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SHARPS COMPLIANCE CORP
Form 10QSB
May 11, 2005

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-QSB

- QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the quarterly period ended March 31, 2005
- TRANSITION REPORT UNDER SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 for the transition period from to .

Commission File Number: 0-22390

SHARPS COMPLIANCE CORP.
(Name of small business issuer in its Charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

74-2657168
(I.R.S. Employer Identification No.)

9350 Kirby Drive, Suite 300, Houston, Texas
(Address of principal executive offices)

77054
(Zip Code)

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

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

Yes No

APPLICABLE ONLY TO CORPORATE ISSUERS

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: 10,538,144 shares of Common Stock, \$0.01 par value as of May 6, 2005.

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

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

ASSETS

March 31,
2005

June 30,
2004

(Unaudited)

CURRENT ASSETS:

Cash and cash equivalents	\$255,302	\$242,803
Restricted cash	10,010	14,678
Accounts receivable, net of allowance of \$19,828 and \$12,896, respectively	776,915	981,408

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Inventory	426,388	393,238
Prepaid and other assets	87,669	138,798
	-----	-----
TOTAL CURRENT ASSETS	1,556,284	1,770,925
PROPERTY AND EQUIPMENT, net of accumulated depreciation of \$614,278 and \$507,945, respectively	447,972	539,800
INTANGIBLE ASSETS, net of accumulated amortization of \$102,041 and \$101,582, respectively	9,592	10,051
	-----	-----
TOTAL ASSETS	\$2,013,848	\$2,320,776
	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	\$480,200	\$592,943
Accrued liabilities	245,456	338,153
Deferred revenue - pump return	59,980	110,702
Current portion of deferred revenue - incineration	96,247	108,299
Current portion of deferred revenue - transportation	696,870	553,938
Notes payable and current portion of long-term debt	-	185,932
Current maturities of capital lease obligations	46,324	37,513
	-----	-----
TOTAL CURRENT LIABILITIES	1,625,077	1,927,480
LONG-TERM DEFERRED REVENUE - INCINERATION, net of current portion	22,180	30,408
LONG-TERM DEFERRED REVENUE - TRANSPORTATION, net of current portion	203,630	179,506
LONG-TERM DEBT, net of current portion	-	10,826
OBLIGATIONS UNDER CAPITAL LEASES, net of current maturities	55,043	84,446
OTHER LIABILITIES	61,750	45,500
	-----	-----
TOTAL LIABILITIES	1,967,680	2,278,166
COMMITMENTS AND CONTINGENCIES	-	-
STOCKHOLDERS' EQUITY		
Common stock, \$.01 par value per share; 20,000,000 shares authorized; 10,538,144 and 10,538,256 shares issued and outstanding, respectively	105,381	105,381
Additional paid-in capital	7,457,639	7,457,639
Accumulated deficit	(7,516,852)	(7,520,410)
	-----	-----

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TOTAL STOCKHOLDERS' EQUITY	46,168	42,610
	-----	-----
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$2,013,848	\$2,320,776
	=====	=====

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

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SHARPS COMPLIANCE CORP. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	For the Three Months Ended March 31,	
	2005	2004
		(Unaudited)
REVENUES:		
Distribution, net	\$ 2,123,791	\$ 2,000,030
Consulting and environmental services	108,853	79,916
TOTAL REVENUES	2,232,644	2,079,946
COSTS AND EXPENSES:		
Cost of revenues	1,398,141	1,234,515
Selling, general and administrative	892,494	864,047
Depreciation and amortization	37,798	40,253
TOTAL COSTS AND EXPENSES	2,328,434	2,138,815
OPERATING LOSS	(95,789)	(58,869)
OTHER EXPENSE		
Interest expense	(5,123)	(9,980)
Other	-	(316)
TOTAL OTHER EXPENSE	(5,123)	(10,296)
NET LOSS BEFORE INCOME TAXES	(100,912)	(69,165)
INCOME TAXES	4,693	-
NET LOSS	\$ (96,219)	\$ (69,165)
	=====	=====
NET LOSS PER COMMON SHARE		
Basic	\$ (.01)	\$ (.01)
	=====	=====

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Diluted	\$ (01)	\$ (.01)
=====		
WEIGHTED AVERAGE SHARES USED IN COMPUTING NET		
LOSS PER COMMON SHARE		
Basic	10,538,144	10,538,256
=====		
Diluted	10,538,144	10,538,256
=====		

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

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SHARPS COMPLIANCE CORP. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	For the Nine Months Ended March 31,	
	2005	2004

	(Unaudited)	
REVENUES:		
Distribution, net	\$ 6,609,598	\$ 5,895,720
Consulting and environmental services	271,477	255,658
TOTAL REVENUES	6,881,075	6,151,378

COSTS AND EXPENSES:		
Cost of revenues	4,116,632	3,703,825
Selling, general and administrative	2,621,420	2,498,772
Depreciation and amortization	121,054	118,501
TOTAL COSTS AND EXPENSES	6,859,106	6,321,098

OPERATING INCOME (LOSS)	21,969	(169,720)
OTHER INCOME EXPENSE		
Interest income	-	48
Interest expense	(18,411)	(37,875)
Other	-	(556)
TOTAL OTHER EXPENSE	(18,411)	(38,383)

NET INCOME (LOSS) BEFORE INCOME TAXES	3,558	(208,103)
INCOME TAXES	-	-

NET INCOME (LOSS)	\$3,558	\$ (208,103)
=====		

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NET INCOME (LOSS) PER COMMON SHARE

Basic	\$-	\$ (.02)
	=====	=====
Diluted	\$-	\$ (.02)
	=====	=====

WEIGHTED AVERAGE SHARES USED IN COMPUTING NET INCOME (LOSS) PER COMMON SHARE

Basic	10,538,144	10,345,074
	=====	=====
Diluted	10,980,340	10,345,074
	=====	=====

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

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

	For the Nine Months Ended March 31,	
	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES:		(Unaudited)
Net income (loss)	\$3,558	\$ (208,103)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	121,053	118,501
Bad debt expense	6,842	-
Gain on disposal of equipment	275	556
Changes in operating assets and liabilities:		
Decrease in restricted cash	4,668	140,735
(Increase) decrease in accounts receivable	197,651	(74,209)
Increase in inventory	(33,150)	(76,823)
Decrease in prepaids and other assets	51,129	13,602
Increase (decrease) in accounts payable and accrued liabilities	(189,190)	37,828
Increase (decrease) in deferred revenue	96,054	(81,832)
	-----	-----
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	258,890	(129,745)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(37,986)	(43,760)
Disposal of fixed asset	17,876	-
Patent	-	(10,409)
	-----	-----
NET CASH USED IN INVESTING ACTIVITIES	(20,110)	(54,169)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payment on notes payable	(31,675)	(115,895)

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Net payments on factoring agreement	(165,085)	(169,420)
Payments on capital lease obligations	(29,523)	(18,315)
Issuance of common stock	-	500,000
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	(226,282)	196,370
NET INCREASE IN CASH AND CASH EQUIVALENT	12,499	12,456
CASH AND CASH EQUIVALENTS, beginning of period	242,803	135,884
CASH AND CASH EQUIVALENTS, end of period	\$255,302	\$148,340
NONCASH INVESTING AND FINANCING ACTIVITIES:		
Property and equipment additions acquired under capital lease	\$8,931	\$9,752

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

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

March 31, 2005

NOTE 1. ORGANIZATION AND BACKGROUND

The accompanying 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.) and Sharps Safety, Inc. (collectively, "Sharps" or the "Company"). All significant intercompany accounts and transactions have been eliminated upon consolidation.

NOTE 2. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission ("SEC") and, accordingly, do not include all information and footnotes required under accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, these interim condensed consolidated financial statements contain all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of the consolidated financial position of the Company as of March 31, 2005 and the results of its operations and cash flows for the three and nine months ended March 31, 2005 and 2004. The results of operations for the three

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and nine months ended March 31, 2005, are not necessarily indicative of the results to be expected for the entire fiscal year ending June 30, 2005. These condensed consolidated financial statements should be read in conjunction with the Company's Annual Report on Form 10-KSB for the year ended June 30, 2004.

Certain reclassifications have been made in the prior year consolidated statement of operations to conform to current year presentation.

NOTE 3. REVENUE RECOGNITION

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

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NOTE 4. ACCOUNT RECEIVABLE

In September and October 2003, the Company secured judgments against Ameritech Environmental, Inc. ("Ameritech") totaling \$176,958 related to the non-payment by Ameritech for services provided by the Company in 2002. The assets of Ameritech representing collateral for the judgments were sold by Ameritech to MedSolutions, Inc. of Dallas, Texas ("MedSolutions") in November 2003. In January 2004, the Company secured a Garnishment Order against MedSolutions whereby MedSolutions was ordered to pay to the Company \$170,765, plus interest at 5%. Payments under the Garnishment Order are scheduled to be made monthly in the amount of \$4,375 (inclusive of interest) with a balloon payment of \$137,721 due November 7, 2004. MedSolutions is currently in breach of the Garnishment Order. In January 2005, the Company filed suit against MedSolutions and Ameritech in the 234th Judicial District Court of Harris County, Texas. The suit alleges collusion, fraudulent conveyance and fraudulent inducement by and between MedSolutions and Ameritech to defraud payment to the Company for amounts owed, as described above. The Company has also requested the Court to appoint a Receiver for all sums owed to protect assets pending review by the Court.

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In the quarters ending March 31, 2003 and June 30, 2003, the Company wrote-off all outstanding amounts, \$75,996 and \$106,397 respectively, due from Ameritech. Therefore, any potential future recoveries of receivables would be recorded as a credit to the allowance for bad debts. Any recovery that may be received by the Company will be reduced by collection-related legal fees estimated at one-third of any amounts collected. Although the Company will continue to aggressively pursue collection of the outstanding amounts under the Garnishment Orders, no assurances regarding collection can be made.

NOTE 5. NOTES PAYABLE AND LONG-TERM DEBT

Notes payable and long-term debt consisted of the following:

	March 31, 2005	June 30, 2004
	----- (Unaudited)	
Factoring agreement with financial institution	\$ -	\$ 165,083
Note payable to Futura	-	13,889
Promissory note to a finance company for the purchase of an automobile	-	17,786
	-----	-----
	-	196,758
Less: current portion of notes payable and long-term debt	-	185,932
	-----	-----
Total notes payable and long-term debt	\$ -	\$ 10,826
	=====	=====

The Company maintains an arrangement with a financial institution for a \$1.25 million asset-based line of credit. The agreement allows the Company to factor customer receivables generated out of its ordinary course of business. The maximum amount available under the line of credit is \$1.0 million (or \$1.25 million of its gross receivable balance). The agreement is automatically renews on an annual basis (August 30 of each year) unless terminated by either party. The Company may borrow up to 80% of the eligible receivables presented and incurs interest on gross invoices financed at a prime rate of interest plus 2%, plus administrative fees of .25% on gross receivables presented. The interest rate decreases to prime plus 1.25% (versus 2%) at such times as the Company's Adjusted Quick Ratio is 1.25 to 1.00 or greater. Adjusted Quick Ratio is defined as cash plus accounts receivable (less than 90 days from invoice date), divided by current liabilities less deferred revenue. During the quarter ended March 31, 2005, there were no borrowings under the arrangement.

NOTE 6. OBLIGATIONS UNDER CAPITAL LEASES

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Capital lease obligations consist of the following:

	March 31, 2005	June 30, 2004
Capital lease for the purchase of accounting and operating system software and hardware, due in monthly installments of \$4,061, interest imputed at 21% through February 2007	\$ 76,613	\$ 99,315
Capital lease for purchase of phone system due in monthly installments of \$455, interest imputed at 12% through August 2007	11,399	14,315
Capital lease for purchase of copier/printer due in monthly installments of \$157, interest imputed at 21% through August 2006	2,173	3,252
Capital lease for purchase of phone system upgrades due in monthly installments of \$157, interest imputed at 16% through December 2007	4,217	5,077
Capital lease for purchase of forklift due in monthly installments of \$290, interest imputed at 11% through July 2007	6,965	-
	101,367	121,959
Less: current portion	46,324	37,513
	\$ 55,043	\$ 84,446

NOTE 7. STOCK-BASED COMPENSATION

The Company adopted Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation", but elected to continue to account for its employee stock-based compensation plan under Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees" and its related interpretations in accounting for its stock option plan. While the Company continues to use APB No. 25, pro forma information regarding net income (loss) and earnings per share is required under SFAS No. 123 and SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure - an amendment of SFAS Statement No. 123", including that the information be determined as if the Company had accounted for its stock options under the fair value method prescribed by SFAS No. 123.

The Company uses the Black-Scholes option valuation model to value options granted. Because changes in input assumptions can materially affect the fair value estimate, the existing model may not necessarily provide the only measure of fair value for the employee stock options.

The Company used the following weighted-average assumptions for options granted during the quarters ended March 31, 2005 and 2004, as follows: risk-free interest rates of 4.33% and 4.04%, respectively; expected annual dividend yield

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of 0%; volatility factors of the expected market price of the Company's common stock of approximately 50% and 45%, respectively; and a weighted-average expected life of the options of 7 years.

Had compensation expense for stock based compensation been determined consistent with the provisions of SFAS No. 123 (and as amended by SFAS No. 148), the Company's net loss for the quarters ended March 31, 2005 and 2004, respectively, would have been increased, as follows:

	Three Months Ended March 31,	
	2005	2004
	(Unaudited)	(Unaudited)
Net loss, as reported	\$ (96,219)	\$ (69,165)
Less: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	\$ (66,473)	\$ (73,911)
	\$ (162,692)	\$ (143,076)
	\$ (162,692)	\$ (143,076)
Basic and diluted net loss per share, as reported	\$ (.01)	\$ (.01)
	\$ (.01)	\$ (.01)
Basic and diluted net loss per share, pro forma	\$ (.02)	\$ (.01)
	\$ (.02)	\$ (.01)

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Had compensation expense for stock based compensation been determined consistent with the provisions of SFAS No. 123 (and as amended by SFAS No. 148), the Company's net income (loss) for the nine months ended March 31, 2005 and 2004, respectively, would have been increased, as follows:

	Nine Months Ended March 31,	
	2005	2004
	(Unaudited)	(Unaudited)
Net income (loss), as reported	\$ 3,558	\$ (208,103)
Less: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	\$ (197,520)	\$ (221,225)
	\$ (193,962)	\$ (429,328)
	\$ (193,962)	\$ (429,328)
Basic and diluted net loss per share, as reported	\$ -	\$ (.02)
	\$ -	\$ (.02)

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Basic and diluted net loss per share, pro forma \$ (.01) \$ (.04)
 =====

NOTE 8. EARNINGS PER SHARE

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

	Nine Months Ended March 31,	
	2005	2004
Net income (loss), as reported	\$ 3,558	\$ (208,103)
Weighted average common shares outstanding	10,538,144	10,345,074
Effect of Dilutive stock options	442,196	-
Weighted average diluted common shares outstanding	10,980,340	10,345,074
Net income per common share		
Basic	\$ -	\$ 0.02
Diluted	\$ -	\$ 0.02

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ITEM 2.

MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATIONS

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

GENERAL

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Sharps is a leading developer of cost effective solutions for improving safety and efficiency related to the proper disposal of medical waste by industry and consumers. These solutions include Sharps Disposal by Mail System(TM), Pitch-It(TM) IV Poles, Trip LesSystem(TM), Sharps Pump Return Box, Sharps Enteral Pump Return Box, Sharps Secure(TM), Sharps SureTemp Tote(TM), IsoWash(TM) Linen Recovery System, Sharps e-Tools, Sharps Environmental Services and Sharps Consulting. Some products and services facilitate compliance with state and federal regulations by tracking, incinerating and documenting the disposal of medical waste. Additionally, some products and services facilitate compliance with educational and training requirements required by federal, state, and local regulatory agencies.

The Pro-Tec product line offers medical sharps disposal containers, specialized for safe disposal of biomedical waste in a full range of services. The Pro-Tec product line is a vertical business integration of the sharps disposal by mail products for the Company. The Company will have savings in product cost on its Sharps Disposable by Mail System(TM) and sales to third parties of this product.

RESULTS OF OPERATIONS

The following analyzes changes in the consolidated operating results and financial condition of the Company during the three months and nine months ended March 31, 2005 and 2004.

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

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2005	2004	2005	2004
Net revenues	100%	100%	100%	100%
Costs and expenses:				
Cost of revenues	(63%)	(59%)	(60%)	(60%)
Selling, general and administrative	(40%)	(42%)	(38%)	(41%)
Depreciation and amortization	(2%)	(2%)	(2%)	(2%)
Total operating expenses	(105%)	(103%)	(100%)	(103%)
Income (loss) from operations	(5%)	(3%)	0%	(3%)
Net income (loss)	(4%)	(3%)	0%	(3%)

THREE MONTHS ENDED MARCH 31, 2005, COMPARED TO THREE MONTHS ENDED MARCH 31, 2004

Total revenues for the three months ended March 31, 2005 of \$2,232,645 increased

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by \$152,699, or 7%, over the total revenues for the three months ended March 31, 2004 of \$2,079,946. The increase in revenues is primarily attributable to increased billings in the Agriculture (\$115,259), Health Care (\$29,066), and Hospitality (\$23,269) markets.

Cost of revenues for the three months ended March 31, 2005 of \$1,398,141 were 63% of revenues, which were higher than the cost of revenues for the three months ended March 31, 2004 of \$1,234,515, or 59% of revenues. The increase was due to; (i) increased revenues over the corresponding prior year period and (ii) cost increases incurred during the three months ended March 31, 2005.

Selling, general and administrative ("S, G&A") expenses for the three months ended March 31, 2005 of \$892,494, increased by \$28,447, or 3%, versus \$864,047 for the corresponding period of the previous year. The increase was consistent with the revenue growth of the business for the three months ended March 31, 2005 versus March 31, 2004.

NINE MONTHS ENDED MARCH 31, 2005, COMPARED TO NINE MONTHS ENDED MARCH 31, 2004

Total revenues for the nine months ended March 31, 2005 of \$6,881,075 increased by \$729,697, or 12%, over the total revenues for the nine months ended March 31, 2004 of \$6,151,378. The increase in revenues is primarily attributable to increased billings in the Agriculture (\$349,191), Healthcare (\$254,041), Retail (\$180,213) and Hospitality (\$94,667) markets.

Cost of revenues for the nine months ended March 31, 2005 of \$4,116,632 were 60% of revenues versus \$3,703,825, or 60% of the revenues for the corresponding period of the previous year.

Selling, general and administrative ("S, G&A") expenses for the nine months ended March 31, 2005 of \$2,621,418, increased by \$122,648, or by 5%, versus \$2,498,772 for the corresponding period of the previous. The increase in the S,G&A is primarily a result of increases in the following expenses: (i) compensation and commissions (\$79,043), (ii) advertising and promotions (\$21,947), (iii) employment placement (\$21,000), and (iv) computer costs (\$13,703).

LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents increased by \$12,499 to \$255,302 at March 31, 2005 from \$242,803 at June 30, 2004.

Accounts receivable decreased by \$204,493 to \$776,915 at March 31, 2005 from \$981,408 at June 30, 2004. The decrease was consistent with the decrease in revenues during the quarter ending March 31, 2005 of \$2,232,644 as compared to the revenues during the quarter ending June 2004 of \$2,468,015.

Property and equipment decreased by \$91,828 to \$447,972 at March 31, 2005 from \$539,800 at June 30, 2004. This decrease is primarily attributable to depreciation expense recognized for the corresponding nine-month period.

Accounts payable decreased by \$112,743 to \$480,200 at March 31, 2005 from \$592,943 at June 30, 2004. The decrease was due the timing of vendor payments.

Notes payable and long-term debt of \$196,758 at June 30, 2004 was completely repaid during the nine months ended March 31, 2005.

Management believes that the Company's current cash resources along with its asset-based factoring line of credit will be sufficient to fund operations for the twelve months ended March 31, 2006.

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The Company maintains an arrangement with a financial institution for a \$1.25 million asset-based line of credit. The agreement allows the Company to factor customer receivables generated out of its ordinary course of business. The maximum amount available under the line of credit is \$1.0 million (or \$1.25 million of its gross receivable balance). The agreement is automatically renews on an annual basis (August 30 of each year) unless terminated by either party. The Company may borrow up to 80% of the eligible receivables presented and incurs interest on gross invoices financed at a prime rate of interest plus 2%, plus administrative fees of .25% on gross receivables presented. The interest rate decreases to prime plus 1.25% (versus 2%) at such times as the Company's Adjusted Quick Ratio is 1.25 to 1.00 or greater. Adjusted Quick Ratio is defined as cash plus accounts receivable (less than 90 days from invoice date), divided by current liabilities less deferred revenue. During the quarter ended March 31, 2005, there were no borrowings under the arrangement.

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CRITICAL ACCOUNTING ESTIMATES

Certain products offered by the Company have revenue producing components that are recognized over multiple delivery points and can consist of up to three separate elements as follows: (1) the sale of the container system, (2) the transportation of the container system and (3) the treatment and disposal (incineration) of the container system. Since the transportation element and the incineration elements are undelivered services at the point of initial sale of the container, the revenue is deferred until the services are performed. The current and long-term portions of deferred revenues are determined through regression analysis and historical trends. Furthermore, through regression analysis of historical data, the Company has determined that a certain percentage of all container systems sold may not be returned. Accordingly, a portion of the transportation and incineration elements is recognized at the point of sale.

RECENTLY ISSUED ACCOUNTING STANDARDS

In January 2003, the FASB issued FASB Interpretation No. 46 ("FIN 46"), "Consolidation of Variable Interest Entities", and subsequently revised the interpretation in December 2003 ("FIN 46R") which requires that companies that control another entity through interests other than voting rights should consolidate the controlled entity. As revised, FIN 46R is generally effective for financial statements for interim or annual periods ending on or after March 15, 2004. The related disclosure requirements are effective immediately. Management does not believe the adoption of FIN 46R will have any impact on the Company's financial position or results of operations.

In April 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities", which amends SFAS No. 133 to provide clarification on the financial accounting and reporting of derivative instruments and hedging activities and requires that contracts with similar characteristics to be accounted for on a comparable basis. The provisions of SFAS No. 149 are effective for contracts entered into or modified after June 30, 2003, and for hedging relationships designated after June 30, 2003. The adoption of SFAS No. 149 will not have a material impact on the Company's results of operations or financial position.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity", which establishes standards on the classification and measurement of certain financial instruments with characteristics of both liabilities and equity. The provisions

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of SFAS No. 150 are effective for financial instruments entered into or modified after May 31, 2003 and to all other instruments that exist as of the beginning of the first interim financial reporting period beginning after June 15, 2003. The adoption of SFAS No. 150 did not have a material impact on the Company's results of operations or financial position.

In November 2004, the FASB issued FASB Statement No. 151, which revised ARB No. 43, relating to inventory costs. This revision is to clarify the accounting for abnormal amounts of idle facility expense, freight, handling costs and wasted material (spoilage). This Statement requires that these items be recognized as a current period charge regardless of whether they meet the criterion specified in ARB 43. In addition, this Statement requires the allocation of fixed production overheads to the costs of conversion be based on normal capacity of the production facilities. This Statement is effective for financial statements for fiscal years beginning after June 15, 2005. Earlier application is permitted for inventory costs incurred during fiscal years beginning after the date of this Statement is issued. Management believes this Statement will have no impact on the financial statements of the Company once adopted.

In December 2004, the FASB issued FASB Statement No. 152, which amends FASB Statement No. 66, Accounting for Sales of Real Estate, to reference the financial accounting and reporting guidance for real estate time-sharing transactions that is provided in AICPA Statement of Position (SOP) 04-2, Accounting for Real Estate Time-Sharing Transactions. This Statement also amends FASB Statement No. 67, Accounting for Costs and Initial Rental Operations of Real Estate Projects, to state that the guidance for (a) incidental operations and (b) costs incurred to sell real estate projects does not apply to real-estate time-sharing transactions. The accounting for those operations and costs is subject to the guidance in SOP 04-2. This Statement is effective for financial statements for fiscal years beginning after June 15, 2005. Management believes this Statement will have no impact on the financial statements of the Company once adopted.

In December 2004, the FASB issued FASB Statement No. 153. This Statement addresses the measurement of exchanges of nonmonetary assets. The guidance in APB Opinion No. 29, Accounting for Nonmonetary Transactions, is based on the principle that exchanges of nonmonetary assets should be measured based on the fair value of the assets exchanged. The guidance in that Opinion, however, included certain exceptions to that principle. This Statement amends Opinion 29 to eliminate the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. A nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. This Statement is effective for financial statements for fiscal years beginning after June 15, 2005. Earlier application is permitted for nonmonetary asset exchanges incurred during fiscal years beginning after the date of this Statement is issued. Management believes this Statement will have no impact on the financial statements of the Company once adopted.

In December 2004, the FASB issued Statement No. 123 (revised 2004) ("FAS 123 (R)"), Share-Based Payments. FAS 123 (R) requires all entities to recognize compensation expense in an amount equal to the fair value of share-based payments, such as stock options granted to employees. The Company is required to apply FAS 123 (R) on a modified prospective method. Under this method, the Company is required to record compensation expense (as previous awards continue

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to vest) for the unvested portion of previously granted awards that remain outstanding at the date of adoption. In addition, the Company may elect to adopt FAS 123 (R) by restating previously issued financial statements, basing the amounts on the expense previously calculated and reported in their pro forma disclosures that had been required by FAS 123. For public entities that file as small business issuers, FAS 123 (R) is effective as of the beginning of the first interim or annual reporting period that begins after December 15, 2005. Management has not completed its evaluation of the effect that FAS 123 (R) will have, but believes that the effect will be consistent with the application disclosed in its pro forma disclosures.

ITEM 3. CONTROLS AND PROCEDURES

Within the ninety days prior to the date of this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-14. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective in timely alerting them to material information relating to the Company (including its consolidated subsidiaries) required to be included in the Company's periodic SEC filings. There were no significant changes in the Company's internal controls or in other factors that could significantly affect these controls subsequent to the date of the Company's evaluation.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

In September and October 2003, the Company secured judgments against Ameritech Environmental, Inc. ("Ameritech") totaling \$176,958 related to the non-payment by Ameritech for services provided by the Company in 2002. Ameritech sold the assets of Ameritech representing collateral for the judgments to MedSolutions, Inc. of Dallas, Texas ("MedSolutions") in November 2003. In January 2004, the Company secured a Garnishment Order against MedSolutions whereby MedSolutions was ordered to pay to the Company \$170,765, plus interest at 5%. Payments under the Garnishment Order are scheduled to be made monthly in the amount of \$4,375 (inclusive of interest) with a balloon payment of \$137,721 due November 7, 2004. MedSolutions is currently in breach of the Garnishment Order. In January 2005, the Company filed suit against MedSolutions and Ameritech in the 234th Judicial District Court of Harris County, Texas. The suit alleges collusion, fraudulent conveyance and fraudulent inducement by and between MedSolutions and Ameritech to defraud payment to the Company for amounts owed, as described above. The Company has also requested the Court to appoint a Receiver for all sums owed to protect assets pending review by the Court.

On June 14, 2004, the Company provided Mr. Ronald E. Pierce, its then current Chief Operating Officer ("Mr. Pierce"), with notice of non-renewal of his employment agreement. As such, July 14, 2004 was Mr. Pierce's last day of employment. The Company has advised Mr. Pierce that under the terms of the employment contract no further compensation (including services) was due. The Company then received various letters from Mr. Pierce's attorney advising that Mr. Pierce is taking the position that the non-renewal of the employment agreement was not timely and, therefore, Mr. Pierce was terminated without cause. Additionally, Mr. Pierce claims that the Company had no right to terminate him on the anniversary date of his Agreement without the obligation of paying Mr. Pierce as if he were terminated without cause. Mr. Pierce has demanded severance related payments totaling approximately \$280,000 (including an \$80,000 bonus) along with the full accelerated vesting of 500,000 stock options previously awarded to Mr. Pierce. The Company believes that notice of such non-renewal was timely, and that in accordance with Mr. Pierce's employment

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agreement, the Company was entitled to provide notice thirty (30) days prior to the anniversary of its intent to terminate the agreement, and no severance would therefore be due to Mr. Pierce. On July 30, 2004, the Company received notice from Mr. Pierce's attorney requesting commencement of arbitration to resolve the claim. No further communications have been received from Mr. Pierce's attorney since July 30, 2004. The Company believes it has meritorious defenses against Mr. Pierce's claims and has not recorded a liability related to this matter.

On or about February 25, 2003, Jason Jodway, a then employee of the Company since April 1999, resigned in lieu of termination of employment by the Company. Thereafter, Mr. Jodway formed Attentus Medical Sales, Inc., a competing entity of the Company. In March 2005, the Company (through its wholly-owned subsidiary Sharps Compliance Inc.) filed a lawsuit in Harris County District Court, Texas

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against Mr. Jodway and Attentus Medical Sales, Inc. The lawsuit claims, (i) breach of a confidentiality agreement, (ii) misappropriation of trade secrets and (iii) tortious interference with the Company's existing and prospective contracts and business relationships. The Company intends to vigorously pursue its claim against Mr. Jodway and Attentus Medical Sales, Inc., though the Company has not quantified its damages to date. In April 2005, Mr. Jodway and Attentus Medical Sales, Inc. filed a general denial in the 152nd District Court of Harris County. Additionally, the defendant filed a counter-claim against Sharps Compliance Inc. asserting his last day of employment was March 28, 2003 and that he is entitled to receive back wages. The Company denies any obligation to Mr. Jodway for such back wages.

ITEM 2. CHANGES IN SECURITIES

On September 24, 2003 the Company completed a private placement of 625,000 shares of common stock at a price of \$0.80 per share. The proceeds of \$500,000 have been utilized by the Company for working capital purposes as well as to support growth plans to further expand the business into the industrial, retail, and other markets.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits:

31.1 Certification of Chief Executive Officer in Accordance with Section 302 of the Sarbanes-Oxley Act
(filed herewith)

31.2 Certification of Chief Financial Officer in Accordance with Section 302 of the Sarbanes-Oxley Act
(filed herewith)

32.1 Certification of Chief Executive Officer in Accordance with Section 906 of the Sarbanes-Oxley Act
(filed herewith)

32.2 Certification of Chief Financial Officer in Accordance with Section 906 of the Sarbanes-Oxley Act
(filed herewith)

ITEMS 3, 4, AND 5 ARE NOT APPLICABLE AND HAVE BEEN OMITTED.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, the registrant has duly caused this report to be signed on its behalf by the undersigned thereto duly authorized.

REGISTRANT:

SHARPS COMPLIANCE CORP.

Dated: May 11, 2005

By: /s/ Dr. Burton J. Kunik

Chairman of the Board, Chief
Executive Officer and President

Dated: May 11, 2005

By: /s/ David P. Tusa

Senior Vice President,
Chief Financial Officer
and Corporate Secretary