6 million and \$288.1 million, respectively, of which capital expenditures were \$14.9 million and \$11 million, respectively, and expenditures of \$10.9 million in 2006 and \$1 million in 2005 were made pursuant to the terms of an acquisition purchase agreement. Additionally, in the third quarter of 2005 \$248.5 million and \$28.7 million were expended in connection with the acquisitions of Carlton-Bates Company and Fastec Industrial Corp., respectively.

*Financing Activities.* Net cash used by financing activities for the first nine months of 2006 was \$6.3 million and net cash provided by financing activities for the first nine months of 2005 was \$147.9 million. During the first nine months of 2006, borrowings and repayments of long-term debt of \$265.4 million and \$294.4 million, respectively, were related to our revolving credit facility and repayments of \$20 million related to the Bruckner Note Payable and \$1.0 million related to our mortgage financing facility. During the first nine months of 2005, proceeds from the issuance of long-term debt were from issuance of the 2017 Notes of \$150 million and from issuance of the 2025 Debentures of \$150 million. During the first nine months of 2005, the Company redeemed \$123.8 million in aggregate principal amount of the 2008 Notes. During the first nine months of 2005, borrowings and repayments of long-term debt each in the amount of \$171 million were related to our revolving credit facility and repayments of \$30 million were related to the Bruckner Note Payable. During the first nine months of 2006 and 2005, the proceeds from the exercise of stock-based compensation arrangements were \$6.5 million and \$6 million, respectively. During the first nine months of 2006, expenditures of \$0.6 million were made in conjunction with the issuance of the 2017 Notes and the 2025 Debentures. During the first nine months of 2005, expenditures of \$0.9 million were made in conjunction with the amendments to the revolving credit facility and the receivables facility and expenditures of \$8.2 million were made for debt issuance costs related to our 2017 Notes and the 2025 Debentures.

*Contractual Cash Obligations and Other Commercial Commitments*

There have not been any material changes in our contractual obligations and other commercial commitments that would require an update to the disclosure provided in our 2005 Annual Report on Form 10-K. Management believes that cash generated from operations, together with amounts available under our revolving credit facility and the accounts receivable securitization facility, will be sufficient to meet our working capital, capital expenditures and other cash requirements for the foreseeable future. There can be no assurances, however, that this will be or will continue to be the case.



**Table of Contents****Off-Balance Sheet Arrangements***Accounts Receivable Securitization Facility*

We maintain a Receivables Facility that had a total purchase commitment of \$400 million as of September 30, 2006. The Receivables Facility has a term of three years and is subject to renewal in May 2008. Under the Receivables Facility, we sell, on a continuous basis, the undivided interest in all domestic accounts receivable to WESCO Receivables Corporation, a wholly owned special purpose entity ( SPE ). The SPE sells, without recourse, to a third-party conduit, all the eligible receivables while maintaining a subordinated interest, in the form of overcollateralization, in a portion of the receivables. We have agreed to continue servicing the sold receivables for the financial institution at market rates; accordingly, no servicing asset or liability has been recorded. As of September 30, 2006, \$315 million in funding was outstanding under the Receivables Facility.

**Inflation**

The rate of inflation affects different commodities and the cost of products purchased and ultimately the pricing of our different products and product classes to our customers. On an overall basis, our pricing related to inflation comprised an estimated \$60 to \$65 million of our sales growth for the three months ended September 30, 2006 and an estimated \$200 to \$215 million of our sales growth for the nine months ended September 30, 2006.

**Seasonality**

Our operating results are not significantly affected by certain seasonal factors. Sales during the first quarter are generally less than 2% below the sales of the remaining three quarters due to reduced level of activity during the winter months of January and February. Sales increase beginning in March with slight fluctuations per month through December.

**Impact of Recently Issued Accounting Standards**

In March 2006, the FASB issued SFAS No. 156, *Accounting for Servicing of Financial Assets-an amendment of FASB Statement No. 140* which amends FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities* ( SFAS 156 ), with respect to the accounting for separately recognized servicing assets and servicing liabilities. This statement clarifies when servicing rights should be separately accounted for, requires companies to account for separately recognized servicing rights initially at fair value, and gives companies the option of subsequently accounting for those servicing rights at either fair value or under the amortization method. SFAS 156 is effective for fiscal years beginning after September 15, 2006. Consistent with its requirements, we will adopt SFAS 156 on January 1, 2007. We do not anticipate that the adoption of SFAS 156 will have a material impact on our financial position or results of operations and cash flows.

In July 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109* ( FIN 48 ). This statement clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements in accordance with SFAS No. 109, *Accounting for Income Taxes*. It prescribes a recognition threshold and measurement attribute for financial statement disclosure of tax positions taken or expected to be taken on a tax return. FIN 48 is effective for fiscal years beginning after December 15, 2006. Consistent with its requirements, we will adopt FIN 48 on January 1, 2007. We are currently evaluating the effect that implementation of FIN 48 will have on our financial position, results of operations and cash flows.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* ( SFAS 157 ) which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS 157 is effective for fiscal years beginning after November 15, 2007. We are currently evaluating the effect that implementation of SFAS 157 will have on our financial position, results of operations, and cash flows.

**Table of Contents**

**Forward-Looking Statements**

From time to time in this report and in other written reports and oral statements, references are made to expectations regarding our future performance. When used in this context, the words anticipates, plans, believes, estimates, intends, expects, projects, will and similar expressions may identify forward-looking statements, although not all forward-looking statements contain such words. Such statements including, but not limited to, our statements regarding our business strategy, growth strategy, productivity and profitability enhancement, new product and service introductions and liquidity and capital resources are based on management's beliefs, as well as on assumptions made by, and information currently available to, management, and involve various risks and uncertainties, certain of which are beyond our control. Our actual results could differ materially from those expressed in any forward-looking statement made by or on our behalf. In light of these risks and uncertainties there can be no assurance that the forward-looking information will in fact prove to be accurate. Factors that might cause actual results to differ from such forward-looking statements include, but are not limited to, an increase in competition, the amount of outstanding indebtedness, the availability of appropriate acquisition opportunities, availability of key products, functionality of information systems, international operating environments and other risks that are described in our Annual Report on Form 10-K for our fiscal year ended December 31, 2005, which is incorporated by reference herein, or other documents subsequently filed with the Securities and Exchange Commission. We have undertaken no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.



**Table of Contents**

**Item 3. Quantitative and Qualitative Disclosures about Market Risks**

There have not been any material changes to our exposures to market risk during the quarter ended September 30, 2006 that would require an update to the disclosures provided in our 2005 Annual Report on Form 10-K.

**Item 4. Controls and Procedures**

*Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures*

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of our disclosure controls and procedures as such term is defined under Rule 13a-15(e) promulgated under the Exchange Act. Based on this evaluation, our principal executive officer and our principal financial officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report.

*Changes in Internal Control Over Financial Reporting*

As a result of our acquisitions of Carlton-Bates Company and Fastec Industrial Corp in the third quarter of 2005, our internal control over financial reporting now includes the operations of those businesses. These controls will be incorporated into our Section 404 assessment for 2006. During the third quarter of 2006, there were no other changes in our internal control over financial reporting identified in connection with management's evaluation of the effectiveness of our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**Table of Contents**

**Part II Other Information**

**Item 1. Legal Proceedings**

From time to time, a number of lawsuits and claims have been or may be asserted against us relating to the conduct of our business, including routine litigation relating to commercial and employment matters. The outcome of any litigation cannot be predicted with certainty, and some lawsuits, may be determined adversely to us. However, management does not believe, based on information presently available, that the ultimate outcome of any such pending matters is likely to have a material adverse effect on our financial condition or liquidity, although the resolution in any quarter of one or more of these matters may have a material adverse effect on our results of operations for that period.

We are a defendant in a lawsuit in a state court in Florida in which a former supplier alleges that we failed to fulfill our commercial obligations to purchase product and seeks monetary damages in excess of \$17 million. We believe that we have meritorious defenses. Neither the outcome nor the monetary impact of this litigation can be predicted at this time. A trial is scheduled for March 2007.

Information relating to legal proceedings is included in Note 8, Commitments and Contingencies of the Notes to the Condensed Consolidated Financial Statements and is incorporated herein by reference.

**Item 6. Exhibits**

*(a) Exhibits*

23.1 Consent of American Appraisal Associates, Inc.

31.1 Certification of Chief Executive Officer pursuant to Rules 13a-14(a) promulgated under the Exchange Act.

31.2 Certification of Chief Financial Officer pursuant to Rules 13a-14(a) promulgated under the Exchange Act.

32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

**Table of Contents**

**Signatures**

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

WESCO International, Inc.

Date: November 9, 2006

/s/ Stephen A. Van Oss

Stephen A. Van Oss  
Senior Vice President, Chief Financial and  
Administrative Officer

30