
EYE CARE CENTERS OF AMERICA, INC.

Form 10-Q

(Prepared based on instructions as outlined by the Securities and Exchange Commission)

THIS FORM HAS NOT BEEN FILED WITH THE SEC

EYE CARE CENTERS OF AMERICA, INC.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

EYE CARE CENTERS OF AMERICA, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(dollars in thousands)

The purchase method of accounting was used to record assets and liabilities assumed by the Company. Such accounting generally results in increased depreciation recorded in future periods. Accordingly, the accompanying financial statements of the Predecessor and the Company are not comparable in all material respects since those financial statements report financial position, results of operations and cash flows of these two separate entities. See Note 2.

	<u>Predecessor</u>	<u>Company</u>
	<u>January 1,</u>	<u>April 2,</u>
	<u>2005</u>	<u>2005</u>
		(Unaudited)
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 3,098	\$ 18,665
Accounts and notes receivable, net	10,455	11,024
Inventory	28,558	28,128
Deferred income taxes, net	2,313	3,891
Prepaid expenses and other	7,552	9,868
Total current assets	<u>51,976</u>	<u>71,576</u>
PROPERTY & EQUIPMENT, net	46,440	44,737
GOODWILL	107,423	388,916
OTHER ASSETS	5,945	21,605
DEFERRED INCOME TAXES, net	13,765	17,357
Total assets	<u>\$ 225,549</u>	<u>\$ 544,191</u>
LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)		
CURRENT LIABILITIES:		
Accounts payable	\$ 21,991	\$ 24,423
Current maturities of long-term debt	19,628	9,571
Deferred revenue	5,198	5,086
Accrued payroll expense	5,874	5,473
Accrued interest	1,914	2,887
Other accrued expenses	8,422	14,158
Total current liabilities	<u>63,027</u>	<u>61,598</u>
LONG TERM DEBT, less current maturities	204,285	315,186
DEFERRED RENT	4,614	4,570
DEFERRED GAIN	1,296	1,238
Total liabilities	<u>273,222</u>	<u>382,592</u>
SHAREHOLDERS' EQUITY (DEFICIT):		
Common stock	74	74
Preferred stock	70,825	-
Additional paid-in capital	18,713	158,447
Retained earnings (deficit)	(137,285)	3,078
Total shareholders' equity (deficit)	<u>(47,673)</u>	<u>161,599</u>
	<u>\$ 225,549</u>	<u>\$ 544,191</u>

See Notes to Condensed Consolidated Financial Statements.

EYE CARE CENTERS OF AMERICA, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(dollars in thousands)

The purchase method of accounting was used to record assets and liabilities assumed by the Company. Such accounting generally results in increased depreciation recorded in future periods. Accordingly, the accompanying financial statements of the Predecessor and the Company are not comparable in all material respects since those financial statements report financial position, results of operations and cash flows of these two separate entities. See Note 2.

	<u>Predecessor</u>		<u>Company</u>
	<u>Thirteen Weeks Ended</u>	<u>Fifty Nine Days Ended</u>	<u>Thirty Two Days Ended</u>
	<u>March 27, 2004</u>	<u>March 1, 2005</u>	<u>April 2, 2005</u>
	(Unaudited)	(Unaudited)	(Unaudited)
NET REVENUES:			
Optical sales	\$ 111,141	\$ 74,839	\$ 38,511
Management fee	962	560	333
Total net revenues	<u>112,103</u>	<u>75,399</u>	<u>38,844</u>
OPERATING COSTS AND EXPENSES:			
Cost of goods sold	33,068	22,648	11,095
Selling, general and administrative expenses	59,576	42,226	19,842
Transaction expenses	-	15,642	-
Total operating costs and expenses	<u>92,644</u>	<u>80,516</u>	<u>30,937</u>
INCOME (LOSS) FROM OPERATIONS	19,459	(5,117)	7,907
INTEREST EXPENSE, NET	4,865	3,433	2,777
INCOME TAX EXPENSE (BENEFIT)	<u>5,023</u>	<u>(1,676)</u>	<u>2,052</u>
NET INCOME (LOSS)	<u>9,571</u>	<u>(6,874)</u>	<u>3,078</u>
LESS PREFERRED STOCK DIVIDENDS	<u>2,021</u>	<u>1,493</u>	<u>-</u>
NET INCOME AVAILABLE TO COMMON SHAREHOLDERS	<u>\$ 7,550</u>	<u>\$ (8,367)</u>	<u>\$ 3,078</u>

See Notes to Condensed Consolidated Financial Statements.

EYE CARE CENTERS OF AMERICA, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(dollars in thousands)

The purchase method of accounting was used to record assets and liabilities assumed by the Company. Such accounting generally results in increased depreciation recorded in future periods. Accordingly, the accompanying financial statements of the Predecessor and the Company are not comparable in all material respects since those financial statements report financial position, results of operations and cash flows of these two separate entities. See Note 2.

	Predecessor		Company
	Thirteen Weeks Ended March 27, 2004	Fifty Nine Days Ended March 1, 2005	Thirty Two Days Ended April 2, 2005
	(Unaudited)	(Unaudited)	(Unaudited)
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income (loss).....	\$ 9,571	\$ (6,874)	\$ 3,078
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Depreciation and amortization.....	3,994	2,683	1,099
Amortization of debt issue costs.....	441	309	206
Deferred liabilities and other.....	490	(1,713)	1,703
Deferred financing costs write-off.....	-	3,534	-
Increase in operating assets and liabilities.....	8,534	3,771	6,675
Net cash provided by operating activities.....	<u>23,030</u>	<u>1,710</u>	<u>12,761</u>
CASH FLOWS FROM INVESTING ACTIVITIES:			
Acquisition of property and equipment, net	<u>(3,637)</u>	<u>(1,850)</u>	<u>(234)</u>
Net cash used in investing activities.....	<u>(3,637)</u>	<u>(1,850)</u>	<u>(234)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:			
Payments on debt and capital leases.....	(9,801)	(213,872)	(26)
Payments for refinancing fees.....	-	(16,925)	(465)
Proceeds from issuance of debt.....	-	314,713	-
Retirement of treasury stock.....	-	1,668	-
Retirement of preferred stock.....	-	(72,318)	-
Common stock buyback.....	-	(168,116)	-
Common stock sale, net.....	-	158,521	-
Other.....	(70)	-	-
Net cash provided by (used in) in financing activities.....	<u>(9,871)</u>	<u>3,671</u>	<u>(491)</u>
NET INCREASE IN CASH.....	9,522	3,531	12,036
CASH AND CASH EQUIVALENTS, beginning of period..	3,809	3,098	6,629
CASH AND CASH EQUIVALENTS, end of period.....	<u>\$ 13,331</u>	<u>\$ 6,629</u>	<u>\$ 18,665</u>

See Notes to Condensed Consolidated Financial Statements.
EYE CARE CENTERS OF AMERICA, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

The condensed consolidated financial statements of Eye Care Centers of America, Inc. which is referred to as the "Company", "we", "our" and "us" include all of our accounts, our wholly owned subsidiaries' accounts and certain private optometrists' accounts for whom we perform management services (the "ODs"). All significant intercompany accounts and transactions have been eliminated in consolidation. Certain reclassifications have been made to the prior period statements to conform to the current period presentation.

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. The condensed consolidated balance sheet for the year ended January 1, 2005 was derived from the audited financial statements as of that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. We believe that all adjustments considered necessary for a fair presentation have been included and are of a normal, recurring nature. Operating results for the fifty nine day period ended March 1, 2005 and the thirty two day period ended April 2, 2005 are not necessarily indicative of the results that may be expected for the fiscal year ended December 31, 2005 ("fiscal 2005"). For further information, refer to the consolidated financial statements and footnotes thereto included in our Registration Statement on Form S-4 for the year ended January 1, 2005 ("fiscal 2004").

2. Merger Agreement

On December 2, 2004, we entered into a definitive merger agreement pursuant to which Thomas H. Lee Partners agreed to sell all of its equity interests in us to ECCA Holdings Corporation ("ECCA Holdings"), a company controlled by Moulin Global Eyecare Holdings Limited, which we refer to as Moulin, and Golden Gate Capital, which we refer to as Golden Gate ("the Acquisition"). Upon consummation of the agreement on March 1, 2005, we became a wholly-owned subsidiary of ECCA Holdings, which was in turn owned 56.5% by Moulin, 42.5% by Golden Gate and 1% by our management. In connection with the Acquisition, we issued \$152 million aggregate principal amount of 10³/₄% Senior Subordinated Notes due February 15, 2015, which we refer to as the New Notes, and entered into a \$190 million senior credit facility, which we refer to as the New Credit Facility. The net proceeds from the New Notes together with borrowings under the New Credit Facility and a \$172.7 million equity contribution from Moulin and Golden Gate was used to finance the Acquisition, including the permanent repayment of our old credit facility and the retirement of our 9¹/₈% Senior Subordinated Notes due 2008 and our Floating Interest Rate Subordinated Term Securities due 2008, which together we refer to as the Retired Notes. We also entered into a long-term supply agreement with Moulin. All of these transactions together are collectively referred to as the transactions; prior to the transactions the company is referred to as the "Predecessor" and subsequent to the transactions the company is referred to as the "Company".

As a result of the Acquisition, the Company has incurred approximately \$15.6 million of non-recurring expenses. These expenses consisted of seller expenses, premium paid to retire the Retired Notes and the write off of previously capitalized loan fees related to the Retired Notes and old credit facility.

The Acquisition was accounted for using the push-down method of accounting. Accordingly, a portion of the purchase price was preliminarily allocated to the identifiable net assets acquired based on their estimated fair values with the balance of the purchase price, \$388.9 million, included in goodwill. The preliminary allocation is pending final valuation of our assets.

3. Critical Accounting Policies

Critical accounting policies are those that require us to make assumptions that are difficult or complex about matters that are uncertain and may change in subsequent periods, resulting in changes to reported results.

The majority of our accounting policies do not require us to make difficult, subjective or complex judgments or estimates or the variability of the estimates is not material. However, the following policies could be deemed critical. We have discussed these critical accounting policies with the audit committee of the Board of Directors.

- Accounts receivable are primarily from third party payors related to the sale of eyewear and include receivables from insurance reimbursements, optometrist management fees, credit card companies, merchandise, rent and license fee receivables. Our allowance for doubtful accounts requires significant estimation and primarily consists of amounts owed to us by third party insurance payors. This estimate is based on the historical ratio of collections to billings. Our allowance for doubtful accounts was \$3.2 million and \$3.6 million at January 1, 2005 and April 2, 2005, respectively.
- Inventory consists principally of eyeglass frames, ophthalmic lenses and contact lenses and is stated at the lower of cost or market. Cost is determined using the weighted average method which approximates the first-in, first-out (FIFO) method. Our inventory reserves require significant estimation and are based on product with low turnover or deemed by us to be unsaleable. Our inventory reserve was \$0.7 million and \$1.1 million at January 1, 2005 and April 2, 2005, respectively.
- Goodwill represents approximately 71% of our assets and consists of the amount by which the purchase price exceeds the market value of acquired net assets. Goodwill must be tested for impairment at least annually using a “two-step” approach that involves the identification of reporting units and the estimation of fair values. This fair value estimation requires significant judgment by us.
- Valuation allowances for deferred tax assets reduce deferred tax assets when it is deemed more likely than not that some portion or all of the deferred tax assets will expire before realization of the benefit or that future deductibility is not probable due to taxable losses. Although realization is not assured due to historical taxable income and the probability of future taxable income, we believe it is more likely than not that all of the deferred tax asset will be realized.
- We maintain our own self-insurance group health plan. The plan provides medical benefits for participating employees. We have an employers' stop loss insurance policy to cover individual claims in excess of \$200,000 per employee. The amount charged to health insurance expense is based on estimates obtained from an actuarial firm. We believe the accrued liability of approximately \$1.3 million, which is included in other accrued expenses, as of April 2, 2005 is adequate to cover future benefit payments for claims that occurred prior to April 2, 2005.

4. Related Party Transactions

In connection with the recapitalization of the Company in 1998, we entered into a management agreement with THL Equity Advisors IV, LLC, or THL Advisors, dated as of April 24, 1998. Pursuant to the management agreement, in addition to one time fees that were payable to THL Advisors at the time of the recapitalization, THL Advisors was entitled to receive (i) management and other consulting services fees of \$500,000 per year, payable quarterly in advance, (ii) one percent (1.0%) of the gross purchase price for acquisitions for its participation in the negotiation and consummation of any such acquisition, (iii) reimbursement of out-of-pocket expenses and (iv) indemnification for certain liabilities incurred in connection with the provision of services under the management agreement. For each of the thirteen week periods ended March 27, 2004 and April 2, 2005, we paid THL Advisors aggregate fees and expenses of approximately \$125,000 and \$75,000, respectively, related to the management agreement. The management agreement was terminated in conjunction with the Acquisition.

During fiscal 1998, Bernard W. Andrews, one of our former directors and who was our Chief Executive Officer at the time, purchased \$1.0 million of our common stock, which was paid for by the delivery by Mr. Andrews of a promissory note payable to us with an original principal amount of \$1.0 million. Mr. Andrews' promissory note accrued interest at a fixed annual rate of 9.0% and was secured by 96,061 shares of our common stock held by Bernard W. Andrews Revocable Trust U/A. The promissory note plus all accrued interest was paid in full in conjunction with the Acquisition.

In connection with the Acquisition, we became a party to an advisory agreement with ECCA Holdings and an entity affiliated with Golden Gate, and a separate advisory agreement with ECCA Holdings and Moulin. Pursuant to each advisory agreement, Golden Gate, on the one hand, and Moulin, on the other hand, will be compensated for the financial, investment banking, management advisory and other services performed for future financial, investment banking, management advisory and other services they perform on our behalf. Each advisory agreement has a term of 10 years following the date on which the transactions are consummated, but will terminate on the date on which Golden Gate or Moulin, as the case may be, ceases to be a direct or indirect holder of equity interests of ECCA Holdings.

We prepaid \$3.0 million to Golden Gate and \$1.5 million to Moulin on the date of the Acquisition as compensation for advisory services to be rendered through the three-year period and 18-month period, respectively, immediately following the date of the Acquisition. Beginning 18 months after the consummation of the Acquisition, we will pay management fees of up to \$500,000 per fiscal quarter to Moulin until the aggregate management fees paid to Moulin under its Advisory Agreement, including those paid upon consummation of the acquisition, total \$3.0 million, and thereafter we will pay management fees of up to \$250,000 per fiscal quarter to each of Golden Gate and Moulin, subject to restrictions in (i) our new senior credit facility and (ii) the indenture governing the New Notes. We have also agreed to reimburse each of Golden Gate and Moulin up to \$125,000 annually for their out-of-pocket fees and expenses, including legal and accounting fees, incurred in connection with the provision of services to us, their ownership of equity securities of ECCA Holdings or the exercise of rights under the various agreements entered in connection with the Acquisition. In addition, we have agreed to pay certain additional transaction fees to each of them in the event we, ECCA Holdings or any of our subsidiaries completes any acquisition (whether by merger, consolidation, purchase of stock or assets or otherwise), debt or equity financing, sale of all or substantially all of our assets, change of control transaction or other similar transaction in an amount equal to 0.5% of the value of each such transaction.

5. Income Taxes

We record income taxes under SFAS No. 109 using the liability method. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse.

6. Supplemental Disclosure of Cash Flow Information (dollars in thousands)

	<u>Predecessor</u>		<u>Company</u>
	<u>Thirteen Weeks Ended March 27, 2004</u>	<u>Fifty Nine Days Ended March 1, 2005</u>	<u>Thirty Two Days Ended April 2, 2005</u>
	(Unaudited)	(Unaudited)	(Unaudited)
Cash paid for interest	\$ 1,868	\$ 5,213	\$ 957
Dividends accrued on preferred stock	\$ 2,021	\$ 1,493	\$ -
Cash paid for taxes	\$ 60	\$ 8	\$ 286

7. New Accounting Pronouncements

In December 2002, SFAS 148, "Accounting for Stock-Based Compensation - Transition and Disclosure" was issued by the FASB. This statement amends SFAS 123 to provide alternative methods of transition for a voluntary change to the fair value method of accounting for stock-based employee compensation. In addition, this statement amends the disclosure requirements of SFAS 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. We adopted the statement on December 29, 2002 and continue to account for stock-based employee compensation under the intrinsic value method. As all options are granted at fair market value, there is no compensation expense recorded for option grants. For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the options' vesting periods. The pro forma calculations include only the effects of 2002, 2003 and 2004 grants as all grants previous to 2002 were exercised or cancelled. As such, the impacts are not necessarily indicative of the effects on reported net income of future years. No options were outstanding during the thirty two day period ended April 2, 2005 as all options were cancelled in connection with the Acquisition. Our pro forma net income for the thirteen weeks ended March 27, 2004 and for the fifty nine day period ended March 1, 2005, respectively, is as follows:

	<u>Predecessor</u>	
	<u>Thirteen Weeks Ended March 27, 2004</u>	<u>Fifty Nine Days Ended March 1, 2005</u>
	(Unaudited)	(Unaudited)
Net income/(loss)	\$ 9,571	\$ (6,874)
Fair value based method compensation expense	40	21
Pro forma net income/(loss)	<u>\$ 9,531</u>	<u>\$ (6,895)</u>

On December 16, 2004, the Financial Accounting Standards Board (FASB) issued FASB Statement No. 123 (revised 2004), Share-Based Payment, which is a revision of FASB Statement No. 123, *Accounting for Stock-Based Compensation*. Statement 123(R) supersedes APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and amends FASB Statement No. 95, *Statement of Cash Flows*. Generally, the approach in Statement 123(R) is similar to the approach described in Statement 123. However, Statement 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the income statement based on their fair values. Pro forma disclosure is no longer an alternative.

Statement 123(R) must be adopted no later than the beginning of the first interim period beginning after December 15, 2005. Early adoption will be permitted in periods in which financial statements have not yet been issued.

Statement 123(R) permits public companies to adopt its requirements using one of two methods:

1. A “modified prospective” method in which compensation cost is recognized beginning with the effective date (a) based on the requirements of Statement 123(R) for all share-based payments granted after the effective date and (b) based on the requirements of Statement 123 for all awards granted to employees prior to the effective date of Statement 123(R) that remain unvested on the effective date.
2. A “modified retrospective” method which includes the requirements of the modified prospective method described above, but also permits entities to restate based on the amounts previously recognized under Statement 123 for purposes of pro forma disclosures either (a) all prior periods presented or (b) prior interim periods of the year of adoption.

The company plans to adopt Statement 123(R) using the modified-prospective method.

As permitted by Statement 123, the Company currently accounts for share-based payments to employees using Opinion 25’s intrinsic value method and, as such, generally recognizes no compensation cost for employee stock options. Accordingly, the adoption of statement 123(R)’s fair value method will have an impact on our result of operations, although it will have no impact on our overall financial position. The impact of adoption of Statement 123(R) cannot be predicted at this time because it will depend on levels of share-based payments granted in the future. However, had we adopted Statement 123(R) in prior periods, the impact of that standard would have approximated the impact of Statement 123 as described in the disclosure of pro forma net income above. Statement 123(R) also requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow as required under current literature. This requirement will reduce net operating cash flows and increase net financing cash flows in periods after adoption. The Company cannot estimate what those amounts will be in the future (because they depend on, among other things, when employees exercise stock options) and there were no amounts recognized in prior periods for such excess tax deductions as there were no exercises of options.

8. *Condensed Consolidating Information (Unaudited)*

The New Notes were issued by us and are guaranteed by all of our subsidiaries but are not guaranteed by ODs. The subsidiaries are wholly owned by us and the guarantees are full, unconditional and joint and several. The following condensed consolidating financial information presents (i) our financial position, results of operations and cash flows, as parent, as if we accounted for our subsidiaries using the equity method, (ii) the subsidiaries, and (iii) ODs. There were no transactions between the subsidiaries during any of the periods presented. Separate financial statements of the subsidiaries are not presented herein as we do not believe that such statements would be material to investors.

Consolidating Balance Sheet
For the Year Ended January 1, 2005

	Parent	Guarantor Subsidiaries	ODs	Eliminations	Consolidated Company
ASSETS					
Current assets:					
Cash and cash equivalents	\$ 2,582	\$ 337	\$ 179	\$ -	\$ 3,098
Accounts and notes receivable, net	142,575	47,353	4,900	(184,373)	10,455
Inventory	-	26,663	1,895	-	28,558
Prepaid expenses and other	2,313	-	-	-	2,313
Deferred income taxes, net	-	7,507	45	-	7,552
Total current assets	147,470	81,860	7,019	(184,373)	51,976
Property and equipment, net	-	46,374	66	-	46,440
Goodwill	166	107,195	87	(25)	107,423
Other assets	6,415	(470)	-	-	5,945
Deferred income taxes, net	13,310	455	-	-	13,765
Investment in subsidiaries	15,973	-	-	(15,973)	-
Total Assets	<u>\$ 183,334</u>	<u>\$ 235,414</u>	<u>\$ 7,172</u>	<u>\$ (200,371)</u>	<u>\$ 225,549</u>
LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)					
Current liabilities:					
Accounts payable	\$ 12	\$ 197,187	\$ 9,165	\$ (184,373)	\$ 21,991
Current maturities of long-term debt	19,301	327	-	-	19,628
Deferred revenue	-	4,748	450	-	5,198
Accrued payroll expense	-	5,514	360	-	5,874
Accrued interest	3,584	(1,670)	-	-	1,914
Other accrued expenses	69	7,595	758	-	8,422
Total current liabilities	22,966	213,701	10,733	(184,373)	63,027
Long-term debt, less current maturities	202,495	1,790	-	-	204,285
Deferred rent	-	4,455	159	-	4,614
Deferred gain	1,213	83	-	-	1,296
Total liabilities	<u>226,674</u>	<u>220,029</u>	<u>10,892</u>	<u>(184,373)</u>	<u>273,222</u>
Shareholders' equity (deficit):					
Common stock	74	-	-	-	74
Preferred stock	70,825	-	-	-	70,825
Additional paid-in capital	23,046	(1,084)	(3,224)	(25)	18,713
Retained earnings (deficit)	(137,285)	16,469	(496)	(15,973)	(137,285)
Total shareholders' equity (deficit)	<u>(43,340)</u>	<u>15,385</u>	<u>(3,720)</u>	<u>(15,998)</u>	<u>(47,673)</u>
	<u>\$ 183,334</u>	<u>\$ 235,414</u>	<u>\$ 7,172</u>	<u>\$ (200,371)</u>	<u>\$ 225,549</u>

Condensed Consolidating Income Statement
For the Thirteen Weeks Ended March 27, 2004

	Parent	Guarantor Subsidiaries	ODs	Eliminations	Consolidated Company
Revenues:					
Optical sales	\$ (214)	\$ 88,306	\$ 23,049	\$ -	\$ 111,141
Management fees	75	7,641	-	(6,754)	962
Equity earnings in subsidiaries	14,297	-	-	(14,297)	-
Total net revenues	14,158	95,947	23,049	(21,051)	112,103
Operating costs and expenses:					
Cost of goods sold	1,017	27,680	4,371	-	33,068
Selling, general and administrative expenses	(1,070)	49,886	17,514	(6,754)	59,576
Total operating costs and expenses	(53)	77,566	21,885	(6,754)	92,644
Income from operations	14,211	18,381	1,164	(14,297)	19,459
Interest expense, net	4,243	620	2	-	4,865
Income tax expense	397	3,862	764	-	5,023
Net income	\$ 9,571	\$ 13,899	\$ 398	\$ (14,297)	\$ 9,571

Condensed Consolidating Statement of Cash Flows
For the Thirteen Weeks Ended March 27, 2004

	Parent	Guarantor Subsidiaries	ODs	Eliminations	Consolidated Company
Cash flows from operating activities:					
Net income	\$ 9,571	\$ 13,899	\$ 398	\$ (14,297)	\$ 9,571
Adjustments to reconcile net income to net					
Cash provided by (used in) operating activities:					
Depreciation and amortization	-	3,994	-	-	3,994
Amortization of debt issue costs	13	428	-	-	441
Deferred liabilities and other	(67)	536	21	-	490
Equity earnings in subsidiaries	(14,297)	1,917	-	12,380	-
Increase/(decrease) in operating assets and liabilities	14,588	(5,863)	(191)	-	8,534
Net cash provided by operating activities	9,808	14,911	228	(1,917)	23,030
Cash flows from investing activities:					
Acquisition of property and equipment	-	(3,637)	-	-	(3,637)
Net cash used in investing activities	-	(3,637)	-	-	(3,637)
Cash flows from financing activities:					
Payments on debt and capital leases	(9,750)	(51)	-	-	(9,801)
Other	-	-	(70)	-	(70)
Net cash used in financing activities	(9,750)	(51)	(70)	-	(9,871)
Net increase in cash and cash equivalents	58	11,223	158	(1,917)	9,522
Cash and cash equivalents at beginning of period	67	3,501	241	-	3,809
Cash and cash equivalents at end of period	\$ 125	\$ 14,724	\$ 399	\$ (1,917)	\$ 13,331

Condensed Consolidating Balance Sheet
April 2, 2005

	Parent	Guarantor Subsidiaries	ODs	Eliminations	Consolidated Company
ASSETS					
Current assets:					
Cash and cash equivalents	\$ 8,267	\$ 9,776	\$ 622	\$ -	\$ 18,665
Accounts and notes receivable, net	186,728	48,638	4,561	(228,903)	11,024
Inventory	-	26,641	1,487	-	28,128
Deferred income taxes	2,388	1,503	-	-	3,891
Prepaid expenses and other	2,690	7,130	48	-	9,868
Total current assets	<u>200,073</u>	<u>93,688</u>	<u>6,718</u>	<u>(228,903)</u>	<u>71,576</u>
Property and equipment, net	-	44,671	66	-	44,737
Goodwill	280,113	108,741	87	(25)	388,916
Other assets	22,487	(882)	-	-	21,605
Deferred income taxes	20,805	(3,448)	-	-	17,357
Investment in subsidiaries	192	-	-	(192)	-
Total assets	<u>\$ 523,670</u>	<u>\$ 242,770</u>	<u>\$ 6,871</u>	<u>\$ (229,120)</u>	<u>\$ 544,191</u>
LIABILITIES AND SHAREHOLDERS' EQUITY/(DEFICIT)					
Current liabilities:					
Accounts payable	\$ 41,817	\$ 203,376	\$ 8,133	\$ (228,903)	24,423
Current maturities of long-term debt	9,222	349	-	-	9,571
Deferred revenue	-	4,629	457	-	5,086
Accrued payroll expense	-	5,104	369	-	5,473
Accrued interest	1,897	990	-	-	2,887
Other accrued expenses	6,218	6,647	1,293	-	14,158
Total current liabilities	<u>59,154</u>	<u>221,095</u>	<u>10,252</u>	<u>(228,903)</u>	<u>61,598</u>
Long-term debt, less current maturities	313,475	1,711	-	-	315,186
Deferred rent	-	4,418	152	-	4,570
Deferred gain	1,027	211	-	-	1,238
Total liabilities	<u>373,656</u>	<u>227,435</u>	<u>10,404</u>	<u>(228,903)</u>	<u>382,592</u>
Shareholders' equity/(deficit)					
Common stock	74	-	-	-	74
Additional paid-in capital	162,835	(1,139)	(3,224)	(25)	158,447
Retained earnings (deficit)	(12,895)	16,474	(309)	(192)	3,078
Total shareholders' equity/(deficit)	<u>150,014</u>	<u>15,335</u>	<u>(3,533)</u>	<u>(217)</u>	<u>161,599</u>
	<u>\$ 523,670</u>	<u>\$ 242,770</u>	<u>\$ 6,871</u>	<u>\$ (229,120)</u>	<u>\$ 544,191</u>

Condensed Consolidating Income Statement
For the Fifty Nine Days Ended March 1, 2005

	Parent	Guarantor Subsidiaries	ODs	Eliminations	Consolidated Company
Revenues:					
Optical sales	\$ -	\$ 57,670	\$ 17,169	\$ -	\$ 74,839
Management fees	-	5,328	-	(4,768)	560
Equity earnings in subsidiaries	4,220	-	-	(4,220)	-
Total net revenues	4,220	62,998	17,169	(8,988)	75,399
Operating costs and expenses:					
Cost of goods sold	-	19,504	3,144	-	22,648
Selling, general and administrative expenses	102	33,961	12,931	(4,768)	42,226
Transaction expenses	15,642	-	-	-	15,642
Total operating costs and expenses	15,744	53,465	16,075	(4,768)	80,516
Income from operations	(11,524)	9,533	1,094	(4,220)	(5,117)
Interest expense, net	182	3,251	-	-	3,433
Income tax expense	(4,832)	3,156	-	-	(1,676)
Net income	\$ (6,874)	\$ 3,126	\$ 1,094	\$ (4,220)	\$ (6,874)

Condensed Consolidating Statement of Cash Flows
For the Fifty Nine Days Ended March 1, 2005

	Parent	Guarantor Subsidiaries	ODs	Eliminations	Consolidated Company
Cash flows from operating activities:					
Net income	\$ (6,874)	\$ 3,126	\$ 1,094	\$ (4,220)	\$ (6,874)
Adjustments to reconcile net income to net					
Cash provided by (used in) operating activities:					
Depreciation and amortization	-	2,683	-	-	2,683
Amortization of debt issue costs	8	301	-	-	309
Deferred liabilities and other	(1,904)	167	24	-	(1,713)
Deferred financing costs write-off	3,534	-	-	-	3,534
Equity earnings in subsidiaries	(4,220)	-	-	4,220	-
Increase/(decrease) in operating assets and liabilities	2,731	1,602	(562)	-	3,771
Net cash provided by operating activities	(6,725)	7,879	556	-	1,710
Cash flows from investing activities:					
Acquisition of property and equipment	-	(1,850)	-	-	(1,850)
Net cash used in investing activities	-	(1,850)	-	-	(1,850)
Cash flows from financing activities:					
Payments on debt and capital leases	(213,819)	(53)	-	-	(213,872)
Payments for refinancing fees	(16,925)	-	-	-	(16,925)
Proceeds from issuance of debt	314,713	-	-	-	314,713
Retirement of treasury stock	1,668	-	-	-	1,668
Retirement of preferred stock	(72,318)	-	-	-	(72,318)
Common stock buyback	(168,116)	-	-	-	(168,116)
Common stock sale, net	158,521	-	-	-	158,521
Net cash used in financing activities	3,724	(53)	-	-	3,671
Net increase in cash and cash equivalents	(3,001)	5,976	556	-	3,531
Cash and cash equivalents at beginning of period	2,582	337	179	-	3,098
Cash and cash equivalents at end of period	\$ (419)	\$ 6,313	\$ 735	\$ -	\$ 6,629

Condensed Consolidating Income Statement
For the Thirty Two Days Ended April 2, 2005

	Parent	Guarantor Subsidiaries	ODs	Eliminations	Consolidated Company
Revenues:					
Optical sales	\$ -	\$ 32,721	\$ 5,790	\$ -	\$ 38,511
Management fees	-	2,758	-	(2,425)	333
Equity earnings in subsidiaries	(4,028)	-	-	4,028	-
Total net revenues	(4,028)	35,479	5,790	1,603	38,844
Operating costs and expenses:					
Cost of goods sold	-	9,836	1,259	-	11,095
Selling, general and administrative expenses	(9,039)	25,869	5,437	(2,425)	19,842
Transaction expenses	-	-	-	-	-
Total operating costs and expenses	(9,039)	35,705	6,696	(2,425)	30,937
Income from operations	5,011	(226)	(906)	4,028	7,907
Interest expense, net	(298)	3,075	-	-	2,777
Income tax expense	2,231	(179)	-	-	2,052
Net income	\$ 3,078	\$ (3,122)	\$ (906)	\$ 4,028	\$ 3,078

Condensed Consolidating Statement of Cash Flows
For the Thirty Two Days Ended April 2, 2005

	Parent	Guarantor Subsidiaries	ODs	Eliminations	Consolidated Company
Cash flows from operating activities:					
Net income	\$ 3,078	\$ (3,122)	\$ (906)	\$ 4,028	\$ 3,078
Adjustments to reconcile net income to net					
Cash provided by (used in) operating activities:					
Depreciation and amortization	-	1,099	-	-	1,099
Amortization of debt issue costs	21	185	-	-	206
Deferred liabilities and other	(693)	2,420	(24)	-	1,703
Deferred financing costs write-off	(3,534)	3,534	-	-	-
Equity earnings in subsidiaries	4,028	-	-	(4,028)	-
Increase/(decrease) in operating assets and liabilities	2,454	3,404	817	-	6,675
Net cash provided by operating activities	5,354	7,520	(113)	-	12,761
Cash flows from investing activities:					
Acquisition of property and equipment	-	(234)	-	-	(234)
Net cash used in investing activities	-	(234)	-	-	(234)
Cash flows from financing activities:					
Payments on debt and capital leases	(22)	(4)	-	-	(26)
Payments for refinancing fees	3,354	(3,819)	-	-	(465)
Proceeds from issuance of debt	-	-	-	-	-
Retirement of treasury stock	-	-	-	-	-
Retirement of preferred stock	-	-	-	-	-
Common stock buyback	-	-	-	-	-
Common stock sale, net	-	-	-	-	-
Net cash used in financing activities	3,332	(3,823)	-	-	(491)
Net increase in cash and cash equivalents	8,686	3,463	(113)	-	12,036
Cash and cash equivalents at beginning of period	(419)	6,313	735	-	6,629
Cash and cash equivalents at end of period	\$ 8,267	\$ 9,776	\$ 622	\$ -	\$ 18,665

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

Introduction

We are the third largest operator of optical retail stores in the United States as measured by revenue. We currently operate 377 stores in 33 states, including 313 directly-owned stores and 64 stores owned by an optometrist's professional entity (an "OD PC"), which we manage under long-term management agreements. Our consolidated financial information includes the results of our 313 directly-owned stores, as well as the results of 52 of the 64 stores operated by an OD PC. The remaining 12 stores operated by an OD PC are not consolidated and we recognize as management fee revenue only the cash flows we earn pursuant to the terms of management agreements for those 12 OD PC-operated stores.

Our net revenues are comprised of optical sales, net of discounts and promotions, from our 365 consolidated stores as well as management fees from the 12 stores owned by OD PCs that are not consolidated in our results. Optical sales include sales of frames, lenses (including lens treatments), contact lenses and eyeglass warranties at all of our 365 consolidated stores, as well as the professional fees of the optometrists at 179 of the stores. These 179 stores include 84 stores where the optometrist is our employee or an independent contractor, the 52 stores operated by an OD PC that are consolidated in our results and the 43 stores with independent optometrists for whom we provide management services. The management fees from the 12 unconsolidated OD PC-operated stores are based on the performance of the stores.

Our operating costs and expenses are comprised of costs of goods sold and selling, general and administrative expenses. Cost of goods sold primarily includes the cost of eyeglass frames, ophthalmic lenses, contact lenses, lab manufacturing costs and buying, warehousing, distribution, shipping and delivery costs. Selling, general and administrative expenses primarily include retail payroll, doctor payroll, occupancy, overhead, advertising and depreciation. Occupancy, overhead and depreciation are less variable relative to sales levels than other components of selling, general and administrative expenses.

In this management's discussion and analysis we use the terms "gross profit," "gross margin," "comparable store sales," "comparable transaction volume" and "average ticket price" to compare our period-over-period performance. Gross profit is defined as optical sales less cost of goods sold in a period. Gross margin is defined as gross profit as a percentage of optical sales in a period. Comparable store sales is calculated by comparing net revenues for a period to net revenues of the equivalent prior period for all stores open at least twelve months during such prior period. Comparable transaction volume is based on the number of comparable store sales in a period. Average ticket price is calculated by dividing comparable net revenues by comparable transaction volume in a period.

We believe that the key driver of our performance is our ability to grow revenue without increasing costs at the same rate by (i) increasing comparable transaction volume by offering value and convenience, (ii) actively managing our store base in targeted markets and (iii) pursuing fee-for-service funded managed vision care relationships. Our performance is also affected by general economic conditions and consumer confidence.

We primarily grow optical sales by offering value and convenience to our customers. Since fiscal 2001, we have focused on our value strategy, which includes a promotion of two complete pairs of single vision eyewear for \$99. We believe our value strategy results in increased comparable transaction volume and also believe it encourages customers to purchase higher margin lenses, lens treatments and accessories, which increases average ticket price.

We also grow optical sales and leverage costs through selective store base expansion by opening new stores in targeted markets. Until a new store matures, its operating costs as a percentage of optical sales are generally higher than that of an established store. Accordingly, the expense related to opening new stores adversely affects our results in that period. Over the longer term, opening a new store in an existing market allows us to leverage existing advertising, field management and overhead to mitigate margin pressure. When entering a new market, we seek to achieve sufficient market penetration to generate brand awareness and economies of scale in advertising, field management and overhead. Consistent with our strategic objectives, we believe the opportunity exists to open an average of 10 to 15 new stores per year over the next two years in existing and new markets. We also manage costs by closing stores that do not meet our performance expectations. Store openings and store closures affect period over period comparisons.

We have made a strategic decision to pursue fee-for-service funded managed vision care plans. Our net revenues derived from fee-for-service funded managed care plans grew at a rate of 2.8% during the first quarter of fiscal 2005 compared to fiscal 2004. Fee-for-service funded managed vision care plans consist of insurance relationships where we receive set fees for services provided to participants of a plan as opposed to capitated funded managed vision care plans where we receive a set fee per plan participant to provide any and all services requested by participants of such plan. Under a fee-for-service funded managed vision care plan we benefit from participants' utilization of the plan, whereas under a capitated funded managed vision care plan we bear risk related to the level at which participants utilize such plan. Substantially all of our current funded managed vision care plans are fee-for-service funded managed vision care plans. Our managed vision care plans also include discount managed vision care plans where participants receive a set discount on eye care products. We believe that participation in managed vision care plans will continue to benefit us and other large optical retail chains with strong local market shares, broad geographic coverage and sophisticated management information and billing systems. During the first quarter of fiscal 2005, approximately 31.0% of our optical revenues were derived from managed vision care programs. We expect that optical revenues derived from managed vision care plans will continue to account for approximately 30% of our net revenues, but that the percentage attributable to fee-for-service funded managed vision care plans will increase as revenues from discount managed vision care plans decline. While the average ticket price on products purchased under managed vision care plans is typically slightly lower than a non-managed vision care sale, managed vision care plan transactions generally earn comparable operating profit margins as they require less promotional spending and advertising support. We believe that the increased volume resulting from managed vision care plans also compensates for the lower average ticket price.

Results of Operations

The following table sets forth the percentage relationship to net revenues of certain income statement data. In order to provide the most beneficial performance comparison, the period January 2, 2005 to March 1, 2005 of the Predecessor and the period March 2, 2005 to April 2, 2005 of the Company have been combined to represent a total thirteen week period. The period-to-period comparison of financial results is not necessarily indicative of future results.

	Thirteen Weeks Ended	
	March 27, 2004	April 2, 2005
Statement of Income Data:		
NET REVENUES:		
Optical sales	99.1 %	99.2 %
Management fee	0.9	0.8
Total net revenues	<u>100.0</u>	<u>100.0</u>
OPERATING COSTS AND EXPENSES:		
Cost of goods sold	29.8 *	29.8 *
Selling, general and administrative expenses	53.6 *	54.8 *
Transaction expenses	0.0	13.7
Total operating costs and expenses	<u>82.6</u>	<u>97.6</u>
INCOME FROM OPERATIONS	17.4	2.4
INTEREST EXPENSE, NET	4.3	5.4
INCOME TAX EXPENSE	4.5	0.3
NET INCOME (LOSS)	<u>8.5 %</u>	<u>(3.3) %</u>

* Percentages based on optical sales only

The following is a discussion of certain factors affecting our results of operations and our liquidity and capital resources. This discussion should be read in conjunction with the consolidated financial statements and notes thereto included elsewhere in this document.

The Thirteen Weeks Ended April 2, 2005 Compared to the Thirteen Weeks Ended March 27, 2004.

Net Revenues. Net revenues increased to \$114.2 million for the thirteen weeks ended April 2, 2005 from \$112.1 million for the thirteen weeks ended March 27, 2004. This increase was largely the result of a comparable store sales increase of 2.0% compared to the first quarter of fiscal 2004. Two calendar changes negatively impacted sales. Our daily revenues dramatically increase after Christmas day. Fiscal 2005 started on January 2 whereas Fiscal 2004 started on December 28 resulting in the net loss of several high revenue days in the first quarter of 2005. Also, the calendar change in the Easter holiday from the second quarter of fiscal 2004 to the first quarter of fiscal 2005, when all of our stores are closed,

negatively impacted comparable store sales. In addition, comparable transaction volume decreased slightly by 0.6% compared to the first quarter of fiscal 2004 while average ticket prices increased by 2.5% compared to the first quarter of fiscal 2004. The increase in comparable store sales and average ticket prices was the result of an increase in frame retail prices and an increase in the sales mix of transitions and polarized lenses. We also had a larger store base in the first quarter of fiscal 2005 compared to the first quarter of fiscal 2004. We had 377 stores open during the first quarter of fiscal 2005 versus 374 stores in the first quarter of fiscal 2004. Funded managed vision care sales increased by 2.8% compared to the first quarter of fiscal 2004. Total managed vision care sales increased by 7.3% compared to the first quarter of fiscal 2004. The increase in total managed vision care sales was primarily due to the larger store base and an increase in the number of plans offered by our managed care partners.

Gross Profit. Gross profit increased to \$79.6 million for the thirteen weeks ended April 2, 2005 from \$78.1 million for the thirteen weeks ended March 27, 2004, primarily as a result of an increase in optical retail prices. Gross profit as a percentage of optical sales remained flat at 70.2%. This was largely caused by an increase in the sales mix of non-branded product which has a higher gross margin than branded product which was offset by larger expenditures in our lab manufacturing processes resulting in the flat trend.

Selling General & Administrative Expenses (SG&A). SG&A increased to \$62.1 million for the thirteen weeks ended April 2, 2005 from \$59.6 million for the thirteen weeks ended March 27, 2004 which is consistent with the increase in sales. SG&A, as a percentage of optical sales, increased to 54.8% for the thirteen weeks ended April 2, 2005 from 53.6% for the thirteen weeks ended March 27, 2004. This percentage increase was primarily due to increased expenditures in advertising and payroll offset by decreased expenditures in overhead expenses.

Transaction Expenses. Transaction expenses were \$15.6 million for the thirteen weeks ended April 2, 2005 all of which were incurred in the period ended March 1, 2005. There were no transaction expenses for the thirteen weeks ended March 27, 2004. The transaction expenses relate to the acquisition of us by Moulin Global Eyecare Holdings Limited and Golden Gate Capital, which we refer to as the "Acquisition", which occurred during the first quarter of fiscal 2005 including seller expenses, management bonuses, write off of debt financing costs and call premium on the old notes.

Net Interest Expense. Net interest expense increased to \$6.2 million for the thirteen weeks ended April 2, 2005 from \$4.9 million for the thirteen weeks ended March 27, 2004. This increase was primarily due to larger outstanding debt balances as a result of the Acquisition and an increase in interest rates as compared to the first quarter of fiscal 2004.

Income Tax Expense. Income tax expense decreased to \$0.3 million for the thirteen weeks ended April 2, 2005 from \$5.0 million for the thirteen weeks ended March 27, 2004.

Net Income (Loss). Net loss was \$3.8 million for the thirteen weeks ended April 2, 2005 compared to net income of \$9.6 million for the thirteen weeks ended March 27, 2004. This was primarily as a result of the transaction expenses and the increase in interest expense.

Liquidity and Capital Resources

Sources of Capital

Our short-term and long-term liquidity needs arise primarily from: (i) interest payments primarily related to our New Credit Facility and the New Notes; (ii) capital expenditures, including those for

opening new stores; and (iii) working capital requirements as may be needed to support our business. We intend to fund our operations, interest expense, capital expenditures and working capital requirements principally from cash from operations. We are a holding company with no direct operations. Our principal assets are the equity interests we hold in our subsidiaries. As a result, we are dependent upon dividends and other payments from our subsidiaries to generate the cash necessary to fund our operations, interest expense, capital expenditures and working capital requirements. There are currently no restrictions on the ability of our subsidiaries to transfer funds to us.

Cash flows from operating activities provided net cash of \$14.5 million for the thirteen weeks ended April 2, 2005 and \$23.0 million for the thirteen weeks ended March 27, 2004. Our other sources of capital are cash on hand and funding from our revolving credit facility. As of April 2, 2005 we had \$18.7 million of cash available to meet our obligations. We had \$25.0 million of borrowings available under the \$25.0 million revolving portion of our new senior credit facility, excluding \$2.4 million letters of credit outstanding.

Payments on debt and issuance of debt and equity transactions related to the Acquisition have been our principal financing activities. Cash flows provided by financing activities were \$3.2 million for the thirteen weeks ended April 2, 2005. Cash flows used in financing activities were \$9.9 million for the thirteen weeks ended March 27, 2004. On May 2, 2005, the Company retired the remaining \$8.3 million in Retired Notes, which includes interest and premium.

Our working capital primarily consists of cash and cash equivalents, accounts receivable, inventory, accounts payable and accrued expenses and was \$10.0 million as of April 2, 2005. Our level of working capital has remained relatively stable since March 27, 2004.

Capital expenditures were \$2.1 million for the thirteen weeks ended April 2, 2005 compared to \$3.6 million for the thirteen weeks ended March 27, 2004. Capital expenditures for all of 2005 are projected to be approximately \$11.0 million. Of the planned 2005 capital expenditures, approximately \$2.8 million is related to commitments to new stores and approximately \$8.2 million is expected to be for improvement of existing facilities and systems.

Based upon current operations, we believe that our cash flows from operations, together with borrowings that are available under the \$25.0 million revolving credit facility portion of our new senior credit facility, will be adequate to meet our anticipated requirements for working capital, capital expenditures and scheduled principal and interest payments through the next twelve months. Our ability to satisfy our financial covenants under our new senior credit facility, meet our debt service obligations and reduce our debt will be dependent on our future performance, which in turn, will be subject to general economic conditions and to financial, business, and other factors, including factors beyond our control. We believe that our ability to repay amounts outstanding under our new senior credit facility and the notes at maturity will likely require additional financing, which may not be available to us on acceptable terms, if at all. A portion of our debt bears interest at floating rates; therefore, our financial condition is and will continue to be affected by changes in prevailing interest rates.

Long-Term Debt

Credit Facility

In December 2002, the Company entered into a credit agreement which provided for \$117.0 million in term loans and \$25.0 million in revolving credit facilities (the Old Credit Facility). In connection with the Acquisition, we entered into a new senior secured credit facility which consists of (i) the \$165.0 million term loan facility (the Term Loan Facility); and (ii) the \$25.0 million secured

revolving credit facility (the Revolver and together with the Term Loan Facility, the New Credit Facility). The borrowings of the New Credit Facility together with the net proceeds from the offering of the New Notes and the equity investment of Moulin and Golden Gate were used to pay a cash portion of the purchase price of the Acquisition, to repay debt outstanding under the Old Credit Facility, to retire the Retired Notes and pay the related tender premium and accrued interest and to pay the related transaction fees and expenses. Thereafter, the New Credit Facility is available to finance working capital requirements and general corporate purposes.

Amortization payments. Prior to the maturity date, funds borrowed under the Revolver may be borrowed, repaid and re-borrowed, without premium or penalty. The term loan will be amortized quarterly through the date of maturity for the Term Loan Facility according to the following schedule:

Year	Amount (in millions)
2006	\$ 1.24
2007	1.65
2008	1.65
2009	1.65
2010	1.65
2011	1.65
2012	155.51
	<u>\$ 165.00</u>

Interest. Our borrowings under the New Credit Facility bear interest at a floating rate, which can either be, at our option, a base rate or a Eurodollar rate, in each case plus an applicable margin. The base rate is defined as the higher of (i) the JPMorgan Chase Bank prime rate or (ii) the federal funds effective rate, plus one half percent (0.5%) per annum. The Eurodollar rate is defined as the rate for Eurodollar deposits for a period of one, two, three, six, nine or twelve months (as selected by us). The applicable margins are:

Facility	Base Rate Margin	Eurodollar Margin
Term Loan Facility	2.00%	3.00%
Revolver	1.75%	2.75%

Following delivery of our financial statements for our fiscal quarter ending July 2, 2005, the applicable margin for borrowings under the Revolver will be determined pursuant to a pricing grid based on the attainment of certain leverage ratios. The applicable margin for borrowings under the Term Loan Facility will not be subject to adjustment.

In addition to paying interest on outstanding principal under the New Credit Facility, we are required to pay a commitment fee to the lenders under the Revolver in respect of the unutilized commitments thereunder at a rate equal to 0.50%. We will also pay customary letter of credit fees.

Security and guarantees. The New Credit Facility is secured by a valid first-priority perfected lien or pledge on (i) 100% of the capital stock of each of our present and future direct and indirect domestic subsidiaries, (ii) 65% of the capital stock of each of our future first-tier foreign subsidiaries, (iii) 100% of the capital stock of Eye Care Centers of America, Inc. and (iv) substantially all our present and future property and assets and those of each guarantor, subject to certain exceptions. Our obligations under the New Credit Facility are guaranteed by each of our existing and future direct and indirect domestic subsidiaries and ECCA Holdings.

Covenants. The New Credit Facility documentation contains customary affirmative and negative covenants and financial covenants. During the term of the New Credit Facility, the negative covenants restrict our ability to do certain things, including but not limited to:

- incur additional indebtedness, including guarantees;
- create, incur, assume or permit to exist liens on property and assets;
- make loans and investments and enter into acquisitions and joint ventures;
- engage in sales, transfers and other dispositions of our property or assets;
- prepay, redeem or repurchase our debt (including the notes), or amend or modify the terms of certain material debt (including the notes) or certain other agreements;
- declare or pay dividends to, make distributions to, or make redemptions and repurchases from, equity holders; and
- agree to restrictions on the ability of our subsidiaries to pay dividends and make distributions.

The following financial covenants are included:

- maximum consolidated leverage ratio;
- maximum capital expenditures; and
- minimum rent-adjusted interest coverage ratio.

As of April 2, 2005, we were in compliance with all of our financial covenants.

Mandatory prepayment. We are required to make a mandatory annual prepayment of the Term Loan Facility in an amount equal to 75% of excess cash flows as defined in the New Credit Facility, which percentage we expect to be reduced upon our achieving certain consolidated leverage ratios. In addition, we are required to make a mandatory prepayment of the Term Loan Facility with:

- 100% of the net cash proceeds of any property or asset sale or casualty, subject to certain exceptions and reinvestment rights;
- 100% of the net cash proceeds of certain debt issuances, subject to certain exceptions; and
- 50% of the net cash proceeds from the issuance of additional equity interests, subject to certain exceptions.

Mandatory prepayments will be applied to the Term Loan Facility, first to the scheduled installments of the term loan occurring within the next 12 months in direct order of maturity, and second, ratably to the remaining installments of the term loan. We may voluntarily repay outstanding loans under the New Credit Facility at any time without premium or penalty, other than customary “breakage” costs with respect to Eurodollar loans.

In connection with the borrowings made under the New Credit Facility, we incurred approximately \$8.0 million in debt issuance costs. These amounts are classified within other assets in the accompanying balance sheets and are being amortized over the life of the New Credit Facility. The unamortized amount of debt issuance costs as of April 2, 2005 related to the New Credit Facility was \$7.9 million.

Notes

In 2005, we issued \$152.0 million aggregate principal amount of our 10 3/4% Senior Subordinated Notes due 2015.

The notes:

- are general unsecured, senior subordinated obligations of the Company;
- are limited to an aggregate principal amount of \$152.0 million, subject to our ability to issue additional notes;
- mature on February 15, 2015;
- will be issued in denominations of \$1,000 and integral multiples of \$1,000;
- will be represented by one or more registered notes in global form, but in certain circumstances may be represented by notes in definitive form ;
- are subordinated in right of payment to all existing and future Senior Indebtedness of the Company, including the New Credit Facility;
- rank equally in right of payment to any future Senior Subordinated Indebtedness of the Company;
- are unconditionally guaranteed on a senior subordinated basis by each existing Subsidiary of the Company and any future Restricted Subsidiary of the Company that is not a Foreign Subsidiary;
- are effectively subordinated to any future Indebtedness and other liabilities of Subsidiaries of the Company that are not guaranteeing the notes;
- may default in the event there is a failure to make an interest or principal payment under the New Credit Facility.

Interest. Interest on the notes compounds semi-annually and:

- accrues at the rate of 10.75% per annum;
- accrues from the date of original issuance or, if interest has already been paid, from the most recent interest payment date;
- is payable in cash semi-annually in arrears on February 15 and August 15, commencing on August 15, 2005;
- is payable to the holders of record on the February 1 and August 1 immediately preceding the related interest payment dates; and
- is computed on the basis of a 360-day year comprised of twelve 30-day months.

Optional redemption. At any time prior to February 15, 2010, the Company may redeem all or part of the notes upon not less than 30 nor more than 60 days' prior notice at a redemption price equal to the sum of (i) 100% of the principal amount thereof, plus (ii) the Applicable Premium as of the date of redemption, plus (iii) accrued and unpaid interest on the notes, if any, to the date of redemption (subject to the right of holders of record on the relevant record date to receive interest due on the relevant interest payment date).

On and after February 15, 2010, the Company may redeem all or, from time to time, a part of the notes upon not less than 30 nor more than 60 days' notice, at the following redemption prices (expressed as a percentage of principal amount) plus accrued and unpaid interest on the notes, if any, to the applicable redemption date (subject to the right of holders of record on the relevant record date to receive

interest due on the relevant interest payment date), if redeemed during the twelve-month period beginning on February 15 of the years indicated below:

<u>YEAR</u>	<u>REDEMPTION PRICE</u>
2010	105.375%
2011	103.583%
2012	101.792%
2013 and thereafter	100.000%

Covenants. The New Notes contain customary affirmative and negative covenants including but not limited to:

- payment of securities
- limitation on indebtedness;
- limitation on restricted payments;
- limitation on liens;
- initial and future subsidiary guarantors;
- change of control.

In connection with the borrowings made under the notes, we incurred approximately \$10.1 million in debt issuance costs. These amounts are classified within other assets in the accompanying balance sheets and are being amortized over the life of the notes. The unamortized amount of debt issuance costs as of April 2, 2005 related to the notes was \$10.0 million.

In 1998, we issued 300,000 shares of a new series of preferred stock (the "Preferred Stock"), par value \$.01 per share. Dividends on shares of the Preferred Stock were cumulative from the date of issue (whether or not declared). Such dividends accrued on a daily basis from the original date of issue at an annual rate per share equal to 13% of the original purchase price per share, with such amount compounded annually. In conjunction with the Acquisition, we redeemed all 300,000 shares of the Preferred Stock at \$100 per share plus all accumulated and unpaid dividends.

Contractual Obligations. We are committed to make cash payments in the future on the following types of agreements:

- Long term debt; and
- Operating leases for stores and office facilities.

The following table reflects a summary of our contractual obligations as of April 2, 2005:

	Payments due by period				
	Total	Less than 1 yr	1 to 3 yrs	3 to 5 yrs	More than 5 yrs
Long Term Debt	\$ 322,718	\$ 9,226	\$ 3,300	\$ 11,285	\$ 298,907
Capital Lease Obligations	2,039	345	860	821	13
Operating Leases	149,027	32,110	53,621	37,149	26,147
Purchase Obligations	-	-	-	-	-
Total future principal payments on contractual obligations	<u>\$ 473,784</u>	<u>\$ 41,681</u>	<u>\$ 57,781</u>	<u>\$ 49,255</u>	<u>\$ 325,067</u>

Off-balance sheet arrangements. As of April 2, 2005, our only off-balance sheet arrangements were letters of credit, in the amount of \$2.4 million, issued under our old credit facility primarily to insurance companies and remain outstanding under our New Credit Facility.

Future Capital Resources. Based upon current operations, anticipated cost savings and future growth, we believe that our cash flow from operations, together with borrowings currently available under the Revolver, are adequate to meet our anticipated requirements for working capital, capital expenditures and scheduled principal and interest payments through the next twelve (12) months. Our ability to satisfy our financial covenants under the New Credit Facility to meet our debt service obligations and to reduce our debt will depend on our future performance, which in turn, will be subject to general economic conditions and to financial, business, and other factors, including factors beyond our control. In the event we do not satisfy our financial covenants set forth in the New Credit Facility, we may attempt to renegotiate the terms of the New Credit Facility with our lenders for further amendments to, or waivers of, the financial covenants of the New Credit Facility. We believe that our ability to repay the New Credit Facility at maturity will likely require additional financing. We cannot assume that additional financing will be available to us. A portion of our debt bears interest at floating rates; therefore, our financial condition is and will continue to be affected by changes in prevailing interest rates.

Seasonality and Quarterly Results

Our sales fluctuate seasonally. Historically, our highest sales and earnings occur in the first and third fiscal quarters; however, the opening of new stores may affect seasonal fluctuations. Hence, quarterly results are not necessarily indicative of results for the entire year.

Forward-Looking Statements

Certain statements contained herein constitute "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. All statements other than statements of historical facts included in this report regarding our financial position, business strategy, budgets and plans and objectives of management for future operations are forward-looking statements. These forward-looking statements may relate to, among other things, our future performance generally, business development activities, strategy, projected synergies, future capital expenditures, financing sources and availability and the effects of regulation and competition. When used in this report, the words "expect," "anticipate," "intend," "plan," "believe," "seek," "estimate," "may," "will" or "should" or, in each case, their negative and similar expressions are generally intended to identify forward-looking statements although not all forward-looking statements contain such identifying words.

You should not place undue reliance on these forward-looking statements, which reflect our management's view and various assumptions only as of the date of this report. Because these forward-looking statements involve risks and uncertainties, many of which are beyond our control, there are important factors that could cause actual results to differ materially from those expressed or implied by these forward-looking statements, including our assumptions, plans, objectives, expectations and intentions with respect to the following:

- our competitive environment;
- the cost and effect of legal, tax or regulatory proceedings;
- changes in general economic conditions;
- changes to our regulatory environment;

- our ability to maintain our relationships with optometrists;
- franchise claims by optometrists;
- our ability to build and maintain managed vision care plans;
- reduction of third-party reimbursement;
- technological advances in vision care;
- conflicts of interest between our controlling shareholders and noteholders;
- failure to realize anticipated cost savings;
- exposure to liability claims if we are unable to obtain adequate insurance;
- changes in general industry and market conditions and growth rates;
- loss of key management personnel;
- changes in accounting policies applicable to our business;
- the impact of unusual items resulting from the implementation of new business strategies, acquisitions and divestitures or future restructuring activities;
- our substantial indebtedness;
- restrictions imposed on our business by the terms of our indebtedness; and
- our ability to fund our capital requirements.

In light of these risks, uncertainties and assumptions, the forward-looking statements and events discussed in this report might not occur. You should assume the information appearing in this report is accurate only as of the date on the front cover of this report, as our business, financial condition, results of operations and prospects may have changed since that date. Unless required by law, we undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Additional information regarding these factors and others that could cause our actual results to differ materially from our expectations is included on our Registration Statement on Form S-4 filed with the Securities and Exchange Commission on May 3, 2005. The information appearing under “Risk Factors” in such Registration Statement on Form S-4 is incorporated by reference into and made a part of this Form 10-Q.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to various market risks. Market risk is the potential loss arising from adverse changes in market prices and rates. We do not enter into derivative or other financial instruments for trading or speculative purposes. There have been no material changes in our market risk during the first quarter of fiscal 2005. For further information, refer to the consolidated financial statements and footnotes thereto included in our Registration Statement on Form S-4.

Our primary market risk exposure is interest rate risk. As of April 2, 2005, \$165.0 million of our long-term debt bore interest at variable rates. Accordingly, our net income is affected by changes in interest rates. For every one hundred basis point change in the average interest rate under our \$165.0 million in long-term borrowings, our annual interest expense would change by approximately \$1.7 million.

In the event of an adverse change in interest rates, we could take actions to mitigate our exposure. However, due to the uncertainty of the actions that would be taken and their possible effects, this analysis assumes no such actions.

ITEM 4. CONTROLS AND PROCEDURES

Our Chief Executive Officer and our Chief Financial Officer have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13(a)-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report. Based upon such evaluation, such officers have concluded that our disclosure controls and procedures are effective as of the end of such period.

There has been no change in our internal controls over financial reporting that occurred during the thirteen weeks ended April 2, 2005 that has materially affected, or is reasonably likely to materially affect, our internal controls over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are a party to routine litigation in the ordinary course of our business. There have been no such pending matters, individually or in the aggregate that we believe to be material to our business or our financial condition that have arisen during the first quarter of fiscal 2005. For further discussion, refer to our Registration Statement on Form S-4.

ITEM 5. OTHER INFORMATION

On April 28, 2005, Moulin announced that events related to its internal controls had caused a delay in publicly releasing its annual results and that such delay had in turn caused Moulin's shares to be suspended from trading on the Stock Exchange of Hong Kong. Moulin also stated that the delay in releasing its annual results and the stock exchange suspension could have a material effect on Moulin's banking arrangements. We do not currently know what impact, if any, these events will have on Moulin's ability to deliver products to us under the supply agreement. We have, however, identified alternative sources in Asia from which we can directly purchase value and private label products at pricing which we believe is comparable to Moulin's estimated pricing and in April 2005 we received our first shipments of value product directly from one of these Asian sources. Therefore, if Moulin is unable to supply product to us under the supply agreement, we believe we will be able to achieve similar cost savings by purchasing directly from alternate sources.