SHARPS COMPLIANCE CORP
Form 10-Q
November 03, 2016

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, 2016
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: 001-34269

SHARPS COMPLIANCE CORP.
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Delaware | 74-2657168 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

| | |
|---|---|
| 9220 Kirby Drive, Suite 500, Houston, Texas | 77054 |
| (Address of principal executive offices) | (Zip Code) |

(713) 432-0300
(Registrant's telephone number, including area code)

Indicate by check mark if 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 has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes No

Indicate by check mark whether the registrant is a large accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule

12b-2 of the Securities Exchange Act of 1934.

| | | | |
|---|---|---|---|
| Large Accelerated Filer | Accelerated Filer | Non-accelerated Filer<br>(Do not check if a smaller reporting company) | Smaller reporting company |

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

As of October 31, 2016, there were 15,906,110 outstanding shares of the Registrant's common stock, par value $0.01 per share.

SHARPS COMPLIANCE CORP. AND SUBSIDIARIES

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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SHARPS COMPLIANCE CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(In thousands, except share and par value)

| | September 30, 2016 | June 30, 2016 |
|---|---|---|
| ASSETS | | |
| CURRENT ASSETS | | |
| Cash and cash equivalents | $ 6,908 | $ 12,435 |
| Accounts receivable, net of allowance for doubtful accounts of $67 and $63, respectively | 7,081 | 5,814 |
| Inventory, net | 4,205 | 3,919 |
| Prepaid and other current assets | 865 | 695 |
| TOTAL CURRENT ASSETS | 19,059 | 22,863 |
| PROPERTY, PLANT AND EQUIPMENT, net | 5,938 | 5,032 |
| OTHER ASSETS | 127 | 84 |
| GOODWILL | 6,724 | 1,039 |
| INTANGIBLE ASSETS, net of accumulated amortization of $653 and $502, respectively | 4,335 | 1,129 |
| TOTAL ASSETS | $ 36,183 | $ 30,147 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| CURRENT LIABILITIES | | |
| Accounts payable | $ 2,623 | $ 1,620 |
| Accrued liabilities | 1,921 | 1,534 |
| Current maturities of long-term debt | 783 | - |
| Deferred revenue | 2,673 | 2,477 |
| TOTAL CURRENT LIABILITIES | 8,000 | 5,631 |
| LONG-TERM DEFERRED REVENUE, net of current portion | 572 | 483 |
| OTHER LONG-TERM LIABILITIES | 183 | 190 |
| LONG-TERM DEBT, net of currrent portion | 2,383 | - |
| TOTAL LIABILITIES | 11,138 | 6,304 |
| COMMITMENTS AND CONTINGENCIES | | |
| STOCKHOLDERS' EQUITY | | |
| Common stock, $0.01 par value per share; 20,000,000 shares authorized; 16,199,953 and 15,740,458 shares issued, respectively and 15,904,338 and 15,444,843 shares outstanding, | 162 | 158 |

| | | |
|---|---|---|
| respectively | | |
| Treasury stock, at cost, 295,615 and 295,615 shares repurchased, respectively. | (1,554 ) | (1,554 ) |
| Additional paid-in capital | 27,496 | 25,331 |
| Accumulated deficit | (1,059 ) | (92 ) |
| TOTAL STOCKHOLDERS' EQUITY | 25,045 | 23,843 |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | $ 36,183 | $ 30,147 |

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

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SHARPS COMPLIANCE CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(In thousands, except per-share data)

| | Three-Months Ended September 30, 2016 | 2015 |
|---|---|---|
| REVENUES | $ 9,531 | $ 7,869 |
| Cost of revenues | 6,572 | 4,990 |
| GROSS PROFIT | 2,959 | 2,879 |
| | | |
| Selling, general and administrative | 3,699 | 2,596 |
| Depreciation and amortization | 200 | 52 |
| | | |
| OPERATING INCOME (LOSS) | (940 ) | 231 |
| | | |
| OTHERE INCOME (EXPENSE) | | |
| Interest income | 4 | 9 |
| Interest expense | (31 ) | - |
| TOTAL OTHER (EXPENSE) INCOME | (27 ) | 9 |
| | | |
| INCOME (LOSS) BEFORE INCOME TAXES | (967 ) | 240 |
| | | |
| INCOME TAX EXPENSE - Current | - | 20 |
| TOTAL INCOME TAX EXPENSE | - | 20 |
| | | |
| NET INCOME (LOSS) | $ (967 ) | $ 220 |
| | | |
| NET INCOME (LOSS) PER COMMON SHARE | | |
| Basic | $ (0.06 ) | $ 0.01 |
| | | |
| Diluted | $ (0.06 ) | $ 0.01 |
| | | |
| WEIGHTED AVERAGE SHARES USED IN COMPUTING NET INCOME (LOSS) PER COMMON SHARE: | | |
| | | |
| Basic | 15,868 | 15,419 |
| Diluted | 15,868 | 15,926 |

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

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SHARPS COMPLIANCE CORP. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(Unaudited)

(In thousands, except share data)

| | Common Stock | | Treasury Stock | | Additional Paid-in | Accumulated | Total Stockholders' |
|---|---|---|---|---|---|---|---|
| | Shares | Amount | Shares | Amount | Capital | Deficit | Equity |
| Balances, June 30, 2015 | 15,575,041 | $ 156 | (191,250) | $ (809) | $ 24,344 | $ (105) | $ 23,586 |
| | | | - | $ - | | | |
| Exercise of stock options | 112,425 | 1 | - | - | 312 | - | 313 |
| Stock-based compensation | - | - | - | - | 676 | - | 676 |
| Issuance of restricted stock | 52,992 | 1 | - | - | (1) | - | - |
| Shares repurchased | - | - | (104,365) | (745) | - | - | (745) |
| Net income | - | - | - | - | - | 13 | 13 |
| Balances, June 30, 2016 | 15,740,458 | 158 | (295,615) | (1,554) | 25,331 | (92) | 23,843 |
| | | | - | - | | | - |
| Exercise of stock options | 46,223 | - | - | - | 141 | - | 141 |
| Stock-based compensation | - | - | - | - | 139 | - | 139 |
| Issuance of common stock for acquisition | 413,272 | 4 | - | - | 1,885 | - | 1,889 |
| Net loss | - | - | - | - | - | (967) | (967) |
| Balances, September 30, 2016 | 16,199,953 | $ 162 | (295,615) | $ (1,554) | $ 27,496 | $ (1,059) | $ 25,045 |

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

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SHARPS COMPLIANCE CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In thousands)

| | Three-Months Ended September 30, 2016 | 2015 |
|---|---|---|
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net (loss) income | $ (967) | $ 220 |
| Adjustments to reconcile net (loss) income to net cash (used in) or provided by operating activities: | | |
| Depreciation and amortization | 338 | 188 |
| Loss on disposal of property, plant and equipment | 6 | - |
| Stock-based compensation expense | 139 | 141 |
| Changes in operating assets and liabilities, net of effects of business acqusitions: | | |
| Accounts receivable | (772) | 1,806 |
| Inventory | (252) | (681) |
| Prepaid and other assets | (213) | 180 |
| Accounts payable and accrued liabilities | 644 | (282) |
| Deferred revenue | 285 | 51 |
| NET CASH (USED IN) PROVIDED BY OPERATING ACTIVITIES | (792) | 1,623 |
| | | |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Purchase of property, plant and equipment | (806) | (462) |
| Cash proceeds from sale of property, plant and equipment | 13 | - |
| Payments for business acquisitions, net of cash acquired | (7,062) | (630) |
| NET CASH USED IN INVESTING ACTIVITIES | (7,855) | (1,092) |
| | | |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Proceeds from exercise of stock options | 141 | 268 |
| Proceeds from long-term debt | 3,000 | - |
| Repayments of long-term debt | (21) | - |
| NET CASH PROVIDED BY FINANCING ACTIVITIES | 3,120 | 268 |
| | | |
| NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS | (5,527) | 799 |
| | | |
| CASH AND CASH EQUIVALENTS, beginning of period | 12,435 | 15,157 |
| | | |
| CASH AND CASH EQUIVALENTS, end of period | $ 6,908 | $ 15,956 |
| | | |
| SUPPLEMENTAL CASH FLOW DISCLOSURES: | | |
| Income taxes paid | $ - | $ 85 |
| | | |
| Interest paid on long-term debt | $ 22 | $ - |
| | | |
| NON-CASH INVESTING & FINANCING ACTIVITIES: | | |
| | | |
| Issurance of common stock for acquisition | $ 1,889 | $ - |

| | | |
|---|---|---|
| Unpaid consideration related to acquistions | $ 140 | $ 70 |
| Transfer of equipment to inventory | $ 34 | $ - |
| Property, plant and equipment financed through accounts payable | $ 310 | $ - |

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

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

NOTE 1 - ORGANIZATION AND BACKGROUND

Organization: The accompanying unaudited condensed consolidated financial statements include the financial transactions and accounts of Sharps Compliance Corp. and its wholly owned subsidiaries, Sharps Compliance, Inc. of Texas (dba Sharps Compliance, Inc.), Sharps e-Tools.com Inc. ("Sharps e-Tools"), Sharps Manufacturing, Inc., Sharps Environmental Services, Inc. (dba Sharps Environmental Services of Texas, Inc.), Sharps Safety, Inc., Alpha Bio/Med Services LLC, Bio-Team Mobile LLC and Citiwaste, LLC (collectively, "Sharps" or the "Company"). All significant intercompany accounts and transactions have been eliminated upon consolidation.

Business: Sharps is a leading full-service national provider of comprehensive waste management services including medical, pharmaceutical and hazardous for small and medium quantity generators. The Company's solutions include Sharps Recovery System™ (formerly Sharps Disposal by Mail System®), TakeAway Medication Recovery System™, MedSafe®, TakeAway Recycle System™, ComplianceTRAC℠, SharpsTracer®, Sharps Secure® Needle Disposal System, Complete Needle™ Collection & Disposal System, TakeAway Environmental Return System™, Pitch-It IV™ Poles, Asset Return System and Spill Kit and Recovery System. The Company also offers its route-based pick-up service in an eleven (11) state region of the Northeast portion of the United States as well as in Texas and Louisiana.

NOTE 2 - BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission ("SEC") for interim financial information and with instructions to Form 10-Q and, accordingly, do not include all information and footnotes required under accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, these interim condensed consolidated financial statements contain all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of the consolidated financial position of the Company as of September 30, 2016, the results of its operations for the three months ended September 30, 2016 and 2015, cash flows for the three months ended September 30, 2016 and 2015 and stockholders' equity for the three months ended September 30, 2016 and the year ended June 30, 2016. The results of operations for the three months ended September 30, 2016 are not necessarily indicative of the results to be expected for the entire fiscal year ending June 30, 2017. These unaudited condensed consolidated financial statements should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended June 30, 2016.

NOTE 3 - SIGNIFICANT ACCOUNTING POLICIES

Revenue Recognition: The Company recognizes revenue when services are provided and from product sales when (i) goods are shipped or delivered, and title and risk of loss pass to the customer, (ii) the price is substantially fixed or determinable and (iii) collectability is reasonably assured except for those sales via multiple-deliverable revenue arrangements. Provisions for certain rebates, product returns and discounts to customers are accounted for as reductions in sales in the same period the related sales are recorded. Product discounts granted are based on the terms of arrangements with direct, indirect and other market participants, as well as market conditions, including prices charged by competitors. Rebates are estimated based on contractual terms, historical experience, trend analysis and projected market conditions in the various markets served. Service agreements which include a vendor managed inventory program include terms that meet the "bill and hold" criteria and as such are recognized when the order is completed, at which point title has transferred, there are no acceptance provisions and amounts are segregated in the Company's warehouse. During the three months ended September 30, 2016 and 2015, the Company recorded revenue from inventory builds that are held in vendor managed inventory under these service agreements of $1.0 million and

$0.6 million, respectively.  As of September 30, 2016 and June 30, 2016, $2.5 million and $2.1 million, respectively, of solutions sold through that date were held in vendor managed inventory pending fulfillment or shipment to patients of pharmaceutical manufacturers who offer these solutions to patients in an ongoing patient support program.

Certain products offered by the Company have revenue producing components that are recognized over multiple delivery points (Sharps Recovery System and various other solutions like the TakeAway Medication Recovery Systems referred to as “Mailbacks” and Sharps Pump and Asset Return Systems, referred to as “Pump Returns”) and can consist of up to three separate elements, or units of measure, as follows: (1) the sale of the compliance and container system, (2) return transportation and (3) treatment service.

In accordance with the relative selling price methodology, an estimated selling price is determined for all deliverables that qualify for separate units of accounting. The actual consideration received in a multiple-deliverable arrangement is then allocated to the units based on their relative sales price. The selling price for the transportation revenue and the treatment revenue utilizes third party evidence. The Company estimates the selling price of the compliance and container system based on the product and services provided, including compliance with local, state and federal laws, adherence to stringent manufacturing and testing requirements, safety to the patient and the community as well as storage and containment capabilities.

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

NOTE 3 - SIGNIFICANT ACCOUNTING POLICIES (continued)

Revenue for the sale of the compliance and container is recognized upon delivery to the customer, at which time the customer takes title and assumes risk of ownership. Transportation revenue is recognized when the customer returns the compliance and container system and the container has been received at the Company's owned or contracted facilities. The compliance and container system is mailed or delivered by an alternative logistics provider to the Company's owned or contracted facilities. Treatment revenue is recognized upon the destruction or conversion and proof of receipt and treatment having been performed on the container. Since the transportation element and the treatment elements are undelivered services at the point of initial sale of the compliance and container, transportation and treatment revenue is deferred until the services are performed. The current and long-term portions of deferred revenues are determined through regression analysis and historical trends. Furthermore, through regression analysis of historical data, the Company has determined that a certain percentage of all compliance and container systems sold may not be returned. Accordingly, a portion of the transportation and treatment elements are recognized at the point of sale.

Business Combinations: The Company includes the results of operations of the businesses that are acquired as of the respective dates of acquisition. The Company allocates the fair value of the purchase price of acquisitions to the assets acquired and liabilities assumed based on their estimated fair values. The excess of the fair value of the purchase price over the fair values of these identifiable assets and liabilities is recorded as goodwill.

Income Taxes: Deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. A valuation allowance is established when it is more likely than not that some portion or all of the deferred tax assets will not be realized. The establishment of a valuation allowance requires significant judgment and is impacted by various estimates. Both positive and negative evidence, as well as the objectivity and verifiability of that evidence, is considered in determining the appropriateness of recording a valuation allowance on deferred tax assets. Under generally accepted accounting principles, the valuation allowance has been recorded to reduce the Company's deferred tax assets to an amount that is more likely than not to be realized and is based upon the uncertainty of the realization of certain federal and state deferred tax assets related to net operating loss carryforwards and other tax attributes.

Accounts Receivable: Accounts receivable consist primarily of amounts due to the Company from normal business activities. Accounts receivable balances are determined to be delinquent when the amount is past due based on the contractual terms with the customer. The Company maintains an allowance for doubtful accounts to reflect the likelihood of not collecting certain accounts receivable based on past collection history and specific risks identified among uncollected accounts. Accounts receivable are charged to the allowance for doubtful accounts when the Company determines that the receivable will not be collected and/or when the account has been referred to a third party collection agency. The Company has a history of minimal uncollectible accounts.

Stock-Based Compensation: Stock-based compensation cost for options and restricted stock awarded to employees and directors is measured at the grant date, based on the calculated fair value of the award and is recognized as an expense over the requisite service period (generally the vesting period of the equity grant).

Fair Value of Financial Instruments: The Company considers the fair value of all financial instruments, including cash and cash equivalents, accounts receivable and accounts payable to approximate their carrying values at September 30, 2016 and June 30, 2016 due to their short-term nature. The carrying value of the Company's debt approximates fair value due to the market rates of interest.

Fair Value Measurements: The Company employs a hierarchy which prioritizes the inputs used to measure recurring fair value into three distinct categories based on the lowest level of input that is significant to the fair value measurement. Our methodology for categorizing assets and liabilities that are measured at fair value pursuant to this hierarchy gives the highest priority to unadjusted quoted prices in active markets and the lowest levels to unobservable inputs, summarized as follows:
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Level 1 – Quoted prices in active markets for identical assets or liabilities.
Level 2 – Other significant observable inputs (including quoted prices in active markets for similar assets or liabilities).
Level 3 – Significant unobservable inputs (including our own assumptions in determining fair value).

We use the cost, income or market valuation approaches to estimate the fair value of our assets and liabilities when insufficient market-observable data is available to support our valuation assumptions. The purchase price allocations relating to the acquisitions completed during the three months ended September 30, 2016 and year ended June 30, 2016 utilized level 3 inputs.

NOTE 4 – RECENTLY ISSUED ACCOUNTING STANDARDS

In May 2014, guidance for revenue recognition was issued which supersedes the revenue recognition requirements currently followed by the Company. The new guidance provides for a single five-step model to be applied in determining the amount and timing of the recognition of revenue related to contracts with customers. The new standard also requires additional financial statement disclosures that will enable users to understand the nature, amount, timing and uncertainty of revenue and cash flows relating to customer contracts. Companies have an option to use either a retrospective approach or cumulative effect adjustment approach to implement the standard. The guidance is effective for annual reporting periods beginning after December 15, 2017 (effective July 1, 2018 for the Company.) The Company is evaluating the impact that the new accounting guidance will have on its consolidated financial statements and related disclosures and has not yet determined the method by which it will adopt the standard.

In July 2015, guidance for inventory measurement was issued, which supersedes the policy currently followed by the Company. The new guidance requires the Company to measure inventory at the lower of cost and net realizable value. The provisions of the new guidance are effective for annual reporting periods beginning after December 15, 2016 (effective July 1, 2017 for the Company) including interim periods within that reporting period. The adoption of this guidance is not expected to have a material effect on the Company's consolidated financial statements.

In February 2016, guidance for leases was issued, which requires balance sheet recognition for rights and obligations of all leases with terms in excess of twelve months. The new guidance also requires additional disclosures about the amount, timing and uncertainty of cash flows arising from leases. The provisions of the new guidance are effective for annual periods beginning after December 15, 2018 (effective July 1, 2019 for the Company), including interim periods within the reporting period, and early application is permitted. The Company is currently evaluating the impact of the new guidance on its consolidated financial statements.

In March 2016, new guidance for stock-based compensation was issued, which simplifies the accounting for stock-based compensation related to income taxes and balance sheet and cash flow classifications. In addition, an entity can make an entity-wide accounting policy election to either estimate the number of awards that are expected to vest or account for forfeitures when they occur. The provisions of the new guidance are effective for annual reporting periods beginning after December 15, 2016 (effective July 1, 2017 for the Company) including interim periods within the reporting period. The Company is currently evaluating the impact of the new guidance on its consolidated financial statements.

NOTE 5 - INCOME TAXES

The establishment of valuation allowances requires significant judgment and is impacted by various estimates. Both positive and negative evidence, as well as the objectivity and verifiability of that evidence, is considered in determining the appropriateness of recording a valuation allowance on deferred tax assets. Under generally accepted accounting principles, the valuation allowance has been recorded to reduce the Company's net deferred tax asset to an amount that is more likely than not to be realized and is based upon the uncertainty of the realization of certain federal and state deferred tax assets related to net operating loss carryforwards and other tax attributes. The Company's net deferred tax assets have been fully reserved by a tax valuation allowance.

No state tax expense was recorded for the three months ended September 30, 2016 as it was not material due to the valuation allowance and net operating losses. The Company's effective tax rate for the three months ended September 30, 2015 was 8.3% reflecting estimated state income taxes. The Company's tax benefit associated with taxable losses during the three months ended September 30, 2016 was offset by a deferred tax valuation allowance. The Company's tax expense associated with taxable income during the three months ended September 30, 2015 was offset by the utilization of net operating loss carryforwards.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 6 - NOTES PAYABLE AND LONG-TERM DEBT

The Company's credit agreement, which was effective on April 9, 2015 with a commercial bank and subsequently amended on June 20, 2016 ("Credit Agreement"), provides for a $9.0 million line of credit facility, the proceeds of which may be utilized as follows: (i) $4.0 million for working capital, letters of credit (up to $1.0 million) and general corporate purposes and (ii) $5.0 million for acquisitions. Indebtedness under the Credit Agreement is secured by the Company's accounts receivable and inventory with advances outstanding under the working capital portion of the credit facility at any time limited to a Borrowing Base (as defined in the Credit Agreement) equal to 80% of eligible accounts receivable plus 50% of eligible inventory. Advances under the acquisition portion of the credit facility are limited to 75% of the purchase price of an acquired company and convert to a five-year term note. Borrowings bear interest at WSJ Prime (for the working capital line) and WSJ Prime plus 0.25% (for the acquisition line) with a floor of 3.0%. The interest rates, which were the same as of September 30, 2016 and June 30, 2016 were approximately 3.5% (for the working capital line) and 3.75% (for the acquisition line). The Company pays a fee of 0.25% per annum on the unused amount of the line of credit.

At September 30, 2016, long-term debt consisted of the following (in thousands, unaudited):

| | |
|---|---|
| Non-interest bearing, unsecured note payable assumed in acquisition (See Note 13), 27 monthly payments of $6,955; maturing September 2018. | $166 |
| Term loan, bearing interest at 3.75%, monthly payments of $50,000; maturing July 2021. | 3,000 |
| Total long-term debt | 3,166 |
| Less: current portion | 783 |
| Long-term debt, net of current portion | $2,383 |

As of September 30, 2016, the Company also had $0.3 million in letters of credit. The Company's availability under its credit facilities is currently approximately $5.7 million ($3.7 million for the working capital and $2.0 million for the acquisitions).

The Credit Agreement contains affirmative and negative covenants that, among other things, require the Company to maintain a minimum level of tangible net worth of $7.0 million, minimum liquidity of $6.0 million and a minimum debt service coverage ratio of not less than 1.15 to 1.00. The Credit Agreement, which expires on April 9, 2018, also contains customary events of default which, if uncured, may terminate the Credit Agreement and require immediate repayment of all indebtedness to the lenders. At September 30, 2016, the Company was in compliance with all the financial covenants under the Credit Agreement except the minimum debt service coverage ratio. A waiver was granted by the lender to the Company to cover the three months ended September 30, 2016. In addition, the lender agreed to revise the calculation of the debt service coverage ratio via an amendment executed in November 2016. With this amendment, the Company expects to be in compliance with all amended covenants for at least one year from the balance sheet date in this quarterly report.

Payments due on long-term debt during each of the five years subsequent to September 30, 2016 are as follows (in thousands, unaudited):

Year Ending September 30,

| | |
|---|---|
| 2017 | $783 |
| 2018 | 683 |
| 2019 | 600 |
| 2020 | 600 |
| 2021 | 500 |
| | $3,166 |

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

NOTE 7 – STOCK-BASED COMPENSATION

Stock-based compensation cost for options and restricted stock awarded to employees and directors is measured at the grant date, based on the calculated fair value of the award and is recognized as an expense over the requisite service period (generally the vesting period of the equity grant). During the three months ended September 30, 2016 and 2015, stock-based compensation amounts are as follows (in thousands):

| | Three-Months Ended September 30, | |
|---|---|---|
| | 2016 | 2015 |
| | (Unaudited) | |
| Stock-based compensation expense included in: | | |
| Cost of revenues | $ 12 | $ 8 |
| Selling, general and administrative | 127 | 133 |
| Total | $ 139 | $ 141 |

NOTE 8 - EARNINGS PER SHARE

Basic earnings per share is computed by dividing net income (loss) by the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed by dividing net income (loss) by the weighted average number of common shares after considering the additional dilution related to common stock options and restricted stock. In computing diluted earnings per share, the outstanding common stock options are considered dilutive using the treasury stock method.

The Company's restricted stock awards and escrow shares that were issued in connection with the Citiwaste acquisition are treated as outstanding for earnings per share calculations since these shares have full voting rights and are entitled to participate in dividends declared on common shares, if any, and undistributed earnings. As participating securities, the shares of restricted stock are included in the calculation of basic EPS using the two-class method. For the periods presented, the amount of earnings allocated to the participating securities was not material.

The following information is necessary to calculate earnings per share for the periods presented (in thousands, except per-share data):

| | Three-Months Ended September 30, | |
|---|---|---|
| | 2016 | 2015 |
| | (Unaudited) | |
| Net income (loss), as reported | $ (967 ) | $ 220 |
| Weighted average common shares outstanding | 15,868 | 15,419 |
| Effect of dilutive stock options | - | 507 |
| Weighted average diluted common shares outstanding | 15,868 | 15,926 |

| | | |
|---|---|---|
| Net income (loss) per common share | | |
| Basic | $ (0.06 ) | $ 0.01 |
| Diluted | $ (0.06 ) | $ 0.01 |
| | | |
| Employee stock options excluded from computation of dilutive income per share amounts because their effect would be anti-dilutive | 145 | 216 |

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

NOTE 9 - EQUITY TRANSACTIONS

During the three months ended September 30, 2016 and 2015, stock options to purchase shares of the Company's common stock were exercised as follows:

| | Three-Months Ended September 30, | |
|---|---|---|
| | 2016 | 2015 |
| | (Unaudited) | |
| Options Exercised | 46,223 | 101,425 |
| Proceeds (in thousands) | $ 141 | $ 268 |
| Average exercise price per share | $ 3.05 | $ 2.64 |

As of September 30, 2016, there was $0.4 million of stock option and restricted stock compensation expense related to non-vested awards which is expected to be recognized over a weighted average period of 2.3 years.

On January 7, 2013, the Company announced that its Board of Directors approved a stock repurchase program effective January 3, 2013, authorizing the Company to repurchase in the aggregate up to $3.0 million of its outstanding common stock over a two-year period. On March 5, 2015, the Board approved a two-year extension on the stock repurchase program through January 1, 2017. During the three months ended September 30, 2016 and 2015, Sharps repurchased no shares. Total shares repurchased under the program are 295,615 shares at a cost of $1.6 million. As of September 30, 2016, approximately $1.4 million remained of the Company's $3.0 million repurchase program.

NOTE 10 – GOODWILL AND INTANGIBLE ASSETS

At September 30, 2016 and June 30, 2016, intangible assets consisted of the following (in thousands, unaudited):

| | | September 30, 2016 | | | June 30, 2016 | | |
|---|---|---|---|---|---|---|---|
| | Estimated Useful Lives | Original Amount | Accumulated Amortization | Net Amount | Original Amount | Accumulated Amortization | Net Amount |
| Customer relationships | 7 years | $3,007 | $ (167) | $ 2,840 | $580 | $ (60) | $ 520 |
| Permits | 6 - 15 years | 1,211 | (215) | 996 | 668 | (191) | 477 |
| Patents | 5 - 17 years | 383 | (255) | 128 | 383 | (251) | 132 |
| Tradename | 7 years | 270 | (10) | 260 | - | - | - |
| Non-compete | 5 years | 117 | (6) | 111 | - | - | - |
| Total intangible assets, net | | $4,988 | $ (653) | $ 4,335 | $1,631 | $ (502) | $ 1,129 |

During the three months ended September 30, 2016 and 2015, amortization expense was $0.2 million and $20 thousand, respectively.

The changes in the carrying amount of goodwill since June 30, 2016 was as follows (in thousands, unaudited):

| | |
|---|---|
| Balance at June 30, 2016 | $ 1,039 |

| | |
|---|---|
| Goodwill acquired during the three months ended September 30, 2016 | 5,685 |
| Balance at September 30, 2016 | $6,724 |

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

NOTE 10 – GOODWILL AND INTANGIBLE ASSETS (continued)

As of September 30, 2016, future amortization of intangible assets is as follows (in thousands, unaudited):

| Year Ending September 30, | |
|---|---|
| 2017 | $616 |
| 2018 | 615 |
| 2019 | 615 |
| 2020 | 615 |
| 2021 | 615 |
| Thereafter | 1,259 |
| | $4,335 |

Future amortization expense may fluctuate depending on future changes in acquisition related assets or changes to the estimated amortizable life of the intangibles.

NOTE 11 – INVENTORY

The components of inventory are as follows (in thousands):

| | September 30, 2016 (Unaudited) | June 30, 2016 |
|---|---|---|
| Raw materials | $1,268 | 1,388 |
| Finished goods | 2,937 | 2,531 |
| Total | $4,205 | 3,919 |

NOTE 12 – REVENUES BY SOLUTION

Total revenues for the three months ended September 30, 2016 and 2015 were $9.5 million and $7.9 million, respectively. The Company has expanded its reporting to include information by solution reflecting recent changes in the Company's business primarily due to recent acquisitions.

| | Three-Months Ended September 30, | | | |
|---|---|---|---|---|
| | 2016 | % Total | 2015 | % Total |
| REVENUES BY SOLUTION: | | | | |
| Mailbacks | $6,249 | 65.5 % | $5,525 | 70.2 % |
| Route-based pickup services | 1,465 | 15.4 % | 361 | 4.6 % |
| Unused medications | 791 | 8.3 % | 1,002 | 12.7 % |
| Third party treatment services | 68 | 0.7 % | 79 | 1.0 % |
| Other[1] | 958 | 10.1 % | 902 | 11.5 % |
| Total revenues | $9,531 | 100.0 % | $7,869 | 100.0 % |

(1) The Company's other products include non-mailback products such as IV poles, accessories, containers, asset return boxes and other miscellaneous items.

NOTE 13 – ACQUISITIONS

Effective on July 17, 2015, the Company acquired Alpha Bio/Med Services LLC, a route-based pickup service located in Pennsylvania for total cash consideration of $0.7 million of which $0.1 million was withheld for payment of adjusted escrow amounts which settled in July 2016.

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

NOTE 13 – ACQUISITIONS (continued)

The following amounts represent the fair value of the assets acquired and liabilities assumed:

| | |
|---|---|
| Accounts receivable | $51 |
| Fixed assets | 70 |
| Intangibles | 267 |
| Goodwill | 413 |
| Accounts payable and accrued liabilities | (101) |
| Total purchase price | $700 |

Effective on December 14, 2015, the Company acquired Bio-Team Mobile LLC, a route-based pickup service located in Pennsylvania for total cash consideration of $1.0 million of which $0.1 million has been withheld for possible settlement amounts through December 2016.

The following amounts represent the fair value of the assets acquired and liabilities assumed:

| | |
|---|---|
| Accounts receivable | $42 |
| Fixed assets | 68 |
| Intangibles | 313 |
| Goodwill | 626 |
| Accounts payable and accrued liabilities | (16) |
| Total purchase price | $1,033 |

Effective July 1, 2016, the Company acquired Citiwaste, LLC ("Citiwaste"), a route-based pickup service located in New York, which is in the business of medical, pharmaceutical and hazardous waste management primarily in the healthcare industry. The purchase price consists of $7.0 million in cash ($3.0 million of which was borrowed under the acquisition portion of its Credit Agreement), 413,272 shares of common stock of the Company (the "Common Stock Consideration"), which constitutes approximately 3.0% of the total outstanding shares of common stock of the Company, and a lease obligation to be paid to the seller for $0.1 million which is presented on the balance sheet in accrued liabilities for a total consideration of $9.0 million.  The issuance of the Common Stock Consideration was not registered under the Securities Act of 1933, as amended, and was issued pursuant to an exemption from the registration requirements thereunder.  The Company will hold 139,216 shares of the Common Stock Consideration in escrow for a one-year period to cover the indemnification obligations of the Sellers under the Agreement.

For the three months ended September 30, 2016, the Company recognized approximately $0.8 million in revenues and $0.1 million in net income related to the acquisition of Citiwaste.

The following amounts represent the fair value of the assets acquired and liabilities assumed:

| | |
|---|---|
| Cash | $5 |
| Accounts receivable | 495 |
| Fixed assets | 30 |
| Intangibles | 3,357 |
| Goodwill | 5,685 |

| | |
|---|---|
| Accounts payable and accrued liabilities | (356 ) |
| Debt assumed | (187 ) |
| Total purchase price | $9,029 |

The amounts recorded for certain assets and liabilities are preliminary in nature and are subject to adjustments to working capital. The actual amounts recorded at the completion of the measurement period may differ materially from the information presented in the accompanying unaudited condensed combined financial information.

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

NOTE 13 – ACQUISITIONS (continued)

During the three months ended September 30, 2016 and 2015, the Company incurred $0.7 million and $0.1 million of acquisition related expenses for investment banking, legal and accounting fees which are included within selling, general and administrative expenses in the condensed consolidated statements of operations. The results of operations of the acquired business have been included in the condensed consolidated statements of operations from the date of acquisition. Pro forma results of operations for Alpha Bio/Med Services and Bio-Team Mobile are not presented because the pro forma effects, individually or in the aggregate, were not material to the Company's consolidated results of operations. The goodwill recorded as of September 30, 2016 for Alpha Bio/Med Services, Bio-Team Mobile, and Citiwaste will be deductible for income taxes. The goodwill recognized for the acquisitions since July 1, 2015 is attributable to expected revenue synergies generated by the integration of our products and services with those acquisitions, cost synergies resulting from the consolidation or elimination of certain functions, and intangible assets that do not qualify for separate recognition such as the assembled workforce of each acquisition.

Supplemental Pro Forma Data

Citiwaste's financial results have been included in our condensed consolidated financial results for the three months ended September 30, 2016. The following table presents summarized unaudited pro forma financial information as if Citiwaste had been included in the Company's results for the three months ended September 30, 2015 (in thousands):

| | September 30, 2015 (Unaudited) |
|---|---|
| Revenues | $ 8,600 |
| Net income | $ 177 |

The basic and diluted earnings per common share is not affected by the pro forma results above nor the issuance of common stock consideration.

The unaudited supplemental pro forma financial data above has been calculated after applying the Company's accounting policies and adjusting the historical results of Citiwaste with pro forma adjustments, net of tax, that assume the acquisition occurred on July 1, 2015.

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ITEM 2.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

INFORMATION REGARDING FORWARD-LOOKING STATEMENTS

This quarterly report on Form 10-Q contains certain forward-looking statements and information relating to the Company and its subsidiaries that are based on the beliefs of the Company's management as well as assumptions made by and information currently available to the Company's management. When used in this report, the words "may," "position," "plan," potential," "continue," "anticipate," "believe," "expect," "estimate," "project" and "intend" and words or ph similar import, as they relate to the Company or its subsidiaries or Company management, are intended to identify forward-looking statements. Such statements reflect the known and unknown risks, uncertainties and assumptions related to certain factors, including without limitations, competitive factors, general economic conditions, customer relations, relationships with vendors, governmental regulation and supervision, seasonality, distribution networks, product introductions and acceptance, technological change, changes in industry practices, onetime events and other factors described herein. Based upon changing conditions, should any one or more of these risks or uncertainties materialize, or should any underlying assumptions prove incorrect, actual results may vary materially from those described herein as anticipated, believed, expected, estimated or intended. Consequently, no forward-looking statements can be guaranteed. When considering these forward-looking statements, you should keep in mind the risk factors and other cautionary statements in this Quarterly Report on 10-Q or refer to our Annual Report on Form 10-K. Actual results may vary materially. You are cautioned not to place undue reliance on any forward-looking statements. You should also understand that is not possible to predict or identify such factors and as such should not consider the preceding list or the risk factors to be a complete list of all potential risks and uncertainties. The Company does not intend to update these forward-looking statements.

GENERAL

Sharps Compliance Corp. is a leading full-service national provider of comprehensive waste management services including medical, pharmaceutical and hazardous. Our solutions facilitate the proper collection, containment, transportation and treatment of numerous types of healthcare-related materials, including hypodermic needles, lancets and other devices or objects used to puncture or lacerate the skin, or sharps, hazardous waste and unused consumer dispensed medications and over-the-counter drugs. We serve customers in multiple markets such as home health care, retail clinics and immunizing pharmacies, pharmaceutical manufacturers, professional offices (physicians, dentists and veterinarians), assisted living and long-term care facilities (assisted living, continuing care, long-term acute care, memory care and skilled nursing), government (federal, state and local), consumers, commercial and agriculture, as well as distributors to many of the aforementioned markets. We assist our customers in determining which of our solution offerings best fit their needs for the collection, containment, return transportation and treatment of medical waste, used healthcare materials, pharmaceutical waste, hazardous waste and unused dispensed medications. Our differentiated approach provides our customers the flexibility to return and properly treat medical waste, used healthcare materials or unused dispensed medications through a variety of solutions and products transported primarily through the United States Postal Service ("USPS"). For customers with facilities or locations that may generate larger quantities of medical waste, we integrate the route-based pick-up service into our complete offering. The benefits of this comprehensive offering include single point of contact, consolidated billing, integrated manifest and proof of destruction repository in addition to our cost savings. Furthermore, we provide comprehensive tracking and reporting tools that enable our customers to meet complex medical, pharmaceutical and hazardous waste disposal and compliance requirements. We believe the fully-integrated nature of our operations is a key factor leading to our success and continued recurring revenue growth. We continue to take advantage of the many opportunities in all markets served as we educate the market place and as prospective customers become more aware of alternatives to traditional methods of disposal (i.e., route-based pick-up services).

Our key markets include heathcare facilities, pharmaceutical manufacturers, home healthcare providers, assisted living/long-term care, surgery centers, retail pharmacies and clinics and the professional market which is comprised of physicians, dentists and veterinary practices. The Company's flagship product, the Sharps® Recovery System, is a comprehensive solution for the containment, transportation, treatment and tracking of medical waste and used healthcare materials. In October 2014, the Company launched MedSafe®, a patent pending solution for the safe collection, transportation and proper disposal of unwanted and expired prescription medications including controlled substances from ultimate users. MedSafe has been designed to meet or exceed the new regulations issued by the Drug Enforcement Administration ("DEA") implementing the Secure and Responsible Drug Disposal Act of 2010 (the "Act") which became effective October 9, 2014. In July 2015 and December 2015, the Company augmented its network of medical and hazardous waste service providers with acquisitions of a route-based pickup services in the Northeast serving Pennsylvania, Maryland, Ohio and other neighboring states. Additionally, the Company now services parts of Texas and Louisiana with route-based pickup service. In July 2016, the Company acquired another route-based pickup service which expanded service to New York and New Jersey and strengthened the Company's position in the Northeast where we serve an eleven contiguous state region. Our other solutions include TakeAway Medication Recovery System™, TakeAway Recycle System™, ComplianceTRAC℠, Universal Waste Shipback Systems, TakeAway Environmental Return System™, SharpsTracer®, Sharps Secure® Needle Disposal System™, Complete Needle™ Collection & Disposal System, Pitch-It IV™ Poles, Asset Return System, Sharps® MWMS™ (a Medical Waste Management System ("MWMS")) and Spill Kit and Recovery System.

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RESULTS OF OPERATIONS

The following analyzes changes in the consolidated operating results and financial condition of the Company during the three months ended September 30, 2016 and 2015. The following table sets forth, for the periods indicated, certain items from the Company's Condensed Consolidated Statements of Operations, dollars in thousands and percentages expressed as a percentage of revenue:

| | Three-Months Ended September 30, | | | |
|---|---|---|---|---|
| | 2016 | % | 2015 | % |
| | (Unaudited) | | | |
| Revenues | $9,531 | 100.0 % | $7,869 | 100.0 % |
| | | | - | |
| Cost of revenues | 6,572 | 69.0 % | 4,990 | 63.4 % |
| Gross profit | 2,959 | 31.0 % | 2,879 | 36.6 % |
| SG&A expense | 3,699 | 38.8 % | 2,596 | 33.0 % |
| Depreciation and amortization | 200 | 2.1 % | 52 | 0.7 % |
| Operating income (loss) | $(940 ) | (9.9 %) | $231 | 2.9 % |
| Interest income | 4 | | 9 | |
| Interest expense | (31 ) | | - | |
| Total other income (expense) | (27 ) | (0.3 %) | 9 | 0.1 % |
| Income (loss) before income taxes | (967 ) | (10.1 %) | 240 | 3.0 % |
| Income tax expense | - | 0.0 % | 20 | |