

INDUSTRIAL SERVICES OF AMERICA INC /FL
Form 10-Q/A
November 14, 2007

FORM 10-Q/A

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

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

For the quarterly period ended June 30, 2007

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 0-20979

INDUSTRIAL SERVICES OF AMERICA, INC.

(Exact Name of Registrant as specified in its Charter)

Florida

(State or other jurisdiction of
Incorporation or Organization)

59-0712746

(IRS Employer
Identification No.)

7100 Grade Lane, PO Box 32428

Louisville, Kentucky 40232

(Address of principal executive offices)

(502) 368-1661

(Registrant's Telephone Number, Including Area Code)

Check 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 X 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.

(Check one): Large accelerated filer ___ Accelerated filer ___ Non-accelerated filer X

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of June 30, 2007: 3,640,899.

EXPLANATORY NOTE

We are filing this Form 10-Q/A, which serves as a first amendment to our Form 10-Q for the quarterly period ended June 30, 2007, as originally filed on August 8, 2007, to correct the table related to Contractual Obligations under Part I, Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations. We have moved \$3,000,000 of the amount that we included for the 3-5 year period in connection with Long-Term Obligations to the 1-3 year column after discovery of the fact that our credit facility with Branch Banking and Trust Company comes due in December 2009, which falls within the 1-3 year column rather than the 3-5 year column. We have made no other changes to the Form 10-Q as filed on August 8, 2007, other than newly executed Rule 13a-14(a) and Section 1350 Certifications.

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

The following discussion and analysis should be read in conjunction with our consolidated financial statements and the accompanying notes thereto included elsewhere in this report.

The following discussion and analysis contains certain financial predictions, forecasts and projections which constitute "forward-looking statements" within the meaning of the federal securities laws. Actual results could differ materially from those financial predictions, forecasts and projections and there can be no assurance that we will achieve such financial predictions, forecasts and projections. Factors that could affect financial predictions, forecasts and projections include the fluctuations in the commodity price index and any conditions internal to our major customers, including loss of their accounts and other factors as listed in our Form 10-K for the year ended December 31, 2006, as filed with the Securities and Exchange Commission.

General

We are primarily focusing our attention now and in the future towards our recycling business segment. We sell processed ferrous and non-ferrous scrap material to end-users such as steel mini-mills, integrated steel makers, foundries and refineries. We purchase ferrous and non-ferrous scrap material primarily from industrial and commercial generators of steel, iron, aluminum, copper, stainless steel and other metals as well as from other scrap dealers who deliver these materials directly to our facilities. We process these materials by sorting, shearing, cutting and/or baling. We will also continue to focus on initiating growth in our management services business segment and our waste and recycling equipment sales, service and leasing division.

We continue to pursue a growth strategy in the waste management services arena by adding new locations of existing customers as well as marketing our services to potential customers. Currently, we service 1,730 customer locations throughout the United States and we utilize an active database of over 6,300 vendors to provide timely, thorough and cost-effective service to our customers.

Our goal is to remain dedicated to the recycling, management services, and equipment industry while sustaining steady growth at an acceptable profit, adding to our net worth, and providing positive returns for stockholders. We intend to increase efficiencies and productivity in our core business while remaining alert for possible acquisitions, strategic partnerships, mergers and joint-ventures that would enhance our profitability.

We have operating locations in Louisville, Kentucky, Seymour, Indiana, and Dallas, Texas and a new facility in New Albany, Indiana. We closed our Lexington location in the first quarter of 2007. We do not have operating locations outside the United States.

Liquidity and Capital Resources

As of June 30, 2007 we held cash and cash equivalents of \$1,452,261.

We currently maintain a \$10.0 million senior revolving credit facility with the Branch Banking and Trust Company. This revolving credit facility has a three year term, provides for advances of up to eighty percent (80%) of our eligible accounts receivable and up to forty percent (40%) of eligible inventory, and up to one hundred percent (100%) of our net book value of eligible equipment less an outstanding indebtedness on the equipment. The revolving credit facility bears interest at the one month LIBOR rate, as published in the Wall Street Journal, plus two and twenty-five one-hundredths percent (2.25%) per annum, 7.57% as of June 30, 2007, and is secured by all our assets (except rental fleet equipment). As of June 30, 2007 we had borrowed \$3,000,000 and as of December 31, 2006 we had borrowed \$1,010,875 against this credit line. The revolving credit facility contains certain restrictive and financial covenants. At June 30, 2007, we were in compliance with all restrictive covenants.

We also have a \$2.0 million loan with Fifth Third Bank secured by our rental fleet equipment. Indebtedness under this loan agreement accrues interest at a fixed interest rate of 6.83%. The maturity date under this agreement is June 2011 with a ten-year amortization schedule. As of June 30, 2007 we had borrowed \$1,855,572 and as of December 31, 2006 we had borrowed \$1,929,016 against this loan. The terms of the loan agreement place certain restrictive covenants on us, including maintenance of a specified tangible net worth, debt to net worth and EBITDA ratio. Consequently, these covenants restrict our ability to incur as much additional debt as we may desire for future growth. At June 30, 2007, we were in compliance with all restrictive covenants.

During the first two quarters of 2007, we paid \$1,072,828 for land, improvements, property and equipment. We paid \$241,785 for property in New Albany, Indiana, located across the Ohio River from Louisville, Kentucky, the site of our headquarters. In the recycling segment we paid \$513,585 for cranes, shear rebuild, scales, trailers, and other operating equipment. Additionally we purchased an excavator via a capital lease valued at \$190,200. In the equipment sales, leasing and service segment, we purchased \$247,195 in rental equipment that we located at customer sites. This rental fleet equipment consists of solid waste handling and recycling equipment such as compactors, pre-crushers, containers and balers. It is our intention to continue to pursue this market. We purchased \$70,263 of office equipment. We also reclassified \$460,516 of construction-in-progress to capital assets.

Also, the Board of Directors at its June 21, 2007 meeting announced authorization to proceed with the purchase of a TSC 80 SXS shredder and complementary facility improvements totaling five million dollars. The selection of the TSC 80 SXS shredding plant will allow us to provide better quality scrap to our consumers, while at the same time broadening the type of scrap that we can process. Our intention is to process many types of heavy grades of scrap that we presently process by shearing and to make specialty shredder grades of material for specific consumers. We plan to finance the purchase of the shredder using our \$10 million senior revolving credit facility or by attracting new capital. The project is scheduled for completion in 2008.

We have a purchasing card with a credit limit of \$6.0 million. We included the balance due on the purchasing card as part of accounts payable. The outstanding balance on the purchasing card at June 30, 2007 was \$717,088 with a due date of July 27, 2007. The card accrues interest at prime plus 5.9% after the first twenty-five days of the purchase; our intention is to pay off the full balance every month so as to not incur finance charges. To date we have not incurred any interest charges on this purchasing card. The card requires monthly minimum payments on any balance outstanding at month end. We receive rebates on an annual basis for all purchases made with the card.

We expect that existing cash flow from operations and available credit under our existing credit facilities will be sufficient to meet our cash needs during the remainder of 2007.

Results of Operations

The following table presents, for the years indicated, the percentage relationship that certain captioned items in our Consolidated Statements of Operations bear to total revenues and other pertinent data:

	<u>Six months ended June</u>	
	<u>2007</u>	<u>30,</u> <u>2006</u>
Statements of Operations Data:		
Total Revenue	100.0%	100.0%
Cost of goods sold.....	84.7%	86.0%
Selling, general and administrative expenses	8.1%	8.7%
Income before other expenses.....	7.2%	5.3%

Six months ended June 30, 2007 compared to six months ended June 30, 2006

Total revenue increased \$5,246,191 or 16.3% to \$37,432,845 in 2007 compared to \$32,186,654 in 2006. Recycling revenue increased \$5,329,402 or 20.2% to \$28,895,786 in 2007 compared to \$23,566,384 in 2006. This is primarily due to a 22% increase in price of commodities in the recycling market. Management services revenue decreased \$221,390 or 2.9% to \$7,492,503 in 2007 compared to \$7,713,893 in 2006. Equipment sales, service and leasing revenue increased \$138,179 or 15.2% to \$1,044,556 in 2007 compared to \$906,377 in 2006. This increase is due to an increase in rental revenue.

Total cost of goods sold increased \$4,023,981 or 14.5% to \$31,714,280 in 2007 compared to \$27,690,299 in 2006. Recycling cost of goods sold increased \$4,116,003 or 20.2% to \$24,498,867 in 2007 compared to \$20,382,864 in 2006. This is primarily due to 25% higher commodity purchase prices in the recycling market. Management services cost of goods sold decreased \$86,275 or 1.3% to \$6,785,338 in 2007 compared to \$6,871,613 in 2006. Additionally, we reduced cost of goods sold by \$142,544 in 2007 and by \$300,000 in 2006 due to a change in management's estimate related to the liability associated with this operation which includes the contract settlement with our former customers. Equipment sales, service and leasing cost of goods sold decreased \$5,747 or 1.3% to \$430,075 in 2007 compared to \$435,822 in 2006.

Selling, general and administrative expenses increased \$213,071 or 7.6% to \$3,013,208 in 2007 compared to \$2,800,137 in 2006. As a percentage of revenue, selling, general and administrative expenses were 8.0% in 2007 compared to 8.7% in 2006. The primary driver of the increase in total expenses is property repairs and maintenance, which increased \$202,650 due to repairs to the premises.

Other income (expense) decreased \$43,705 to other expense of (\$41,118) in 2007 compared to other income of \$2,587 in 2006. This was primarily due to an increase in loss on disposal of assets of \$36,314 and an increase in interest expense of \$16,883.

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Income tax provision increased \$370,338 to \$1,049,860 in 2007 compared to \$679,522 in 2006. The effective tax rate in 2007 was 39.4% compared to 40.0% in 2006 based on federal and state statutory rates.

Three months ended June 30, 2007 compared to three months ended June 30, 2006

Total revenue increased \$1,825,462 or 10.3% to \$19,528,096 in 2007 compared to \$17,702,634 in 2006. Recycling revenue increased \$1,901,115 or 14.1% to \$15,364,200 in 2007 compared to \$13,463,085 in 2006. This is primarily due to a 62% increase in price of commodities in the recycling market. Management services revenue decreased \$120,697 or 3.2% to \$3,648,276 in 2007 compared to \$3,768,974 in 2006. Equipment sales, service and leasing revenue increased \$45,044 or 9.6% to \$515,620 in 2007 compared to \$470,575 in 2006. This increase is due to an increase in rental revenue.

Total cost of goods sold increased \$1,227,687 or 8.1% to \$16,472,512 in 2007 compared to \$15,244,825 in 2006. Recycling cost of goods sold increased \$1,305,200 or 11.2% to 12,965,403 in 2007 compared to \$11,660,202 in 2006. This is due to 40% higher commodity purchase prices in the recycling market. Management services cost of goods sold decreased \$74,215 or 1.0% to \$3,297,917 in 2007 compared to \$3,372,132 in 2006. Additionally, we reduced cost of goods sold by \$107,266 in 2007 and by \$150,000 in 2006 due to a change in management's estimate related to the liability associated with this operation which includes the contract settlement with our former customers. Equipment sales, service and leasing cost of goods sold decreased \$3,298 or 1.6% to \$209,192 in 2007 compared to \$212,491 in 2006.

Selling, general and administrative expenses increased \$198,917 or 13.7% to \$1,649,201 in 2007 compared to \$1,450,284 in 2006. As a percentage of revenue, selling, general and administrative expenses were 8.4% in 2007 compared to 8.2% in 2006. The primary driver of the increase in total expenses is property repairs and maintenance, which increased \$198,000 due to property improvements.

Other expense increased \$40,981 to \$43,912 in 2007 compared to \$2,931 in 2006 primarily due to a decrease in gain/increase in loss on sale of assets.

Income tax provision increased \$139,335 to \$541,172 in 2007 compared to \$401,837 in 2006. The effective tax rate in 2007 was 39.7% compared to 40.0% in 2006 based on federal and state statutory rates.

Financial condition at June 30, 2007 compared to December 31, 2006

Cash and cash equivalents increased \$120,454 to \$1,452,261 as of June 30, 2007 compared to \$1,331,807 as of December 31, 2006.

We used net cash from operating activities of \$653,683 for the six months ended June 30, 2007. Primarily this was due to an increase in accounts receivable of \$2,427,873.

We used net cash from investing activities of \$1,008,858 for the six months ended June 30, 2007. Primarily, we purchased recycling and rental fleet equipment of \$1,072,828. The rental fleet equipment consists of solid waste handling and recycling equipment such as compactors, containers and balers. It is our intention to continue to pursue this market.

Our net cash from financing activities of \$1,782,995 for the six months ended June 30, 2007 is primarily due to the advance of \$4,350,000 on our line of credit offset by payments on debt of \$2,434,319.

Accounts receivable trade increased \$2,427,873 or 48.3% to \$7,454,314 as of June 30, 2007 compared to \$5,026,441 as of December 31, 2006. This change is primarily due to an increase in selling prices in the Recycling segment.

Inventories consist principally of ferrous and nonferrous scrap materials and waste equipment machinery held for resale. We value inventory at the lower of cost or market. Inventory increased \$435,181 or 13% to \$3,863,407 as of June 30, 2007 compared to \$3,428,226 as of December 31, 2006.

Inventory aging for the period ended June 30, 2007 (Days Outstanding):

Description	1-30	31-60	61-90	Over 90	Total
Waste equipment machinery	\$ -	\$ -	\$ -	\$ 19,426	\$ 19,426
Ferrous materials	1,074,037	612,846	441,365	35,068	2,163,316
Non-ferrous materials	1,403,515	122,982	54,321	74,575	1,655,393
Other	<u>25,272</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>25,272</u>
	\$2,502,824	\$ 735,828	\$ 495,686	\$ 129,069	\$3,863,407

Inventory aging for the year ended December 31, 2006 (Days Outstanding):

Description	1-30	31-60	61-90	Over 90	Total
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Waste equipment machinery	\$ 33,720	\$ 22,480	\$ -	\$ -	\$ 56,200
Ferrous Materials	864,489	448,842	166,509	188,097	1,667,937
Non-ferrous materials	1,467,679	41,840	42,989	126,147	1,678,655
Other	<u>25,434</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>25,434</u>
	\$2,391,322	\$ 513,162	\$ 209,498	\$ 314,244	\$3,428,226

Accounts payable trade increased \$490,171 or 10.8% to \$5,035,228 as of June 30, 2007 compared to \$4,545,057 as of December 31, 2006, primarily due to market conditions.

Working capital increased \$2,886,952 to \$6,411,050 as of June 30, 2007 compared to \$3,524,098 as of December 31, 2006. The increase was primarily driven by the \$2.4 million increase in accounts receivable.

Contractual Obligations

The following table provides information with respect to our known contractual obligations for the quarter ended June 30, 2007.

Obligation Description	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Long-Term Debt Obligations (1)	\$4,855,572	\$154,607	\$3,342,671	\$1,358,294	\$0
Capital Lease Obligations (2)	353,900	231,398	122,502	0	0
Operating Lease Obligations (3)	<u>705,465</u>	<u>427,944</u>	<u>192,021</u>	<u>85,500</u>	<u>0</u>
Total	\$5,914,937	\$ 813,949	\$3,657,194	\$1,443,794	\$0

(1) We currently maintain a \$10.0 million senior revolving credit facility with the Branch Banking and Trust Company. Indebtedness under this credit facility accrues interest at BB&T's prime rate less one eighth. The maturity date under this agreement is December 2009. We have collateralized the credit facility with all our assets except our rental fleet.

We also have a \$2.0 million loan agreement with Fifth Third Bank. Indebtedness under this loan agreement accrues interest at a fixed interest rate of 6.83%. The maturity date is June 2011 with a ten-year amortization schedule and is collateralized by our rental fleet equipment.

(2) We lease various pieces of equipment that qualify for capital lease treatment. These lease arrangements require monthly lease payments expiring at various dates through April 2010.

(3) We lease the Louisville, Kentucky facility from K&R, LLC, the sole member of which is Harry Kletter, our chief executive officer, under an operating lease expiring December 2007. We have monthly rental payments of \$42,106 through December 2007. In the event of a change of control, the monthly payments become \$62,500. We also lease a management services operations facility and various pieces of equipment in Dallas, Texas for which monthly payments of \$2,525 are due through September 2007. We also lease security equipment for which monthly payments of \$464 are due through July 2009. We lease property in Lexington, Kentucky for which monthly payments of \$2,250 are due through January 2012, and we lease property in Louisiana for which monthly payments of \$5,250 are due through February 2009.

Impact of Recently Issued Accounting Standards

The Financial Accounting Standards Board has published SFAS No. 157, *Fair Value Measurements*, to eliminate the diversity in practice that exists due to the different definitions of fair value and the limited guidance for applying those definitions in GAAP that are dispersed among the many accounting pronouncements that require fair value measurements. SFAS No. 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (an exit price). SFAS No. 157 also stipulates that, as a market-based measurement, fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability, and establishes a fair value hierarchy that distinguishes between (a) market participant assumptions developed based on market data obtained from sources independent of the reporting entity (observable inputs) and (b) the reporting entity's own assumptions about market participant assumptions developed based on the best information available in the circumstances (unobservable inputs).

SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years, although earlier application is encouraged. Additionally, prospective application of the provisions of SFAS No. 157 is required as of the beginning of the fiscal year in which it is initially applied, except when certain circumstances require retrospective application.

Item 6. Exhibits

See exhibit index.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report on Form 10-Q/A to be signed on its behalf by the undersigned thereunto duly authorized.

INDUSTRIAL SERVICES OF AMERICA, INC.

Date: November 13, 2007

/s/ Harry Kletter
Chairman and Chief Executive Officer
(Principal Executive and Financial
Officer)

Date: November 13, 2007

/s/ Alan L. Schroering
Chief Financial Officer

INDEX TO EXHIBITS

<u>Exhibit Number</u>	<u>Description of Exhibits</u>
31.1	Rule 13a-14(a) Certification of Harry Kletter for the Form 10-Q/A for the quarter ended June 30, 2007.
31.2	Rule 13a-14(a) Certification of Alan Schroering for the Form 10-Q/A for the quarter ended June 30, 2007.
32.1	Section 1350 Certification of Harry Kletter and Alan Schroering for the Form 10-Q/A for the quarter ended June 30, 2007.

