SHARPS COMPLIANCE CORP
Form 10QSB
May 15, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-QSB

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

For the quarterly period ended March 31, 2008

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

For the transition period from _________ to _________.

Commission File Number: 0-22390

SHARPS COMPLIANCE CORP.
(Exact name of small business issuer as specified in its charter)

Delaware	**74-2657168**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
9220 Kirby Drive, Suite 500, Houston, Texas	**77054**
(Address of principal executive offices)	(Zip Code)

(713) 432-0300
(Issuer's telephone number)

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

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

APPLICABLE ONLY TO CORPORATE ISSUERS

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date:
12,565,183 shares of Common Stock, $0.01 par value as of May 13, 2008.

Transitional Small Business Disclosure Format (check one): Yes o No x

SHARPS COMPLIANCE CORP. AND SUBSIDIARIES

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PART I FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

SHARPS COMPLIANCE CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

	March 31, 2008 (Unaudited)	June 30, 2007
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 2,212,359	$ 2,134,152
Restricted cash	10,010	10,010
Accounts receivable, net of allowance for doubtful accounts of $15,605 and $15,793, respectively	1,261,729	1,330,731
Inventory	529,995	364,005
Prepaid and other assets	206,947	186,101
TOTAL CURRENT ASSETS	4,221,040	4,024,999
PROPERTY AND EQUIPMENT, net of accumulated depreciation of $867,156 and $878,248, respectively	1,206,300	590,567
INTANGIBLE ASSETS, net of accumulated amortization of $134,461 and $120,327, respectively	125,570	75,002
TOTAL ASSETS	$ 5,552,910	$ 4,690,568
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	$ 490,449	$ 557,302
Accrued liabilities	222,451	613,851
Deferred revenue	1,040,338	883,678
Current maturities of capital lease obligations	-	1,809
TOTAL CURRENT LIABILITIES	1,753,238	2,056,640
LONG-TERM DEFERRED REVENUE	524,462	392,803
RENT ABATEMENT	-	72,000
TOTAL LIABILITIES	2,277,700	2,521,443
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' EQUITY		
Common stock, $0.01 par value per share; 20,000,000 shares authorized; 12,505,183 and 11,998,453 shares issued and outstanding, respectively	125,052	119,985
Additional paid-in capital	9,159,420	8,596,321
Accumulated deficit	(6,009,262)	(6,547,181)

TOTAL STOCKHOLDERS' EQUITY		3,275,210		2,169,125
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$	5,552,910	$	4,690,568

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

SHARPS COMPLIANCE CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (LOSS)

	For the Three Months Ended March 31, 2008	2007
	(Unaudited)	
REVENUES		
Product	$ 2,852,682	$ 2,803,128
Environmental services	75,018	90,523
TOTAL REVENUES	2,927,700	2,893,651
COSTS AND EXPENSES		
Cost of revenues	1,786,892	1,681,437
Selling, general and administrative	1,174,449	952,608
Special Charge	-	138,000
Depreciation and amortization	69,684	52,313
TOTAL COSTS AND EXPENSES	3,031,025	2,824,358
OPERATING INCOME (LOSS)	(103,325)	69,293
OTHER INCOME (EXPENSE)		
Interest income	20,565	16,133
Interest expense	-	(322)
Other income	500	-
TOTAL OTHER INCOME	21,065	15,811
INCOME (LOSS) BEFORE INCOME TAXES	(82,260)	85,104
INCOME TAXES	(1,329)	(3,134)
NET INCOME (LOSS)	$ (83,589)	$ 81,970
NET INCOME (LOSS) PER COMMON SHARE		
Basic	$ (.01)	$ .01
Diluted	$ (.01)	$ .01
WEIGHTED AVERAGE SHARES USED IN COMPUTING NET INCOME (LOSS) PER COMMON SHARE:		
Basic	12,478,315	11,552,360
Diluted	12,478,315	13,395,644

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

SHARPS COMPLIANCE CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME

	For the Nine Months Ended March 31, 2008	2007
	(Unaudited)	
REVENUES		
Product	$ 9,784,250	$ 8,819,371
Environmental services	285,364	246,941
TOTAL REVENUES	10,069,614	9,066,312
COSTS AND EXPENSES		
Cost of revenues	5,890,095	5,194,825
Selling, general and administrative	3,514,876	2,831,152
Special Charge	-	138,000
Depreciation and amortization	193,301	142,002
TOTAL COSTS AND EXPENSES	9,598,272	8,305,979
OPERATING INCOME	471,342	760,333
OTHER INCOME (EXPENSE)		
Interest income	73,005	27,601
Interest expense	(44)	(4,500)
Other Income	500	32,500
TOTAL OTHER INCOME	73,461	55,601
INCOME BEFORE INCOME TAXES	544,803	815,934
INCOME TAXES	(6,884)	(21,180)
NET INCOME	$ 537,919	$ 794,754
NET INCOME PER COMMON SHARE		
Basic	$ .04	$ .07
Diluted	$ .04	$ .07
WEIGHTED AVERAGE SHARES USED IN COMPUTING NET INCOME PER COMMON SHARE:		
Basic	12,231,333	10,918,402
Diluted	13,515,878	11,971,720

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

SHARPS COMPLIANCE CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	For the Nine Months Ended March 31, 2008	2007
	(Unaudited)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 537,919	$ 794,754
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	193,301	142,002
Stock based compensation expense	44,212	1,762
Excess tax benefits from stock-based award activity	(16,064)	-
Changes in operating assets and liabilities:		
(Increase) decrease in accounts receivable	69,002	(392,557)
Increase in inventory	(165,990)	(144,284)
Increase in prepaid and other assets	(20,846)	(86,595)
Increase (decrease) in accounts payable and accrued liabilities	(442,052)	180,771
Increase in deferred revenue	288,319	218,857
NET CASH PROVIDED BY OPERATING ACTIVITIES	487,801	714,710
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property and equipment	(472,205)	(250,098)
Purchase of treatment facility	(350,000)	-
Improvements to treatment facility	(44,832)	-
Additions to intangible assets	(64,702)	(2,207)
NET CASH USED IN INVESTING ACTIVITIES	(931,739)	(252,305)
CASH FLOWS FROM FINANCING ACTIVITIES		
Payments on capital lease obligations	(1,809)	(37,657)
Excess tax benefits from stock-based award activity	16,064	-
Proceeds from exercise of stock options	507,890	869,407
NET CASH PROVIDED BY FINANCING ACTIVITIES	522,145	831,750
NET INCREASE IN CASH AND CASH EQUIVALENTS	78,207	1,294,155
CASH AND CASH EQUIVALENTS, beginning of period	2,134,152	296,959
CASH AND CASH EQUIVALENTS, end of period	$ 2,212,359	$ 1,591,114
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid for interest	$ 44	$ 4,498

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

SHARPS COMPLIANCE CORP. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 1 - ORGANIZATION AND BACKGROUND

The accompanying unaudited condensed consolidated financial statements include the financial transactions and accounts of Sharps Compliance Corp. and it's wholly owned subsidiaries, Sharps Compliance, Inc. of Texas (dba Sharps Compliance, Inc.), Sharps e-Tools.com, Inc. ("Sharps e-Tools"), Sharps Manufacturing, Inc., Sharps Environmental Services, Inc. (dba Sharps Environmental Services of Texas, Inc.) and Sharps Safety, Inc. (collectively, "Sharps" or the "Company"). All significant intercompany accounts and transactions have been eliminated upon consolidation.

NOTE 2 - BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission ("SEC") for interim financial information and with instructions to Form 10-QSB and, accordingly, do not include all information and footnotes required under accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, these interim condensed consolidated financial statements contain all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of the consolidated financial position of the Company as of March 31, 2008 and the results of its operations and cash flows for the three and nine months ended March 31, 2008 and 2007. The results of operations for the three and nine months ended March 31, 2008, are not necessarily indicative of the results to be expected for the entire fiscal year ending June 30, 2008. These unaudited condensed consolidated financial statements should be read in conjunction with the Company's Annual Report on Form 10-KSB for the year ended June 30, 2007.

NOTE 3 - SIGNIFICANT ACCOUNTING POLICIES

REVENUE RECOGNITION

The Company complies with the Securities and Exchange Commission's ("SEC") Staff Accounting Bulletin ("SAB") No. 101, "Revenue Recognition", which provides guidance related to revenue recognition based on interpretations and practices followed by the SEC. Under SAB No. 101, certain products offered by the Company have revenue producing components that are recognized over multiple delivery points (Sharps Disposal by Mail Systems, referred to as "Mailback" and Sharps Return Boxes, referred to as "Pump Returns") and can consist of up to three separate elements as follows: (1) the sale of the container system, (2) the transportation of the container system and (3) the treatment and disposal (incineration) of the container system. The individual fair value of the transportation and incineration services are determined by the sales price of the service offered by third parties, with the fair value of the container being the residual value. Revenue for the sale of the container is recognized upon delivery to the customer, at which time the customer takes title and assumes risk of ownership. Transportation revenue on Mailbacks is recognized when the customer returns the mailback container system and the container has been received at the Company's treatment facility. The Mailback container system is mailed to the incineration facility using the United States Postal Service ("USPS") or United Parcel Service ("UPS"). Incineration revenue is recognized upon the destruction and certification of destruction having been prepared on the container. Since the transportation element and the incineration elements are undelivered services at the point of initial sale of the container, the Mailback revenue is deferred until the services are performed. The current and long-term portions of deferred revenues are determined through regression analysis and historical trends. Furthermore, through regression analysis of historical data, the Company has determined that a certain percentage of all container systems sold may not be returned. Accordingly, a portion of the transportation and incineration elements is recognized at the point of sale.

NOTE 4 – RECENTLY ISSUED ACCOUNTING STANDARDS

In June 2006, the FASB issued Interpretation No. 48 ("FIN 48"), Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109*,* to clarify certain aspects of accounting for uncertain tax position, including issues related to the recognition and measurement of those tax positions. The Company adopted the provisions of FIN 48 as of July 1, 2007. The adoption of FIN 48 did not have a material effect on the Company's consolidated financial statements. The Company classifies interest and penalties associated with the payment of income taxes in the Other Income (Expense) section of its consolidated statement of income (loss). Tax return filings which are subject to review by local tax authorities by major jurisdiction are as follows:

- United States – fiscal years ended June 2004, 2005, 2006 and 2007
- State of Texas – fiscal years ended June 2004, 2005, 2006 and 2007

In September 2006, the FASB issued Statement No. 157, "Fair Value Measurements." SFAS 157 defines fair value, establishes a framework and gives guidance regarding the methods used for measuring fair value, and expands disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently evaluating the impact that this pronouncement may have on our consolidated financial statements.

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In February 2007, the FASB issued SFAS No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities — including an Amendment of FASB Statement No. 115.” This statement permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value and establishes presentation and disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities. SFAS 159 is effective as of the beginning of an entity’s first fiscal year that begins after November 15, 2007. Early adoption is permitted as of the beginning of a fiscal year that begins on or before November 15, 2007, provided the entity also elects to apply the provisions of SFAS No. 157. The Company expects to adopt SFAS 159 beginning July 1, 2008. The Company is currently evaluating the impact that this pronouncement may have on our consolidated financial statements.

NOTE 5 - INCOME TAXES

During the three and nine months ended March 31, 2008 the Company recorded a provision of $1,329 and $6,884 for estimated income taxes. During the three and nine months ended March 31, 2007 the Company recorded a provision of $3,134 and $21,180 for estimated incomes taxes. For federal income tax purposes the Company is in an Alternative Minimum Tax (“AMT”) situation. During the nine months ended March 31, 2008 the Company recorded a reduction to income taxes of $21,180 for prior year tax estimates to the tax return. The Company expects to utilize its net operating loss carry forwards to offset any ordinary taxable income for the year ending June 30, 2008.

NOTE 6 - NOTES PAYABLE AND LONG-TERM DEBT

Effective February 5, 2007, the Company entered into an Amended Credit Agreement with JPMorgan Chase Bank, N.A. (“Credit Agreement”) which provides for a $2.5 million Line of Credit Facility the proceeds of which may be utilized for, (i) working capital, (ii) letters of credit (up to $200,000), (iii) acquisitions (up to $500,000) and (iv) general corporate purposes. Indebtedness under the Credit Agreement is secured by substantially all of the Company’s assets. Borrowings bear interest at a fluctuating rate per annum equal to either, (i) prime rate or (ii) LIBOR plus a margin of 2.75%. Any outstanding revolving loans, and accrued and unpaid interest, will be due and payable on March 27, 2009, the maturity date of the facility. The aggregate principal amount of advances outstanding at any time under the Facility shall not exceed the Borrowing Base which is equal to, (i) 80% of Eligible Accounts Receivable (as defined) plus (ii) 50% of Eligible Inventory (as defined). The Credit Agreement contains affirmative and negative covenants that, among other items, require the Company to maintain a specified tangible net worth and fixed charge coverage ratio. The Credit Agreement also contains customary events of default. Upon the occurrence of an event of default that remains uncured after any applicable cure period, the lenders’ commitment to make further loans may terminate and the Borrower may be required to make immediate repayment of all indebtedness to the lenders. The lender would also be entitled to pursue other remedies against the Company and the collateral. As of March 31, 2008, there were no borrowings under this Line Of Credit Facility and the Company was in compliance with all loan covenants. Under the Credit Agreement, and based upon the Company’s March 31, 2008 level of accounts receivable and inventory, the amount available to borrow at quarter end was $1.3 million.

NOTE 7 – STOCK-BASED COMPENSATION

In December 2004, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards (“SFAS”) No. 123 (revised 2004), *Share-Based Payment* (“SFAS 123R”) that addresses the accounting for share-based payment transactions in which an enterprise receives employee services in exchange for equity instruments of the enterprise or liabilities that are based on the fair value of the enterprise’s equity instruments or that may be settled by the issuance of such equity instruments. SFAS 123R eliminates the ability to account for share-based compensation transactions using the intrinsic value method under Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* (“APB 25”), and generally requires instead that such transactions be accounted for using a fair-value-based method. We adopted SFAS 123R beginning July 1, 2006. There is no compensation expense related to the unvested portion of stock options granted prior to July 1, 2006 since the Company’s Board of Directors approved, in June 2006, the acceleration of the vesting of all unvested stock options previously awarded.

SFAS 123R requires the use of a valuation model to calculate the fair value of stock-based awards. The Company has elected to use the Black-Scholes-Merton ("BSM") pricing model to determine the fair value of stock- options on the dates of grant, consistent with that used for pro forma disclosures under SFAS No. 123, *Accounting for Stock-Based Compensation*. Restricted Stock Units ("RSUs") are measured based on the fair market values of the underlying stock on the dates of grant. The Company first awarded RSUs on July 2, 2007 (49,500 units).

The Company elected the modified prospective transition method as permitted by SFAS 123R, and accordingly, prior periods have not been restated to reflect the impact of SFAS 123R. Under this method, the Company is required to recognize stock-based compensation for all new and unvested stock-based awards that are ultimately expected to vest as the requisite service is rendered beginning July 1, 2006. Stock-based compensation is measured based on the fair values of all stock-based awards on the dates of grant.

For the three and nine months ended March 31, 2008, the Company recognized stock-based compensation expense of $23,774 and $44,212, respectively, which is included in the line item "selling, general and administrative expenses" of the Condensed Consolidated Statement of Income (Loss). Stock-based compensation expense recognized for the three and nine months ended March 31, 2007 was $1,762.

NOTE 8 - EARNINGS PER SHARE

Earnings per share are measured at two levels: basic per share and diluted per share. Basic per share is computed by dividing net income by the weighted average number of common shares outstanding during the period. Diluted per share is computed by dividing net income by the weighted average number of common shares after considering the additional dilution related to common stock options. In computing diluted earnings per share, the outstanding common stock options are considered dilutive using the treasury stock method. The following information is necessary to calculate earnings per share for the periods presented:

	Nine Months Ended March 31,			
		2008		**2007**
	(Unaudited)			
Net income, as reported	$	537,919	$	794,754
Weighted average common shares outstanding		12,231,333		10,918,402
Effect of Dilutive stock options		1,284,545		1,053,318
Weighted average diluted common shares outstanding		13,515,878		11,971,720
Net income per common share				
Basic	$	0.04	$	0.07
Diluted	$	0.04	$	0.07
Employee stock options excluded from computation of diluted income per share amounts because their effect would be anti-dilutive		150,000		-

NOTE 9 - STOCK TRANSACTIONS

During the quarter ended March 31, 2008 stock options to purchase 320,000 of common shares were exercised. Total proceeds to the Company were $354,850 (average price of $1.11 per share). During the quarter ended March 31, 2007 stock options to purchase 992,802 of common shares were exercised. Total proceeds to the Company were $748,767 (average price of $0.75 per share).

During the nine months ended March 31, 2008, stock options to purchase 506,730 shares of common stock were exercised. Total proceeds to the Company were $507,890 (average price of $1.00 per share). During the nine months ended March 31, 2007, stock options to purchase 1,153,790 were exercised. Total proceeds to the company were $869,407 (average price of $0.75 per share).

ITEM 2.

MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

INFORMATION REGARDING FORWARD-LOOKING STATEMENTS

This quarterly report on Form 10-QSB contains certain forward-looking statements and information relating to Sharps that are based on the beliefs of the Company's management as well as assumptions made by and information currently available to the Company's management. When used in this report, the words "anticipate," "believe," "estimate" and "intend" and words or phrases of similar import, as they relate to Sharps or Company management, are intended to identify forward-looking statements. Such statements reflect the current risks, uncertainties and assumptions related to certain factors including, without limitations, competitive factors, general economic conditions, customer relations, relationships with vendors, governmental regulation and supervision, seasonality, distribution networks, product introductions and acceptance, technological change, changes in industry practices, onetime events and other factors described herein. Based upon changing conditions, should any one or more of these risks or uncertainties materialize, or should any underlying assumptions prove incorrect, actual results may vary materially from those described herein as anticipated, believed, estimated, expected or intended. The Company does not intend to update these forward-looking statements.

GENERAL

Sharps is a leading developer and manufacturer of cost effective solutions for improving safety, efficiency and costs related to the proper disposal of medical waste by industry and consumers. Sharps primary markets include healthcare, retail, agriculture, hospitality, professional, industrial, commercial, governmental and pharmaceutical. The Company's products and services represent solutions for industries and consumers dealing with the complexity of managing regulatory compliance, environmental sensitivity, employee and customer safety, corporate risk and operating costs related to medical waste disposal. Sharps is a leading proponent and participant in the development of public awareness and solutions for the safe disposal of needles, syringes and other sharps in the community setting.

The Company's primary products include Sharps Disposal by Mail System®, Pitch-It™ IV Poles, Trip LesSystem®, Sharps Pump Return Box, Sharps Enteral Pump Return Box, Sharps Secure®, Sharps SureTemp Tote®, IsoWash® Linen Recovery System, Biohazard Spill Clean-Up Kit and Disposal System, Sharps e-Tools, Sharps Environmental Services and Sharps Consulting. Some products and services facilitate compliance with state and federal regulations by tracking, incinerating and documenting the disposal of medical waste. Additionally, some products and services facilitate compliance with educational and training requirements required by federal, state, and local regulatory agencies.

RESULTS OF OPERATIONS

The following analyzes changes in the consolidated operating results and financial condition of the Company during the three and nine months ended March 31, 2008 and 2007.

The following table sets forth, for the periods indicated, certain items from the Company's Condensed Consolidated Statements of Income (Loss), expressed as a percentage of revenue (unaudited):

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2008	**2007**	**2008**	**2007**
Net revenues	100%	100%	100%	100%
Costs and expenses:				
Cost of revenues	(61)%	(58)%	(59)%	(57)%
Selling, general and administrative	(41)%	(33)%	(35)%	(31)%
Special Charge	-	(5)%	-	(2)%
Depreciation and amortization	(2)%	(2)%	(2)%	(2)%
Total operating expenses	(104)%	(98)%	(96)%	(92)%
Income (Loss) from operations	(4)%	2%	4%	8%
Total other income	1%	1%	1%	1%
Net income (loss)	(3)%	3%	5%	9%

THREE MONTHS ENDED MARCH 31, 2008 AS COMPARED TO THREE MONTHS ENDED MARCH 31, 2007

Total revenues for the three months ended March 31, 2008 of $2,927,700 increased by $34,049, or 1.2%, over the total revenues for the three months ended March 31, 2007 of $2,893,651. Billings by market are as follows:

	Three Months Ended March 31,		
	2008	**2007**	**Variance**
	(Unaudited)	(Unaudited)	(Unaudited)
Billings by Market:			