

COLONIAL COMMERCIAL CORP
Form 10-Q
November 13, 2006

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549**

FORM 10-Q

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

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

OR

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

For the transition period from _____ to _____

Commission file number: **1-6663**

COLONIAL COMMERCIAL CORP.
(Exact name of registrant as specified in its charter)

New York
(State or other jurisdiction of incorporation or
organization)

11-2037182
(I.R.S. Employer Identification No.)

275 Wagaraw Road, Hawthorne, New Jersey
(Address of principal executive offices)

07506
(Zip Code)

973-427-8224
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

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

Large accelerated filer Accelerated filer Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

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

Class	Outstanding at November 1, 2006
Common Stock, \$.05 par value per share	4,593,579 shares
Convertible Preferred Stock, \$.05 par value per share	467,601 shares

COLONIAL COMMERCIAL CORP. AND SUBSIDIARIESCONTENTS

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Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements**

COLONIAL COMMERCIAL CORP. AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

September 30,
2006
(Unaudited)December 31,
2005

Assets

Current assets:

Cash	\$	790,174	\$	613,456
Accounts receivable, net of allowance for doubtful accounts of \$215,757 in 2006 and \$185,971 in 2005		9,379,331		8,489,717
Inventory		14,123,645		12,214,261
Prepaid expenses and other current assets		1,256,986		1,066,658
Deferred tax asset - current portion		637,500		637,500
Total current assets		26,187,636		23,021,592
Property and equipment		1,598,782		1,669,484
Goodwill		1,628,133		1,628,133
Other intangibles		4,000		11,334
Other assets - noncurrent		118,052		135,832
Deferred tax asset - noncurrent		1,071,000		1,071,000
Total assets	\$	30,607,603	\$	27,537,375

Liabilities and Stockholders' Equity

Current liabilities:

Trade payables	\$	6,723,810	\$	5,991,946
Accrued liabilities		2,005,860		2,047,159
Income taxes payable		12,666		12,772
Borrowings under credit facility - revolving credit		13,712,099		11,183,008
Borrowings under credit facility - term loan/overadvance		-		562,977
Notes payable - current portion; includes related party notes of \$30,000 in 2006 and \$60,389 in 2005		136,594		165,112
Total current liabilities		22,591,029		19,962,974
Notes payable, excluding current portion; includes related party notes of \$1,028,750 in 2006 and \$1,000,625 in 2005		1,386,816		1,400,834
Total liabilities		23,977,845		21,363,808

Commitments and contingencies

Stockholders' equity:

Redeemable convertible preferred stock, \$.05 par value, 2,500,000 shares authorized, 467,601 in 2006 and 484,721 in 2005 shares issued and outstanding, liquidation preference of \$2,338,005 in 2006 and \$2,423,605 in 2005		23,380		24,236
Common stock, \$.05 par value, 20,000,000 shares authorized, 4,593,579 in 2006 and 4,544,459 in 2005 shares issued and outstanding		229,679		227,223

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Additional paid-in capital	10,633,259	10,626,859
Accumulated deficit	(4,256,560)	(4,704,751)
Total stockholders' equity	6,629,758	6,173,567
Total liabilities and stockholders' equity	\$ 30,607,603	\$ 27,537,375

See accompanying notes to unaudited condensed consolidated financial statements.

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COLONIAL COMMERCIAL CORP. AND SUBSIDIARIES
Condensed Consolidated Statements of Operations
(Unaudited)

	For The Three Months Ended September 30,	
	2006	2005
Sales	\$ 19,217,556	\$ 17,377,655
Cost of sales	13,504,230	12,285,200
Gross profit	5,713,326	5,092,455
Selling, general and administrative expenses, net	4,857,533	4,449,626
Operating income	855,793	642,829
Other income	63,707	63,546
Interest expense, net; includes related party interest of \$26,431 in 2006 and \$23,684 in 2005	(359,214)	(269,897)
Income before income taxes	560,286	436,478
Income tax expense (benefit)	30,839	(582,141)
Net Income	\$ 529,447	\$ 1,018,619
Income per common share:		
Basic	\$ 0.12	\$ 0.24
Diluted	\$ 0.10	\$ 0.19
Weighted average shares outstanding:		
Basic	4,592,968	4,300,270
Diluted	5,301,782	5,296,133

See accompanying notes to unaudited condensed consolidated financial statements.

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COLONIAL COMMERCIAL CORP. AND SUBSIDIARIES
Condensed Consolidated Statements of Operations
(Unaudited)

	For The Nine Months Ended September 30,	
	2006	2005
Sales	\$ 52,257,581	\$ 48,226,815
Cost of sales	36,516,555	33,749,170
Gross profit	15,741,026	14,477,645
Selling, general and administrative expenses, net	14,407,601	13,068,688
Operating income	1,333,425	1,408,957
Other income	192,963	213,282
Interest expense, net; includes related party interest of \$77,825 in 2006 and \$68,225 in 2005	(995,116)	(763,788)
Income before income taxes	531,272	858,451
Income tax expense (benefit)	83,081	(481,417)
Net income	\$ 448,191	\$ 1,339,868
Income per common share:		
Basic	\$ 0.10	\$ 0.32
Diluted	\$ 0.08	\$ 0.25
Weighted average shares outstanding:		
Basic	4,574,227	4,217,250
Diluted	5,300,467	5,290,507

See accompanying notes to unaudited condensed consolidated financial statements.

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COLONIAL COMMERCIAL CORP. AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows
(Unaudited)

	For The Nine Months Ended September 30,	
	2006	2005
Cash flows from operating activities:		
Net income	\$ 448,191	\$ 1,339,868
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Deferred tax benefit	-	(641,500)
Stock-based compensation	-	(52,525)
Provision for doubtful accounts	116,035	29,343
Depreciation	340,216	285,211
Amortization of intangibles	7,334	12,750
Accretion of debt discount	28,125	28,125
Changes in operating assets and liabilities:		
Accounts receivable	(1,005,649)	(395,053)
Inventory	(1,909,384)	(139,892)
Prepaid expenses and other current assets	(190,328)	(293,483)
Other assets - noncurrent	17,780	40,529
Trade payables	731,864	876,375
Accrued liabilities	(41,299)	164,182
Income taxes payable	(106)	(29,018)
Net cash (used in) provided by operating activities	(1,457,221)	1,224,912
Cash flows from investing activities:		
Additions to property and equipment	(269,514)	(305,359)
Net cash used in investing activities	(269,514)	(305,359)
Cash flows from financing activities:		
Issuance of common stock and exercise of stock options	8,000	19,000
Retirement of preferred stock		(15,400)
Repayments of notes payable: includes related party repayments of \$30,389 in 2006, and \$0.00 in 2005	(83,734)	(48,919)
Issuance of notes payable	13,073	48,400
Repayments under credit facility - term loan/overadvance	(562,977)	(853,690)
Borrowings under credit facility - revolving credit	2,529,091	85,649
Net cash provided by (used in) financing activities	1,903,453	(764,960)
Increase in cash	176,718	154,593
Cash - beginning of period	613,456	310,659
Cash - end of period	\$ 790,174	\$ 465,252

See accompanying notes to unaudited condensed consolidated financial statements.

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COLONIAL COMMERCIAL CORP. AND SUBSIDIARIES

Notes To Condensed Consolidated Financial Statements

September 30, 2006

(Unaudited)

1. Summary of Significant Accounting Policies and Practices

The condensed consolidated financial statements of Colonial Commercial Corp. and Subsidiaries (the "Company") included herein have been prepared by the Company and are unaudited; however, such information reflects all adjustments (consisting solely of normal recurring adjustments), which are, in the opinion of management, necessary for a fair presentation of the financial position, results of operations, and cash flows for the interim periods to which the report relates. The results of operations for the period ended September 30, 2006 are not necessarily indicative of the operating results that may be achieved for the full year.

Certain information and footnote disclosures, normally included in consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States of America, have been condensed or omitted. It is suggested that these consolidated financial statements be read in conjunction with the consolidated financial statements and notes thereto included in the Company's Form 10-K for the year ended December 31, 2005.

We have one continuing industry segment - wholesale distribution of heating, ventilation, air conditioning equipment and plumbing fixtures.

Inventory is comprised of finished goods.

2. Stock Options

The Company adopted SFAS No. 123 (revised 2004), "Share-Based Payment" (SFAS No. 123(R)), which supersedes Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees." The revised statement addresses the accounting for share-based payment transactions with employees and other third parties, eliminates the ability to account for share-based transactions using APB No. 25 and requires that the compensation costs relating to such transactions be recognized in the consolidated financial statements. SFAS No. 123(R) requires additional disclosures relating to the income tax and cash flow effects resulting from share-based payments. The Company has adopted the modified prospective application method of SFAS No. 123(R), effective January 1, 2006, and the adoption of SFAS No. 123(R) has an immaterial impact on its consolidated results of operations and earnings per share.

The Company recognized stock-based compensation related to option repricing for options previously awarded using the intrinsic-value method. For the quarter and nine months ended September 30, 2005, the amount of stock based compensation was \$(26,785) and \$(52,525), respectively. During the quarter and nine months ended September 30, 2006 and 2005, no stock options were granted and all outstanding options were fully vested.

In June 1996, the Company adopted the 1996 Stock Option Plan (the "1996 Plan") to grant options to key employees and other persons who render service (non-employee) to the Company. The 1996 Plan expired on December 31, 2005.

At September 30, 2006, a total of 74,000 options were outstanding under the 1996 Plan. The outstanding options have expiration dates ranging from 2009 to 2013.

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On September 29, 2006, the Company adopted the Colonial Commercial Corp. 2006 Stock Plan, (the “2006 Plan”). The 2006 Plan enables the Company to grant equity and equity-linked awards to our Directors, officers, employees and other persons who provide services to the Company. The 2006 Plan is intended to allow us to provide incentives that will (1) strengthen the desire of highly competent persons to provide services to us and (2) further stimulate their efforts on our behalf.

The following is a summary of certain provisions of the 2006 Plan. A copy of the 2006 Plan is filed as Exhibit 10.01 to this Report.

Shares Available. The maximum number of shares of common stock that may be delivered under the 2006 Plan is 1,000,000, subject to adjustment for certain specified changes to the Company's capital structure.

Eligibility. All directors, officers and other employees and other persons who provide services to the Company are eligible to participate in the 2006 Plan.

Administration. The administrator of the 2006 Plan will be the board or any other committee which the board designates to serve as the administrator of the 2006 Plan.

Types of Awards. The types of awards that may be made under the 2006 Plan are stock options, stock appreciation rights, restricted stock awards, and stock units. The board or the committee that administers the 2006 Plan will fix the terms of each award, including, to the extent relevant, the following: (1) exercise price for options, base price for stock appreciation rights, and purchase price, if any, for restricted stock awards, (2) vesting requirements and other conditions to exercise, (3) term and termination, (4) effect, if any, of a change of control and (5) method of exercise and of any required payment by the recipient.

Term of Plan. No award may be granted under the 2006 Plan after the close of business on the day immediately preceding the tenth anniversary of the adoption of the 2006 Plan. However, all awards made prior to such time will remain in effect in accordance with their terms.

During the quarter and nine months ended September 30, 2006, no stock options were granted under the 2006 Plan.

The following table summarizes information about stock options at September 30, 2006:

Options Outstanding and Exercisable

Range of Exercise Prices	Shares	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price
\$.25	74,000	5.29	\$.25

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The following table illustrates the effect on income if the fair-value-based method had been applied to all outstanding awards in each period.

	For the Quarter Ended September 30, 2005	For the Nine Months Ended September 30, 2005
Net income, as reported	\$ 1,018,619	\$ 1,339,868
Add: Stock-based compensation related to option repricing	(26,785)	(52,525)
Pro forma net income	\$ 991,834	\$ 1,287,343
Basic income per share, as reported	0.24	0.32
Basic income per share, pro forma	0.23	0.31
Diluted income per share, as reported	0.19	0.25
Diluted income per share, pro forma	0.19	0.24

3. Equity Transactions

On April 3, 2006, Ronald Miller obtained 12,000 shares of common stock, by exercising 12,000 outstanding stock options. Mr. Miller is a Director of the Company.

On April 17, 2006, Jack Rose obtained 12,000 shares of common stock, by exercising 12,000 outstanding stock options. Mr. Rose was a Director of the Company at the time of the transaction.

On May 16, 2006, a non-executive employee of the Company obtained 4,000 shares of common stock by exercising 4,000 outstanding stock options.

On May 31, 2006, a non-executive employee of the Company obtained 4,000 shares of common stock by exercising 4,000 outstanding stock options.

The Company's reports on Form 8-K and Form 8-K/A filed on April 21, 2006 and April 25, 2006, respectively, refer to sales of common stock by former directors of the Company to two current directors and other investors. Concurrently with these transactions, Messrs. Bernard Korn, William Koon, Jack Rose and Carl Sussman resigned as Directors of the Company, and Mr. Korn also resigned as Chief Executive Officer and Chairman of the Board. Michael Goldman, who continues as a Director of the Company, was elected as Chairman of the Board and William Pagano, also continues as a Director and was appointed Chief Executive Officer. On May 11, 2006, Stuart H. Lubow and Phillip Siegel became Directors of the Company. Mr. Siegel also serves on the Audit Committee of the Company.

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During the quarter ended September 30, 2006 and 2005, holders of a total of 1,323 shares and 238,131 shares, respectively, of redeemable preferred stock converted these shares into 1,323 shares and 238,131 shares, respectively, of common stock.

During the nine months ended September 30, 2006 and 2005, holders of a total of 17,120 shares and 257,059 shares, respectively, of redeemable preferred stock converted these shares into 17,120 shares and 257,059 shares, respectively, of common stock.

4. Supplemental Cash Flow Information

The following is supplemental information relating to the consolidated statements of cash flows:

	For the Nine Months Ended	
	September 30, 2006	September 30, 2005
Cash paid during the period for:		
Interest	\$ 946,646	\$ 704,032
Income taxes	\$ 81,954	\$ 253,046

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	<u>Net Income Per Common Share</u>			
	For the Quarter Ended September 30,		For the Nine Months Ended September 30,	
	2006	2005	2006	2005
Net Income (numerator)	\$ 529,447	\$ 1,018,619	\$ 448,191	\$ 1,339,868
Weighted average common shares (denominator for basic income per share)	4,592,968	4,300,270	4,574,227	4,217,250
Effect of dilutive securities:				
Convertible preferred stock	468,212	668,193	474,083	745,333
Convertible notes	175,000	175,000	175,000	175,000
Stock options	65,602	152,670	77,157	152,924
Weighted average common and potential common shares outstanding (denominator for diluted income per share)	5,301,782	5,296,133	5,300,467	5,290,507
Basic net income per share	\$ 0.12	\$ 0.24	\$ 0.10	\$ 0.32
Diluted net income per share	\$ 0.10	\$ 0.19	\$ 0.08	\$ 0.25

6. Financing Arrangements

At September 30, 2006, the amount outstanding under the Company's credit facility with Wells Fargo Business Credit, Inc. ("Wells") was \$13,712,099. In addition, the Company has a standby letter of credit in the amount of \$300,000 which expires on July 31, 2007. Availability under the revolving credit line is determined by a percentage of available assets as defined in the Agreement, less letter of credit and reserves, and was \$887,901 as of September 30, 2006. The interest rate on the credit facility, as of September 30, 2006 was 8.0% (prime minus .25%).

The facility contains covenants relating to the financial condition of the Company, its business operations, and restricts the payment of dividends, subordinated debt, purchase of securities and capital expenditures. The Company is in compliance with all of its financial loan covenants.

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7.

Litigation

Universal Supply Group, Inc.

Universal Supply Group, Inc. is a New York corporation (“Universal”). On June 25, 1999, Universal acquired substantially all of the assets of Universal Supply Group, Inc., a New Jersey corporation, including its name, pursuant to the terms of a purchase agreement. The Company filed a copy of the purchase agreement with the Securities and Exchange Commission on March 30, 1999 as Exhibit 10(g) on Form 10KSB, and the Company filed a copy of an amendment to the purchase agreement on July 9, 1999 as Exhibit 10(a)(ii) on Form 8-K. Subsequent to the sale, Universal Supply Group, Inc. (the selling corporation) formerly known as Universal Engineering Co., Inc., changed its name to Hilco, Inc. Hilco, Inc. acquired the assets of Amber Supply Co., Inc., formerly known as Amber Oil Burner Supply Co., Inc., in 1998, prior to Hilco’s sale of assets to Universal. Hilco, Inc. is hereinafter referred to as the “Predecessor.” The majority shareholders of Hilco, Inc. were John A. Hildebrandt and Paul Hildebrandt.

The Company understands that Predecessor and many other companies have been sued in the Superior Court of New Jersey (Middlesex County) by plaintiffs filing lawsuits alleging injury due to asbestos. Currently, there exist 94 plaintiffs in these lawsuits relating to alleged sales of asbestos products, or products containing asbestos, by the Predecessor. The Company never sold any asbestos related products.

Of the existing plaintiffs, seven filed actions in 2006, 15 filed actions in 2005, 43 filed actions in 2004, 27 filed actions in 2003, and two filed actions in 2002. There are 105 other plaintiffs that have had their actions dismissed and eight other plaintiffs that have settled as of September 30, 2006 for a total of \$3,313,000. There has been no judgment against the Predecessor.

Our Universal subsidiary was named by 24 plaintiffs; of these, two filed actions in 1999, one filed an action in 2000, five filed actions in 2001, eleven filed actions in 2005 and five filed actions in 2006. Six plaintiffs naming Universal have had their actions dismissed and, of the total \$3,313,000 of settled actions, two plaintiffs naming Universal have settled for \$26,500. No money was paid by Universal in connection with any settlement. Following these dismissed and settled actions, there currently exist 16 plaintiffs that name Universal.

As set forth in more detail below, the Company has been indemnified against asbestos-based claims, and insurance companies are defending the interests of the Predecessor and the Company in these cases.

Based on advice of counsel, the Company believes that none of the litigation that was brought against the Company’s Universal subsidiary through September 30, 2006 is material, and that the only material litigation that was brought against Predecessor through that date was Rhodes v. A.O. Smith Corporation, filed on April 26, 2004 in the Superior Court of New Jersey, Law Division, Middlesex County, Docket Number MID-L-2979-04AS. The Company was advised that the Rhodes case was settled for \$3,250,000 under an agreement reached in connection with a \$10,000,000 jury verdict that was rendered on August 5, 2005. The Company was not a defendant in the Rhodes case.

The Company believes that Rhodes differed from the other lawsuits in that plaintiff established that he contracted mesothelioma as a result of his occupational exposure to asbestos dust and fibers and that a predecessor of the Company was a major supplier of the asbestos containing products that allegedly caused his disease.

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Indemnification

John A. Hildebrandt, Paul Hildebrandt and the Predecessor have jointly and severally agreed to indemnify our Universal subsidiary from and against any and all damages, liabilities and claims due to exposure to asbestos at any time prior to the June 25, 1999 closing of the purchase agreement referred to earlier. These agreements are set forth in the purchase agreement. Paul Hildebrandt, one of the indemnitors, was a director of the Company from September 29, 2004 to January 28, 2005.

The indemnitors may use their own counsel to defend these claims. The indemnitors are not liable for any settlement effected without their consent. The indemnitors may settle and pay money claims without the consent of the Company. There is no indemnification unless claims aggregate \$50,000; once this trigger point is reached, indemnification is required for all claims, including the first \$50,000, but excluding claims of less than \$10,000. The indemnification requirement survives at least until 30 days after the running of any relevant statutes of limitation.

The obligation of the indemnitors is joint and several, so that the Company can have recourse against any one or more of these indemnitors, whether or not any other indemnitor has previously defaulted on its obligation to us. There are no other limitations to our rights to indemnification.

Insurance

The assets that the Predecessor sold to us included its insurance policies and other agreements and contracts. The policies provide coverage for liability accruing during the periods for which premiums were paid. The Predecessor was formed in 1940. Copies of policies are available for each year beginning in 1970 and ending with the closing under the purchase agreement in 1999. Copies of policies for the period from 1940 to 1969 are not available.

Insurance companies acknowledge coverage for potential asbestos claims under certain of these policies. Insurance companies under additional policies have reserved their right to deny coverage but have continued to defend and indemnify the Predecessor and the Company under the contested policies.

There are periods during the years from 1940 to 1999 in which our Predecessor did not have coverage for potential asbestos claims. Subject to litigation, insurance companies may maintain that the existence of these periods' results in coverage for only a portion of a particular injury that varies with the period during which there was asbestos coverage relating to the injury, and that the balance of any settlement or judgment is to be paid by the insured. To date, no insurance company has claimed any contribution for a gap in coverage except for a claim for \$159.64 made by one insurance company to the Predecessor in 1995. The Predecessor asserted that it had no obligation to pay this amount and did not make any payment.

Insurance companies have to date defended us and the Predecessor, and have paid all settlement amounts and defense costs. Except for \$159.64 referred to above, the insurance companies have not requested any payments from us or from the Predecessor.

Our Universal subsidiary has not engaged in the sale of asbestos products since its formation in 1997. Its product liability policies for all years since 1998 exclude asbestos claims.

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General

Regardless of indemnification and insurance coverage, we do not in any event consider our Company to be liable for the asbestos-based lawsuits that name us or for any other claim that arises as a result of actions or omissions by Predecessor companies. We expressly disclaimed the assumption of any liabilities when we purchased the assets of the Predecessor. It is our opinion that the existing asbestos litigation will not have a material adverse effect on the Company. Nevertheless, we could be materially and adversely affected if we are held liable for substantial asbestos claims or if the Company incurs substantial legal or settlement costs. This material and adverse effect would occur if indemnitors fail to honor their indemnification agreements and insurance is not available either because policy limits are exceeded, or because insurance companies successfully claim limitations on their liabilities by reason of gaps in coverage or otherwise.

Since we do not regard as likely the potential payment of any asbestos-based claim, we have not accrued any balance for any period relating to asbestos claims, and we have not recorded any amount for asbestos claims for any period in any of our financial statements.

8. New Accounting Pronouncements

In June 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*-an interpretation FASB No. 109 ("FIN 48"), which prescribes accounting for and disclosure of uncertainty in tax positions. This interpretation defines the criteria that must be met for the benefits of a tax position to be recognized in the financial statements and the measurement of tax benefits recognized. The provisions of FIN 48 are effective as of the beginning of the Company's 2007 fiscal year, with the cumulative effect of the change in accounting principle recorded as an adjustment to opening retained earnings. The Company is currently evaluating the impact of adopting FIN 48 on the Company's consolidated financial statements.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurements*, ("SFAS 157"). This Standard defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The adoption of SFAS 157 is not expected to have a material impact on the Company's financial position, results of operations or cash flows.

9. Related Party Transaction

On August 31, 2006, the Company purchased from Goldman Associates of NY, Inc., ("Goldman Associates"), its Speed Queen home laundry equipment inventory and its related accounts receivable at their then book value of \$149,625. Goldman Associates is an affiliate of Michael Goldman, who is the Chairman of Colonial, as well as president and majority shareholder of Goldman Associates. Separately, the Company entered into a non-exclusive agreement with Alliance Laundry Systems, LLC for the distribution of Speed Queen home laundry equipment in the New York metropolitan area, and in portions of Connecticut, Delaware and Eastern Pennsylvania.

The Company owes Goldman Associates \$750,000 pursuant to a secured note which is subordinate to the Company's senior secured lender. The note bears interest at the prime rate and is due on June 30, 2008.

The wife of Michael Goldman is the holder of a convertible unsecured note in the amount of \$25,000, issued pursuant to the terms of a private placement made on July 29, 2004, with 50% of the principal payable on June 1, 2008 and the balance on June 1, 2009.

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The daughter of Michael Goldman has been a Director of the Company since October 22, 2004, and is the Chief Operating Officer of Goldman Associates as well as a member of their Board of Directors.

10. Subsequent Events

None

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

The Company

Colonial Commercial Corp. ("Colonial") is a New York corporation, which was incorporated on October 28, 1964. Unless otherwise indicated, the term "Company" refers to Colonial Commercial Corp. and its consolidated subsidiaries. The Company's operations are conducted through its wholly-owned subsidiaries, Universal Supply Group, Inc. ("Universal"), The RAL Supply Group, Inc. ("RAL") and American/Universal Supply, Inc. ("American").

Forward-Looking Statements

This report on Form 10-Q contains forward-looking statements relating to such matters as anticipated financial performance and business prospects. When used in this report, the words, "anticipates," "expects," "believes," "may," "intend" and similar expressions are intended to be among the statements that identify forward-looking statements. From time to time, the Company may also publish forward-looking statements. The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. Forward-looking statements involve risks and uncertainties, including, but not limited to, the consummation of certain events referred to in this report, technological changes, competitive factors, maintaining customer and vendor relationships, inventory obsolescence and availability, and other risks detailed in the Company's periodic filings with the Securities and Exchange Commission, which could cause the Company's actual results and experience to differ materially from the anticipated results or other expectations expressed in the Company's forward-looking statements.

Critical Accounting Policies

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires that we make estimates and judgments on the reported amounts of assets, liabilities, revenues and expenses, and the related disclosure of contingent assets and liabilities. We base our estimates on historical experience and on various other assumptions we believe to be applicable and reasonable under the current circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

In addition, we are periodically faced with uncertainties, the outcomes of which are not within our control and will not be known for prolonged periods of time.

We believe the following to be critical accounting policies that affect the most significant estimates and judgments used in the preparation of our consolidated financial statements:

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

ContentsRevenue Recognition

Revenue for the Company primarily consists of sales of heating, ventilation and air conditioning equipment, climate control systems and plumbing fixtures and supplies. The Company recognizes revenue after shipment of products has occurred in accordance with the shipping terms. There are no further obligations on the part of the Company subsequent to revenue recognition, except for returns of defective products from the Company's customers, which are covered under the manufacturer's warranty. The Company will receive a vendor credit from the manufacturer related to the warranted product in question, at which time credits are issued to the customer. The Company does not provide a warranty on products sold; rather the warranty is provided by the manufacturer.

Accounts Receivable

Accounts receivable consist of trade receivables recorded at original invoice amount, less an estimated allowance for uncollectible accounts. Trade credit is generally extended on a short-term basis; thus trade receivables generally do not bear interest. However, a service charge may be applied to receivables that are past due. These service charges are not recognized until collected, and are then included in other income. Trade receivables are periodically evaluated for collectibility based on past credit history with customers and their current financial condition. Changes in the estimated collectibility of trade receivables are recorded in the results of operations for the period in which the estimate is revised. Trade receivables that are deemed uncollectible are offset against the allowance for uncollectible accounts. The Company generally does not require collateral for trade receivables.

Inventory

Inventory is stated at the lower of cost or market and consists solely of finished goods. Cost is determined using the first-in, first-out method.

Distribution costs of incoming freight, purchasing, receiving, inspection, warehousing and handling costs are included in selling, general and administrative expenses. Such costs were \$114,189 and \$102,592 for the quarter ended September 30, 2006 and 2005, respectively, and \$305,496 and \$291,590 for the nine months ended September 30, 2006 and 2005, respectively.

Property and Equipment

Property and equipment are stated at cost. Depreciation is calculated on the straight line method over the estimated useful lives of the assets as follows:

Computer hardware and software	3-5 years
Furniture and fixtures	5 years
Automobiles	3-5 years

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

Deferred Income Tax Asset

The Company's deferred income tax asset represents certain future tax benefits related to the expected utilization of net operating loss carryforwards. The Company records a valuation allowance against any portion of the deferred income tax asset when it believes, based on the weight of available evidence, it is more likely than not that some portion of the deferred tax asset will not be realized.

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Goodwill and Other Intangible Assets

Statement of Financial Accounting Standards (SFAS) 142, "Goodwill and Other Intangible Assets," requires that goodwill having indefinite lives not be amortized, but instead be tested for impairment at least annually. Intangible assets determined to have finite lives are amortized over their remaining useful lives.

Results of Operations For the Quarter Ended September 30, 2006 and 2005

Sales increased by 10.6%, or \$1,839,901, to \$19,217,556 for the quarter ended September 30, 2006 from \$17,377,655 for the same period in 2005. The increase in sales is primarily a result of increased market penetration at two of the Company's subsidiaries, an increase in general industry pricing, and a continuing strong demand for residential and light commercial heating, air conditioning and plumbing fixtures, supplies and accessories. The increases in these areas were offset by weaknesses in sales of commercial control systems.

Gross profit increased by 12.2%, or \$620,871, to \$5,713,326 for the quarter ended September 30, 2006 from \$5,092,455 for the same period in 2005. Gross profit expressed as a percentage of sales increased by 0.4% to 29.7% in 2006 compared to 29.3% for the comparable period in 2005. The increase in the percentage of gross profit is primarily the result of improved pricing received from manufacturers, purchasing of additional inventory prior to price increases to preserve price protection, and sales of higher margin, more efficient models of air conditioning and heating systems. Cost of sales excludes the distribution costs of incoming freight, purchasing, receiving, inspection, warehousing and handling costs, as these costs are included in our selling, general and administrative expenses. Our gross margins may not be comparable to those of other entities since some entities include these distribution costs in the cost of sales. These distribution costs were \$114,189 and \$102,592 for the quarter ended September 30, 2006 and 2005, respectively.

Operating income increased by 33.1%, or 212,964, to \$855,793 for the quarter ended September 30, 2006 from \$642,829 for the same period in 2005. This percentage increase in operating income reflects the effect of the difference between the increase in gross profit of 12.2% compared to the increase in selling, general and administrative expenses of 9.2%. The increase in selling, general and administrative expenses was \$407,907, to \$4,857,533 for the quarter ended September 30, 2006 from \$4,449,626 for the same period in 2005. This was caused by increased expenses for personnel to improve customer service, expansion of our commercial departments, and added cost for increased health insurance, gasoline, utility expenses and interest expenses and decreasing sales in our commercial control systems business. Staffing costs increased by \$246,115, while costs for trucking and fuel increased by \$26,011.

Pre-tax income increased by 28.4%, or \$123,808, to \$560,286 for the quarter ended September 30, 2006 from \$436,478 for the same period in 2005. Interest expense, net increased by 33.1%, or \$89,317, to \$359,214 for the quarter ended September 30, 2006 from \$269,897 for the same period in 2005. The interest expense increase is primarily the result of increasing interest rates and increased borrowings under the credit line to support higher inventory levels and accounts receivable related to the increased sales of air conditioning products and higher inventory levels in the third quarter of 2006. The revolving credit line bears interest at .25% below prime rate, which was 8.25% at September 30, 2006 compared to 6.75% at September 30, 2005.

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The Company's net income decreased by 48.0%, or \$489,172, to \$529,447 for the quarter ended September 30, 2006, compared to net income of \$1,018,619 for the same period in 2005. The primary reason for the decrease in the Company's net income was the inclusion of a deferred tax benefit in the quarter ended September 30, 2005 in the amount of \$641,500 with no benefit recognized in the quarter ended September 30, 2006. In 2005, the tax benefit resulted from extending the tax benefit calculation from a two year earnings projection to a three year earnings projection, due to improved earnings predictability.

Results of Operations For the Nine Months Ended September 30, 2006 and 2005

Sales increased by 8.4%, or \$4,030,766, to \$52,257,581 for the nine months ended September 30, 2006 from \$48,226,815 for the same period in 2005. The increase in sales is primarily a result of increased market penetration at two of the Company's subsidiaries, an increase in general industry pricing, and a continuing strong demand for residential and light commercial heating, air conditioning and plumbing fixtures, supplies and accessories. The increases in these areas were offset by weaknesses in sales of commercial control systems.

Gross profit increased by 8.7%, or \$1,263,381, to \$15,741,026 for the nine months ended September 30, 2006 from \$14,477,645 for the same period in 2005. Gross profit expressed as a percentage of sales increased by 0.1% to 30.1% in 2006 compared to 30.0% for the comparable period in 2005. Cost of sales excludes the distribution costs of incoming freight, purchasing, receiving, inspection, warehousing and handling costs, as these costs are included in our selling, general and administrative expenses. Our gross margins may not be comparable to those of other entities since some entities include these distribution costs in the cost of sales. These distribution costs were \$305,496 and \$291,590 for the nine months ended September 30, 2006 and 2005, respectively.

Operating income decreased by 5.4%, or \$75,532, to \$1,333,425 for the nine months ended September 30, 2006 from \$1,408,957 for the same period in 2005. This percentage decrease in operating income reflects the effect of the difference between the increase in gross profit of 8.7% compared to the increase in selling, general and administrative expenses of 10.2%. The increase in selling, general and administrative expenses was \$1,338,913, to \$14,407,601 for the nine months ended September 30, 2006 from \$13,068,688 for the same period in 2005. This was caused by increased expenses for personnel to improve customer service, expansion of our commercial departments, and added cost for increased health insurance, gasoline, utility expenses and interest expenses and decreasing sales in our commercial control systems business. Staffing costs increased by \$797,022, while costs for trucking, fuel, and facilities increased by \$197,670.

Pre tax income decreased by 38.1%, or \$327,179, to \$531,272 for the nine months ended September 30, 2006 from \$858,451 for the same period in 2005. Other income decreased by 9.5%, or \$20,319, to \$192,963 for the nine months ended September 30, 2006 from \$213,282 for the same period in 2005. This decrease is primarily the result of a decrease in service charges collected from customers' past due invoices in the nine months ended September 30, 2006. Interest expense, net increased by 30.3%, or \$231,328, to \$995,116 for the nine months ended September 30, 2006 from \$763,788 for the same period in 2005. The interest expense increase is primarily the result of increasing interest rates and increased borrowings under the credit line to support higher inventory levels and accounts receivable related to the increased sales of air conditioning products and higher inventory levels in the third quarter of 2006. The revolving credit line bears interest at .25% below prime rate, which was 8.25% at September 30, 2006 compared to 6.75% at September 30, 2005.

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The Company's net income decreased by 66.5%, or \$891,677, to \$448,191 for the nine months ended September 30, 2006, compared to net income of \$1,339,868 for the same period in 2005. This decrease in net income was caused by the decrease in pre-tax income of \$327,179, as stated above, in addition to the effect of the inclusion of a deferred tax benefit in the nine months ended September 30, 2005 in the amount of \$641,500 with no benefit recognized in the nine months ended September 30, 2006. In 2005, the tax benefit resulted from extending the tax benefit calculation from a two year earnings projection to a three year earnings projection, due to improved earnings predictability.

The following table summarizes information derived from the Company's consolidated statements of income expressed as a percentage of sales for the quarter and nine months September 30, 2006 and 2005.

	For the Quarter Ended September 30,		For the Nine Months Ended September 30,	
	2006	2005	2006	2005
Sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	70.3	70.7	69.9	70.0
Gross profit	29.7	29.3	30.1	30.0
Selling, general and administrative expenses	25.3	25.6	27.5	27.1
Operating income	4.4	3.7	2.6	2.9
Other income	0.4	0.4	0.3	0.4
Interest expense, net	(1.9)	(1.6)	(1.9)	(1.6)
Income before taxes	2.9	2.5	1.0	1.7
Income taxes	(0.1)	3.4	(0.1)	1.1
Net income	2.8%	5.9%	0.9%	2.8%

Liquidity and Capital Resources

The Company has a \$15,000,000 secured loan facility pursuant to a credit and security agreement ("Agreement") with Wells. On May 11, 2006 the Company received a \$500,000 overadvance, payable in equal installments of \$12,500 each business day commencing July 11, 2006. The overadvance was paid in full on September 5, 2006. Effective June 23, 2006, the Agreement was amended to extend the maturity date from August 1, 2009 to August 1, 2010. The facility consists of a revolving line of credit which expires on August 1, 2010. In addition, the Company has a standby letter of credit in the amount of \$300,000 which expires on July 31, 2007. Availability under the revolving credit line is determined by a percentage of available assets as defined in the Agreement, less letter of credit and reserves, and was \$887,901 as of September 30, 2006. The balance outstanding under the revolving line of credit was \$13,712,099 as of September 30, 2006. The revolving credit line bears interest at .25% below prime. Substantially all of the assets of the Company, as well as a pledge of the stock of Colonial Commercial Corp.'s operating subsidiaries, collateralize the loans. The facility contains covenants relating to the financial condition of the Company, its business operations, and restricts the payment of dividends, subordinated debt, purchase of securities and capital expenditures. The Company is in compliance with all of its financial loan covenants. All loans are due on demand by the bank, and accordingly, have been classified as current liabilities.

The Company believes that the credit facility is sufficient to finance its current operating needs. However, the business of the Company would be materially and adversely affected if the bank demands payment of the loan and the Company is unable to refinance the loan.

As of September 30, 2006, the Company had \$790,174 in cash compared with \$613,456 at December 31, 2005.

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Net cash used in operating activities was \$1,457,221 for the nine months ended September 30, 2006. The net cash used in operating activities for the 2006 period is primarily a result of a net income of \$448,191 and non-cash charges of \$491,710, offset by cash used in operating assets and liabilities of \$2,397,122. The increase in accounts receivable of \$1,005,649 was primarily a result of increased sales during the third quarter. Accounts payable increased due to a \$1,909,384 increase in inventory over the nine months ended September 30, 2006. The increase in inventory was primarily the result of additional product lines, inventory purchased prior to expected vendor-announced price increases and seasonal purchases in preparation for increased demand for heating products in the fourth quarter.

Cash flows used in investing activities of \$269,514 during the nine months ended September 30, 2006 were due to purchases of equipment.

The cash flows provided by financing activities of \$1,903,453 consisted of \$2,529,091 in borrowings under the credit facility-revolving credit, \$500,000 in borrowings under the credit facility-overadvance, \$8,000 received from the exercise of stock options and \$13,073 from the issuance of notes payable. Cash flows used in financing activities consisted of \$562,977 for repayments under the credit facility-term loan, \$500,000 repayments under the credit facility-overadvance and \$83,734 for repayments on notes payable.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Market risk represents the risk of changes in value of a financial instrument, derivative or non-derivative, caused by fluctuations in interest rates, foreign exchange rates and equity prices. The Company has no financial instruments that give it exposure to foreign exchange rates or equity prices.

The Company's pre-tax earnings and cash flows are exposed to changes in interest rates. All borrowings under its credit facility bear interest based on the prime rate less .25% and a \$750,000 note to Goldman Associates of NY, Inc. which bears interest at prime. A hypothetical 10% adverse change in such rates would reduce the pre-tax earnings and cash flows by approximately \$116,000 over a one-year period, assuming the borrowing level remains consistent with the outstanding borrowings as of September 30, 2006. The fair value of the borrowings under the credit facility is not affected by changes in market interest rates.

The Company's remaining interest-bearing obligations are at fixed rates of interest and as such, do not expose the pre-tax earnings and cash flows to changes in market interest rates. The change in fair value of the Company's fixed rate obligations resulting from a hypothetical 10% adverse change in interest rates would not be material.

Item 4. Controls and Procedures

a. Evaluation of Disclosure Controls and Procedures

An evaluation has been carried out under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and the operation of our "disclosure controls and procedures" (as such term is defined in Rule 13a-15(e) under the Securities Exchange Act of 1934) as of September 30, 2006 ("Evaluation Date"). Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of the Evaluation Date, the disclosure controls and procedures are reasonably designed and effective to ensure that (i) information required to be disclosed by us in the reports we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (ii) such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Contentsb. Changes in Internal Controls

Subsequent to that evaluation, there have been no changes in our internal controls or other factors that could materially affect these controls after such evaluation.

PART II. OTHER INFORMATION**Item 1. Legal Proceedings**

The Company's Legal Proceedings are incorporated by reference from Part I Financial Information, Item 1 Financial Statements, Section 6 Litigation, of this Report on Form 10-Q.

Items 1A, 2 and 3 are not applicable and have been omitted.**Item 4. Submission of Matters to a Vote of Security Holders**

a. A Special Meeting of Shareholders was held on September 29, 2006.

b. On September 29, 2006, the common and preferred shareholders voted in favor of the following proposals:

i. To adopt an amendment to the Restated Certificate of Incorporation, as amended, that would allow the Company to issue up to 10,000,000 shares of preferred stock in one or more series, the terms of any such series to be determined by the Board of Directors from time to time.

ii. To adopt a restated Certificate of Incorporation to include only those articles that are currently applicable to the Company and that incorporates all amendments to date.

iii. To adopt the Colonial Commercial Corp. 2006 Stock Plan.

PROPOSAL	FOR	AGAINST	ABSTAINED
To adopt an amendment to the Restated Certificate of Incorporation, as amended, that would allow the Company to issue up to 10,000,000 shares of preferred stock in one or more series, the terms of any such series to be determined by the Board of Directors from time to time.	3,143,995	318,895	10,179
To adopt a restated Certificate of Incorporation to include only those articles that are currently applicable to the Company and that incorporates all amendments to date.	3,150,949	313,625	8,495
To adopt the Colonial Commercial Corp. 2006 Stock Plan.	3,075,472	311,862	85,735

A copy of the Restated Certificate of Incorporation is filed as Exhibit 3.01 to this Report. A copy of the Colonial Commercial Corp. 2006 Stock Plan is filed as an Exhibit 10.01 to this Report.

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Item 5 is not applicable and has been omitted.

Item 6. Exhibits

<u>3.01</u>	Restated Certificate of Incorporation of Colonial Commercial Corp. dated September 29, 2006.
<u>10.01</u>	Colonial Commercial Corp. 2006 Stock Plan.
<u>31.01</u>	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
<u>31.02</u>	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
<u>32.01</u>	Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
<u>32.02</u>	Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

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

Dated: November 13, 2006

COLONIAL COMMERCIAL CORP.

/s/ William Pagano
William Pagano,
Chief Executive Officer

/s/ William Salek
William Salek,
Chief Financial Officer