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COLONIAL COMMERCIAL CORP
Form 10-Q
February 25, 2004

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT UNDER SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE QUARTER ENDED SEPTEMBER 30, 2003 COMMISSION FILE NO. 1-6663

COLONIAL COMMERCIAL CORP.

(Exact Name of Company as Specified in its Charter)

NEW YORK

11-2037182

(State or Other Jurisdiction of
Incorporation or Organization)

(I.R.S. Employer Identification Number)

120 NEW SOUTH ROAD, HICKSVILLE, NEW YORK

11801

(Address of Principal Executive Offices)

(Zip Code)

Company's Telephone Number, Including Area Code: 516-681-4647

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Yes No X

-

Indicate by check mark whether the Company (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 Company was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes No X

-

Indicate the number of shares outstanding of the Company's Common Stock and Convertible Preferred Stock as of January 21, 2004

Common Stock, par value \$.05 per share - 2,405,794 shares
Convertible Preferred Stock, par value \$.05 per share - 1,464,252 shares

COLONIAL COMMERCIAL CORP. AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

COLONIAL COMMERCIAL CORP. AND SUBSIDIARIES
Condensed Consolidated Balance Sheets
September 30, 2003 and December 31, 2002

Assets	2003 ----- (Unaudited)	2002 -----
Current assets:		
Cash and cash equivalents	\$ 487,897	296,
Accounts receivable, net of allowance for doubtful accounts of \$355,000 in 2003 and \$265,000 in 2002, respectively	6,022,050	5,186,
Inventory	9,876,706	5,730,

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Prepaid expenses and other current assets	774,426	338,
	-----	-----
Total current assets	17,161,079	11,552,
Property and equipment, net	1,515,873	631,
Goodwill	1,628,133	1,416,
Other intangibles	64,584	85,
	-----	-----
	\$ 20,369,669	13,686,
	=====	=====
Liabilities and Stockholders' Equity (Deficit)		
Current liabilities:		
Accounts payable	\$ 5,999,835	2,446,
Accrued liabilities	1,566,884	1,435,
Income taxes payable	72,208	40,
Borrowings under credit facility	12,291,883	10,350,
Notes payable - current portion	30,889	30,
	-----	-----
Total current liabilities	19,961,699	14,303,
Notes payable, excluding current portion	411,861	64,
	-----	-----
Total liabilities	20,373,560	14,368,
	-----	-----
Commitments and contingencies		
Stockholders' (deficit):		
Redeemable convertible preferred stock, \$.05 par value, liquidation preference of \$7,321,260 at September 30, 2003 and December 31, 2002, 2,468,860 shares authorized, 1,464,252 shares issued and outstanding at September 30, 2003 and December 31, 2002	73,213	73,
Common stock, \$.05 par value, 20,000,000 shares authorized, 2,405,794 and 1,603,794 shares issued and outstanding at September 30, 2003 and December 31, 2002	120,290	80,
Additional paid-in capital	9,167,013	8,966,
Accumulated deficit	(9,364,407)	(9,801,
	-----	-----
Total stockholders' deficit	(3,891)	(681,
	-----	-----
	\$ 20,369,669	13,686,
	=====	=====

See accompanying notes to unaudited condensed consolidated financial statements.

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Net sales	\$ 11,321,632	10,591,830
Cost of sales	8,097,564	7,690,627
	-----	-----
Gross profit	3,224,068	2,901,203
Selling, general and administrative expenses, net	2,841,206	2,730,264
	-----	-----
Operating income	382,862	170,939
Interest income	370	348
Other income	134,410	140,777
Interest expense	(149,182)	(153,868)
	-----	-----
Income before income tax expense	368,460	158,196
Income tax expense	42,801	15,802
	-----	-----
Net income	\$ 325,659	142,394
	=====	=====
Income per common share:		
Basic	\$ 0.14	0.09
Diluted	0.08	0.05
Weighted average shares outstanding:		
Basic	2,292,468	1,603,794
Diluted	3,881,522	3,068,046

See accompanying notes to unaudited condensed consolidated financial statements.

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COLONIAL COMMERCIAL CORP. AND SUBSIDIARIES
Condensed Consolidated Statements of Operations
Nine Months Ended September 30, 2003 and 2002
(Unaudited)

	2003	2002
	-----	-----
Net sales	\$ 30,368,961	26,996,230
Cost of sales	21,681,398	19,238,679
	-----	-----
Gross profit	8,687,563	7,757,551
Selling, general and administrative expenses, net	8,096,637	7,634,032
	-----	-----
Operating income	590,926	123,519
Interest income	694	1,503
Other income	274,217	234,482

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Interest expense	(447,606)	(436,996)
	-----	-----
Income (loss) before income tax expense	418,231	(77,492)
Income tax expense (recovery)	(19,163)	17,509
	-----	-----
Net income (loss)	\$ 437,394	(95,001)
	=====	=====
Income (loss) per common share:		
Basic:	\$ 0.24	(0.06)
Diluted	0.13	(0.06)
Weighted average shares outstanding:		
Basic	1,833,352	1,603,771
Diluted	3,339,205	1,603,771

See accompanying notes to unaudited condensed consolidated financial statements.

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COLONIAL COMMERCIAL CORP. AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows
Nine Months Ended September 30, 2003 and 2002
(Unaudited)

	2003	2002
	-----	-----
Cash flows from operating activities:		
Net income (loss)	\$ 437,394	(95,001)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Provision for doubtful accounts	157,547	81,166
Depreciation	147,954	116,500
Amortization of intangibles	31,249	32,450
Changes in assets and liabilities, net of the effects of acquisitions:		
Accounts receivable	(409,418)	(284,424)
Inventory	(1,863,962)	286,048
Prepaid expenses and other current assets	(305,126)	(18,251)
Accounts payable	2,237,001	841,601
Investment securities - trading	--	122,506
Accrued liabilities	(64,892)	(131,808)
Income taxes payable	31,978	(5,515)
Deferred compensation	--	(122,506)
	-----	-----
Net cash provided by operating activities	399,725	822,766
	-----	-----
Cash flows from investing activities:		
Cash acquired in the acquisition of RAL Supply Group, Inc.	3,575	--
Payment for acquisition of Goldman Associates	--	(670,981)
Additions to property and equipment	(293,788)	(67,754)
	-----	-----

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Net cash used in investing activities	(290,213)	(738,735)
<hr style="border-top: 1px dashed black;"/>		
Cash flows from financing activities:		
Payments on notes payable	(26,554)	(238,668)
Issuance of notes payable	73,642	75,396
Net repayments under credit facility	(206,067)	109,008
Proceeds from issuance of common stock	240,600	--
<hr style="border-top: 1px dashed black;"/>		
Net cash provided by (used in) financing activities	81,621	(54,264)
<hr style="border-top: 1px dashed black;"/>		
Increase in cash and cash equivalents	191,133	29,767
Cash and cash equivalents - beginning of period	296,764	576,514
<hr style="border-top: 1px dashed black;"/>		
Cash and cash equivalents - end of period	\$ 487,897	606,281
<hr style="border-top: 3px double black;"/>		

See accompanying notes to unaudited condensed consolidated financial statements.

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COLONIAL COMMERCIAL CORP. AND SUBSIDIARIES

Notes To Consolidated Financial Statements

September 30, 2003
(Unaudited)

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND PRACTICES

The 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, 2003 are not necessarily indicative of the operating results that may be achieved for the full year.

On January 28, 2002, Atlantic Hardware & Supply Corporation ("Atlantic"), a wholly-owned subsidiary of the Company, filed a voluntary petition with the U. S. Bankruptcy Court for the Eastern District of New York to reorganize under Chapter 11 of the U. S. Bankruptcy Code. This immediately put the Company in default of its loan and security agreement (the "agreement") related to its credit facility with its secured lender (the "Bank"). Atlantic simultaneously obtained a debtor-in-possession ("DIP") credit facility with its pre-petition lender, the Bank. The Company is not part of the Chapter 11 filing. As of December 31, 2001, Atlantic was deconsolidated and the Company's 100% investment in Atlantic's common stock was written off.

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

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consolidated financial statements and notes thereto included in the Company's Form 10-K for the year ended December 31, 2002.

The Company has one continuing industry segment - wholesale distribution of heating, ventilation and air conditioning.

Inventory is comprised of finished goods.

(2) SUBSEQUENT EVENT

(a) Private Placement

On February 12, 2004, the Company completed a private placement, pursuant to Regulation D of the Securities Act of 1933. The

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Company raised \$360,000 through the issuance of 600,000 shares of common stock at \$0.60 per share. Bernard Korn (Chairman and President of the Company) purchased 165,000 shares, William Pagano (Director of the Company and President of the Company's wholly owned subsidiary, Universal Supply Group, Inc. ("Universal")), purchased 165,000 shares, and Rita Folger (a private investor who owns 9.42% of the Company) purchased 100,000 shares. The remaining 170,000 shares were purchased by a private investor who owns less than 5% of the Company.

The Company has used substantially all of the proceeds from the private placement to purchase 592,730 shares of escheated convertible preferred stock at \$0.60 per share from the State of Ohio. The Company has retired these convertible preferred shares.

The stock from the private placement cannot be sold, transferred or otherwise disposed of, unless subsequently registered under the Securities Act of 1933 and applicable state or Blue Sky laws, or pursuant to an exemption from such registration, which is available at the time of desired sale, and bear a legend to that effect.

(3) PRIVATE PLACEMENT

On July 16, 2003, the Company completed a private placement, pursuant to Regulation D of the Securities Exchange Act of 1933. The Company raised \$240,600 through the issuance of 802,000 shares of common stock at \$0.30 per share. Bernard Korn (Chairman and President of the Company) purchased 167,000 shares, James W. Stewart, (Executive Vice President and Director of the Company) purchased 100,000 shares, William Pagano (Director of the Company and President of the Company's wholly owned subsidiary, Universal Supply Group, Inc.), purchased 335,000 shares, Jack Rose (Director of the Company) purchased 50,000 shares and Rita Folger (a private investor who owns 6.86% of the Company) purchased 150,000 shares. The proceeds of the private placement were used for general working capital purposes. The stock cannot be sold, transferred or otherwise disposed of, unless subsequently registered under the Securities Act of 1933 and applicable state or Blue Sky laws, or pursuant to an exemption from such registration, which is available at the time of desired sale, and bear a legend to that effect.

(4) RAL ACQUISITION

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On September 30, 2003, RAL Purchasing, Inc., a newly formed, wholly owned subsidiary of the Company, purchased substantially all of the assets and assumed certain liabilities of RAL Supply Group, Inc. ("RAL") for a price of \$2,447,061. The purchase was financed as follows:

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Borrowings on the Company's credit facility	\$ 2,147,061
5-Year unsecured notes issued by RAL Purchasing, Inc. to third parties, at annual rate of 9%	300,000

Total outlay	\$ 2,447,061
	=====

In connection with this acquisition, the Company's limit on its credit facility was increased by \$1,500,000 to \$13,500,000. All borrowings under the credit facility are collateralized by substantially all of the assets of the Company. In addition, the 5-year notes are guaranteed by the Company.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition.

At September 30, 2003

Current assets	\$ 3,000,430
Property, plant and equipment	738,092
Goodwill	211,204
Covenant not to compete	10,000

Total assets acquired	3,959,726
Current liabilities	
Total liabilities assumed	1,512,665

Net assets acquired	\$2,447,061
	=====

Presented below are the pro forma financial results prepared under the assumption that the acquisition of RAL had been completed at the beginning of fiscal year 2002.

(in 000's except for EPS for data)	Nine Months Ended		Three Months Ended	
	September 30, 2003 ----	September 30, 2002 ----	September 30, 2003 ----	September 30, 2002 ----
Net Sales	\$37,355	35,645	13,809	13,385
Operating Income	963	636	440	389

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Net Income	746	297	407	320
Earnings per share				
Basic	\$.41	.19	.18	.20
Diluted	\$.22	.10	.10	.10

RAL is a distributor of heating and cooling equipment and high-end plumbing fixtures with six locations, servicing Orange, Rockland, Ulster and Sullivan counties in New York. Four locations have showrooms. RAL's products are marketed primarily to contractors, consumers, builders and the commercial sector. As a result of the acquisition, the Company is expecting to be

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one of the leading distributors of heating and cooling equipment and high-end plumbing fixtures in the market. The results of operations of RAL will be included in the consolidated results of operations from September 30, 2003.

(5) GOODWILL AND INTANGIBLES

Costs in excess of the fair value of tangible and identifiable intangible assets acquired and liabilities assumed in a purchase business combination are recorded as goodwill. SFAS No. 142, "Goodwill and Other Intangible Assets," requires that companies no longer amortize goodwill, but instead test for impairment at least annually using a two-step approach. The Company adopted SFAS No. 142 in the first quarter of fiscal 2002 and no longer amortizes goodwill. The Company evaluates goodwill, at a minimum, on an annual basis and whenever events and changes in circumstances suggest that the carrying amount may not be recoverable. Impairment of goodwill is tested at the reporting unit level by comparing the reporting unit's carrying amount, including goodwill, to the fair value of the reporting unit. The fair values of the reporting units are estimated using a combination of the income or discounted cash flows, approach and the market approach, which utilizes comparable companies' data. If the carrying amount of the reporting unit exceeds its fair value, goodwill is considered impaired and a second step is performed to measure the amount of impairment loss, if any.

The Company has determined that Universal and RAL are reporting units. Goodwill activity for these reporting units is as follows:

Balance at December 31, 2002	\$ 1,416,929
Additions to goodwill	
RAL Purchasing, Inc.	211,204

Balance at September 30, 2003	\$ 1,628,133
	=====

The Company has certain identifiable intangible assets that are subject to amortization. Intangible assets are included in "Other Intangibles" in the condensed consolidated balance sheet. The components of

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intangible assets are as follows:

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Acquired Intangible Assets	September 30, 2003	
	Gross Carrying Amount	Accumulated Amortization
Amortized intangible assets		
Covenants not to compete	\$ 241,667	(177,083)
	=====	=====

(6) SUPPLEMENTAL CASH FLOW INFORMATION

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

	Nine Months Ended	
	September 30, 2003	September 30, 2002
Cash paid during the period for:		
Interest	\$ 391,942	\$ 382,829
Income taxes	\$ -	\$ 23,024

During the nine months ended September 30, 2003, the Company financed \$2,447,061 of debt incurred in connection with the acquisition of RAL (note 3).

During the nine months ended September 30, 2002, the Company converted 34 shares of convertible preferred stock, which were converted to a similar number of common shares.

(7) COMPREHENSIVE INCOME (LOSS)

The Company has no items of other comprehensive income (loss); therefore, there is no difference between the Company's comprehensive income (loss) and net income (loss) for the periods presented.

(8) NET INCOME (LOSS) PER COMMON SHARE

A reconciliation between the numerators and denominators of the basic and diluted income (loss) per common share is as follows:

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	Nine Months Ended September 30,		Three M Sept
	2003	2002	2003
Net income (loss) numerator	\$ 437,394	(95,001)	325,659
	=====	=====	=====
Weighted average common shares (denominator for basic income per share)	1,833,352	1,603,771	2,292,468
Effect of dilutive securities:			
Convertible preferred stock	1,464,252	--	1,464,252
Employee stock options	41,601	--	124,802
	-----	-----	-----
Weighted average common and potential common shares outstanding (denominator for diluted Income per share)	3,339,205	1,603,771	3,881,522
	=====	=====	=====
Basic income (loss) per share	0.24	(0.06)	0.14
	=====	=====	=====
Diluted income (loss) per share	0.13	(0.06)	0.08
	=====	=====	=====

(9) STOCK OPTIONS

The Company uses the intrinsic-value method of accounting for stock-based awards granted to employees. No stock-based compensation cost is included in net income, as all options granted during periods presented had an exercise price equal to the market value of the stock on the date of grant. In accordance with SFAS No. 148, "Accounting for Stock Based Compensation - Transition and Disclosure," the following table presents the effect on net loss and net loss per share had compensation cost for the Company's stock plans been determined consistent with SFAS No. 123. The fair value of each option grant is estimated on the date of grant by use of the Black-Scholes option pricing model.

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	For the Nine Months Ended September 30,		For the Three Months Ended September 30,	
	2003	2002	2003	2002
	-----	-----	-----	-----
Net income (loss), as reported	\$ 437,394	(95,001)	325,659	14
Less stock-based compensation				

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expense determined under fair value method for all stock options, net of related income tax benefit	(26,000)	(22,164)	--
	-----	-----	-----
Pro forma net income	411,394	(117,165)	325,659
Basic income (loss) per share, as reported	.24	(.06)	.14
Basic income (loss) per share, pro forma	.22	(.07)	.14
Diluted income (loss) per share, as reported	.13	(.06)	.08
Diluted income (loss) per share, pro forma	.12	(.07)	.08

In February 2003, the Company granted 104,000 options to six of the Board of Directors. The options, which are immediately exercisable, were issued at \$.25 per share (which was not less than the fair market value on the date of the grant) and expire in ten years. No expense was recorded as a result.

(10) NEW ACCOUNTING PRONOUNCEMENTS

In November 2002, the FASB issued FASB Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others" ("FIN 45"). FIN 45 requires that upon issuance of guarantee, a guarantor must recognize a liability for the fair value of an obligation assumed under a guarantee. FIN 45 also requires additional disclosures by a guarantor in its interim and annual financial statements about the obligations associated with guarantees issued. The recognition provisions of FIN 45 will be effective for any guarantees that are issued or modified after December 31, 2002. The adoption of FIN 45 did not have an impact on the Company's consolidated financial statements.

In January 2003, the FASB issued Interpretation No. 46 (FIN 46), "Consolidation of Variable Interest Entities, an interpretation of ARB No. 51". FIN 46 addresses the consolidation by business enterprises of variable interest entities, as defined in the Interpretation. FIN 46 is effective for all new variable interest entities created or acquired after December 15, 2003. The Company does not believe that the adoption of FIN 46 will have any impact on the Company's consolidated financial statements.

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In May 2003, the FASB issued Statement No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity." Statement No. 150 changes the accounting guidance for certain financial instruments that, under previous guidance, could be classified as equity or "mezzanine" equity by now requiring those instruments to be classified as liabilities (or assets in some circumstances) in the statement of financial position. Further, Statement No. 150 requires disclosure regarding the terms of those instruments and settlement alternatives. Statement No. 150 is generally effective for all financial instruments entered into or modified after

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May 31, 2003 and is otherwise effective at the beginning of the first interim period beginning after June 15, 2003. The adoption of this pronouncement will not have any impact on the Company's financial position and results of operations.

In January 2003, the Company adopted the FASB's Emerging Issue Task Force (EITF) Issue No. 02-16 "Accounting by a Reseller for Cash Consideration Received from a Vendor" ("EITF 02-16"). The consensus reached by the EITF addressed the accounting for "Cash Consideration" (which includes slotting fees, cooperative advertising payments, etc.). The consensus of the EITF establishes an overall presumption that the cash received from vendors is a reduction in the price of vendor's products and should be recognized accordingly as a reduction in the cost of sales at the time the related inventory is sold. Some consideration could be characterized as a reduction of expense if the cash received represents a reimbursement of specific, incremental, identifiable costs incurred by the retailer to sell the vendor's products.

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

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," "intends," 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.

Results of Operations - Three Months Ended September 30, 2003 and 2002

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The Company reported net income of \$325,659 for the three months ended September 30, 2003, as compared to net income of \$142,394 in the 2002 quarter.

Net sales increased \$729,802. This increase primarily reflects an increase in sales to other wholesale distributors and increased market penetration. Gross margins on sales during the same period increased by 1.1% to 28.5%, due to overall product mix. Selling, general and administrative expenses increased \$110,942 primarily due to increased personnel, offset by the fact that the third quarter of 2002 had \$178,873 of non-recurring professional and other fees relating to the Company's secured credit line and its guarantee of the credit line obligations of Atlantic.

Interest expense decreased \$4,686 due primarily to the fact that prime rates decreased and Universal's borrowing rate on its revolving line of credit

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decreased, partially offset by the interest incurred on the \$2.5 million term loan assumed by Universal on November 21, 2002 (see Liquidity and Capital Resources below for further details).

During the third quarter of 2003, the Company recorded a state tax provision of \$42,801, as compared to the third quarter of 2002, when the Company recorded a state tax provision of \$15,802.

Results of Operations - Nine Months Ended September 30, 2003 and 2002

The Company reported net income of \$437,394 for the third quarter of 2003, as compared to a net loss of \$95,001 in the prior year.

Net sales increased \$3,372,731, as a result of an increase in sales to other wholesale distributors, favorable winter weather conditions and increased market penetration. Gross margins remained relatively even at 28.6%. Selling, general and administrative expense increased \$462,605 primarily due to increased personnel, offset by the fact that the nine months ended September 30, 2002 had \$344,385 of non-recurring professional and other fees relating to the Company's secured credit line and its guarantee of the credit line obligations of Atlantic.

Interest expense increased \$10,610 mainly due primarily to the \$2.5 million term loan assumed by Universal on November 21, 2002 (see Liquidity and Capital Resources below for further details), offset by the fact that prime rates decreased and Universal's borrowing rate on its revolving line of credit decreased.

The Company recorded a state tax provision of \$72,208 and a federal tax benefit of \$91,371 for the nine months ended September 30, 2003, as compared to the nine months ended September 30, 2002, when the Company recorded a state tax provision of \$17,509.

Liquidity and Capital Resources

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As of September 30, 2003, the Company had \$487,897 in cash and cash equivalents compared with \$296,764 at December 31, 2002.

Between December 31, 2002 and September 30, 2003, the only material changes in obligations associated with operating agreements, obligations to financial institutions and other long-term debt obligations was that the borrowings on the credit line increased by \$1,940,994, primarily due to the acquisition of RAL (see further details below).

Cash flows provided by operations were \$399,725 during the nine months ended September 30, 2003. Accounts payable increased due primarily to increased inventory purchases resulting from an overall increase in sales. The increase in accounts payable was offset by the corresponding increase in inventory, as well as an increase in accounts receivable. Accounts receivable increased due to an increase in sales in the third quarter of 2003 and timing of customer payments.

Cash flows used in investing activities of \$290,213 during the nine months ended September 30, 2003 were due to purchases of property and equipment totaling \$293,788 less \$3,575 cash acquired. On September 30, 2003, the Company, through its newly formed, wholly owned subsidiary, RAL Purchasing, Inc., purchased substantially all of the assets and certain liabilities of RAL Supply Group, Inc. ("RAL"). The purchase price of \$2,447,061 paid at closing was funded

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by \$2,147,061 of borrowings on the Company's credit facility, and 5-year, 9% notes issued by RAL Purchasing, Inc. to a third party in the amount of \$300,000. The 5-year notes are guaranteed by the Company. The Company's limit on its credit facility was increased by \$1,500,000 to \$13,500,000, as a result of the acquisition.

The cash flows provided by financing activities of \$81,621 were from net repayments on the credit facility of \$206,067, net repayments on notes payable of \$47,088 and the proceeds of the issuance of stock through a private placement. On July 16, 2003, the Company completed a private placement pursuant to Regulation D of the Securities Act of 1933. The Company raised \$240,600 through the issuance of 802,000 shares of Common Stock at \$0.30 per share. The stock was sold to officers and directors of the Company and one private investor. The proceeds of the private placement were used for general working capital purposes.

On January 28, 2002, Atlantic, a wholly-owned subsidiary of the Company, filed a voluntary petition with the U. S. Bankruptcy Court for the Eastern District of New York to reorganize under Chapter 11 of the U. S. Bankruptcy Code. The Company is not part of the Chapter 11 filing. The business of Atlantic is conducted by one employee whose sole function is to collect on accounts receivables for the benefit of Atlantic's creditors, and the company does not believe that Atlantic will emerge from the reorganization with any value for the Company.

On November 21, 2002, the Company released from its guarantees of the indebtedness (approximately \$5.8 million) by Atlantic to the Company's and Atlantic's lending bank, in return for the agreement by the Company and Universal to pay to the

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bank \$2.5 million as a five-year term loan under the Company's line of credit with the bank, or, if earlier, on demand by the bank.

At September 30, 2003, amounts outstanding under the credit facility were \$12,291,883, of which, (i) \$142,000 represents a term loan payable in 7 remaining equal monthly installments of approximately \$21,000 and (ii) \$2,280,000 represents a separate term loan payable in 50 remaining monthly installments of agreed amounts under an amortization schedule. Although the term loans are payable over specified periods, 7 and 50 months, respectively, the Bank can demand payment at any time.

The Company believes that the credit facility is sufficient to finance its current operating needs.

RECENT ACCOUNTING PRONOUNCEMENTS

In November 2002, the FASB issued FASB Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, including Indirect Guarantees of Indebtedness of Others" ("FIN 45"). FIN 45 requires that upon issuance of guarantee, a guarantor must recognize a liability for the fair value of an obligation assumed under a guarantee. FIN 45 also requires additional disclosures by a guarantor in its interim and annual financial statements about the obligations associated with guarantees issued. The recognition provisions of FIN 45 will be effective for any guarantees that are issued or modified after December 31, 2002. The adoption of FIN 45 did not have an impact on the Company's consolidated financial statements.

In January 2003, the FASB issued Interpretation No. 46 (FIN 46),

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"Consolidation of Variable Interest Entities, an interpretation of ARB No. 51" FIN 46 addresses the consolidation by business enterprises of variable interest entities, as defined in the interpretation. FIN 46 is effective for all new variable interest entities created or acquired after December 15, 2003. The Company does not believe that the adoption of FIN 46 will have any impact on the Company's consolidated financial statements.

In May 2003, the FASB issued Statement No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity." Statement No. 150 changes the accounting guidance for certain financial instruments that, under previous guidance, could be classified as equity or "mezzanine" equity by now requiring those instruments to be classified as liabilities (or assets in some circumstances) in the statement of financial position. Further, Statement No. 150 requires disclosure regarding the terms of those instruments and settlement alternatives. Statement No. 150 is generally effective for all financial instruments entered into or modified after May 31, 2003 and is otherwise effective at the beginning of the first interim period beginning after June 15, 2003. The adoption of this pronouncement will not have any impact on the Company's financial position and results of operations.

In January 2003, the Company adopted the FASB's Emerging Issue Task Force (EITF) Issue No. 02-16 "Accounting by a Reseller for Cash Consideration Received from

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a Vendor" ("EITF 02-16"). The consensus reached by the EITF addressed the accounting for "Cash Consideration" (which includes slotting fees, cooperative advertising payments, etc.). The consensus of the EITF establishes an overall presumption that the cash received from vendors is a reduction in the price of vendor's products and should be recognized accordingly as a reduction in the cost of sales at the time the related inventory is sold. Some consideration could be characterized as a reduction of expense if the cash received represents a reimbursement of specific, incremental, identifiable costs incurred by the retailer to sell the vendor's products.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company's pre-tax earnings and cash flows are exposed to changes in interest rates as all borrowings under its credit facility bear interest based on the prime rate plus 0.5%, except for the \$2.5 million term loan, which bears interest at a rate of prime plus 2.5%. A hypothetical 10% adverse change in such rates would reduce the pre-tax earnings and cash flow by approximately \$60,000 over a one-year period, assuming the borrowing level remains consistent with the outstanding borrowings as of September 30, 2003. 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 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

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The Company's senior management is responsible for establishing and maintaining a system of disclosure controls and procedures (as defined in Rule 13a-14 and 15d-14 under the Securities Exchange Act of 1934 (the "Exchange Act")) designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported as specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Act is accumulated and communicated to the issuer's management, including its principal executive officer or officers and principal financial officer or officers, or persons performing similar functions, as appropriate to allow them to make informed decisions regarding required disclosure.

The Company has evaluated the effectiveness of the design and operation of its disclosure controls and procedures under the supervision of and with the participation of management, including the Chief Executive Officer and Chief Financial Officer within 90 days prior to the filing date of this report. Based on that evaluation our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure

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controls and procedures are effective in alerting them to material information required to be included in our periodic Securities and Exchange Commission filings.

(b) CHANGES IN INTERNAL CONTROLS

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

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

On January 28, 2002, Atlantic, a wholly-owned subsidiary of the Company, filed a voluntary petition with the U. S. Bankruptcy Court for the Eastern District of New York to reorganize under Chapter 11 of the U. S. Bankruptcy Code. The Company and its other operations are not part of the Chapter 11 filing. The business of Atlantic is today conducted by one employee, whose sole function is to collect on accounts receivables for the benefit of Atlantic's creditors, and the Company does not believe that Atlantic will emerge from the reorganization with any value for the Company.

Item 6. Exhibits and Reports on Form 8-K

a. Exhibits:

- | | |
|------|--|
| 31.1 | Certification of Chief Executive Officer Pursuant to Rule 15d-14 of the Securities and Exchange Act of 1934, as amended, as Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of Chief Financial officer Pursuant to Rule 15d-14 of the Securities and Exchange Act of 1934, as amended, as Pursuant to Section 302 of the |

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Sarbanes-Oxley Act of 2002.

32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes- Oxley Act of 2002.

32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes- Oxley Act of 2002.

b. Reports on Form 8-K:

None

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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: February 19, 2004

COLONIAL COMMERCIAL CORP.

/S/ BERNARD KORN

Bernard Korn,
Chairman of the Board and President

/S/ JAMES W. STEWART

James W. Stewart,
Executive Vice President and Treasurer

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