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SHARPS COMPLIANCE CORP  
Form 10QSB  
May 09, 2007

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, 2007
- 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.  
(Exact name of small business issuer as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

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

9220 Kirby Drive, Suite 500, 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

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

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: 11,808,100 shares of Common Stock, \$0.01 par value as of May 4, 2007.

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

	March 31, 2007
	----- (Unaudited)
ASSETS	
CURRENT ASSETS	
Cash and cash equivalents .....	\$ 1,591,114
Restricted cash .....	10,010
Accounts receivable, net of allowance for doubtful accounts of \$18,940 and \$20,024, respectively .....	1,327,840
Inventory .....	469,972
Prepaid and other assets .....	174,943
	-----
TOTAL CURRENT ASSETS .....	3,573,879

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PROPERTY AND EQUIPMENT, net of accumulated depreciation of \$901,077 and \$790,397, respectively .....	582,043
INTANGIBLE ASSETS, net of accumulated amortization of \$117,365 and \$116,805, respectively .....	62,074
	-----
TOTAL ASSETS .....	\$ 4,217,996 =====
LIABILITIES AND STOCKHOLDERS' EQUITY	
CURRENT LIABILITIES	
Accounts payable .....	\$ 641,701
Accrued liabilities .....	325,621
Deferred revenue .....	881,933
Current maturities of capital lease obligations .....	4,412
	-----
TOTAL CURRENT LIABILITIES .....	1,853,667
LONG-TERM DEFERRED REVENUE .....	375,256
OBLIGATIONS UNDER CAPITAL LEASES, net of current maturities .....	--
RENT ABATEMENT .....	71,250
	-----
TOTAL LIABILITIES .....	2,300,173
COMMITMENTS	
	-----
STOCKHOLDERS' EQUITY	
Common stock, \$0.01 par value per share; 20,000,000 shares authorized; 11,705,100 and 10,551,310 shares issued and outstanding, respectively .....	117,051
Additional paid-in capital .....	8,337,899
Accumulated deficit .....	(6,537,127)
	-----
TOTAL STOCKHOLDERS' EQUITY .....	1,917,823
	-----
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY .....	\$ 4,217,996 =====

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

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	For the Three Months Ended March,	
	2007	2006
	(Unaudited)	
REVENUES		
Product .....	\$ 2,803,128	\$ 2,408
Environmental services .....	90,523	122
TOTAL REVENUES .....	2,893,651	2,531
COSTS AND EXPENSES		
Cost of revenues .....	1,681,437	1,466
Selling, general and administrative .....	952,608	1,024
Special Charge .....	138,000	
Depreciation and amortization .....	52,313	42
TOTAL COSTS AND EXPENSES .....	2,824,358	2,534
OPERATING INCOME (LOSS) .....	69,293	(2)
OTHER INCOME (EXPENSE)		
Interest income .....	16,133	3
Interest expense .....	(322)	(2)
TOTAL OTHER INCOME (EXPENSE) .....	15,811	
INCOME (LOSS) BEFORE INCOME TAXES .....	85,104	(2)
INCOME TAXES .....	(3,134)	
NET INCOME (LOSS) .....	\$ 81,970	\$ (2)
NET INCOME PER COMMON SHARE		
Basic .....	\$ .01	\$
Diluted .....	\$ .01	\$
WEIGHTED AVERAGE SHARES USED IN COMPUTING NET INCOME PER COMMON SHARE:		
Basic .....	11,552,360	10,547
Diluted .....	13,395,644	10,547

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 INCOME

	For the Nine Months Ended March 31,	
	2007	2006
	(Unaudited)	
REVENUES		
Product .....	\$ 8,819,371	\$ 7,588
Environmental services .....	246,941	266
TOTAL REVENUES .....	9,066,312	7,854
COSTS AND EXPENSES		
Cost of revenues .....	5,194,825	4,524
Selling, general and administrative .....	2,831,152	2,879
Special Charge .....	138,000	
Depreciation and amortization .....	142,002	110
TOTAL COSTS AND EXPENSES .....	8,305,979	7,514
OPERATING INCOME .....	760,333	340
OTHER INCOME (EXPENSE)		
Interest income .....	27,601	8
Interest expense .....	(4,500)	(10)
Other Income .....	32,500	
TOTAL OTHER INCOME (EXPENSE) .....	55,601	(2)
INCOME BEFORE INCOME TAXES .....	815,934	337
INCOME TAXES .....	(21,180)	(8)
NET INCOME .....	\$ 794,754	\$ 328
NET INCOME PER COMMON SHARE		
Basic .....	\$ .07	\$
Diluted .....	\$ .07	\$
WEIGHTED AVERAGE SHARES USED IN COMPUTING NET INCOME PER COMMON SHARE:		
Basic .....	10,918,402	10,547

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Diluted ..... 11,971,720 10,814

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

	For the Nine Months Ended March 31,	
	2007	2006
	(Unaudited)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income .....	\$ 794,754	\$ 328,992
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization .....	142,002	110,732
Bad debt expense .....	--	--
Stock based compensation expense .....	1,762	--
Changes in operating assets and liabilities:		
(Increase) decrease in accounts receivable .....	(392,557)	96,264
(Increase) decrease in inventory .....	(144,284)	1,180
Increase in prepaid and other assets .....	(86,595)	(374)
Increase (decrease) in accounts payable and accrued liabilities .....	180,771	(182,583)
Increase (decrease) in deferred revenue .....	218,857	(31,566)
	-----	-----
NET CASH PROVIDED BY OPERATING ACTIVITIES .....	714,710	322,645
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property and equipment .....	(250,098)	(144,621)
Purchase of intangible assets .....	(2,207)	(60,308)
	-----	-----
NET CASH USED IN INVESTING ACTIVITIES .....	(252,305)	(204,929)
CASH FLOWS FROM FINANCING ACTIVITIES		
Payments on capital lease obligations .....	(37,657)	(35,581)
Proceeds from exercise of stock options .....	869,407	1,141
	-----	-----
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES .....	831,750	(34,440)
	-----	-----
NET INCREASE IN CASH AND CASH EQUIVALENTS .....	1,294,155	83,276
CASH AND CASH EQUIVALENTS, beginning of period .....	296,959	258,427
	-----	-----
CASH AND CASH EQUIVALENTS, end of period .....	\$ 1,591,114	\$ 341,703
	=====	=====

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## SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION

Cash paid for interest .....	\$	4,498	\$	10,539
		=====		=====

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

The accompanying unaudited condensed consolidated financial statements include the financial transactions and accounts of Sharps Compliance Corp. and it's 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") for interim financial information and with instructions to Form 10-QSB 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 March 31, 2007 and the results of its operations and cash flows for the three and nine months ended March 31, 2007 and 2006. The results of operations for the three and nine months ended March 31, 2007, are not necessarily indicative of the results to be expected for the entire fiscal year ending June 30, 2007. These unaudited 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, 2006. Certain prior year amounts have been reclassified to conform to current period presentation.

### NOTE 3 - SIGNIFICANT ACCOUNTING POLICIES

#### 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

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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") or United Parcel Service ("UPS"). 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, a portion of the transportation and incineration elements is recognized at the point of sale.

### NOTE 4 - RECENTLY ISSUED ACCOUNTING STANDARDS

In July 2006, the FASB issued FIN No. 48, "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109." This interpretation clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements in accordance with SFAS No. 109, "Accounting for Income Taxes." It prescribes a recognition threshold and measurement attribute for financial statement disclosure of tax positions taken or expected to be taken on a tax return. This interpretation is effective for fiscal years beginning after December 15, 2006. The Company will be required to adopt this interpretation in the first quarter of fiscal year 2008. Management is currently evaluating the requirements of FIN No. 48.

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In September 2006, the SEC released Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements," which provides interpretive guidance on the SEC's views regarding the process of quantifying materiality of financial statement misstatements. SAB 108 is effective for fiscal years ending after November 15, 2006, with early application for the first interim period ending after November 15, 2006. The Company does not expect that the application of SAB 108 will have any material impact on its financial position and results of operations.

In September 2006, the FASB issued Statement No. 157, "Fair Value Measurements." SFAS 157 defines fair value, establishes a framework and gives guidance regarding the methods used for measuring fair value, and expands disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company does not expect the new standard to have a material impact on its financial position and results of operations.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities -- Including an Amendment of FASB Statement No. 115." This statement permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value and establishes presentation and



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disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities. SFAS 159 is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. Early adoption is permitted as of the beginning of a fiscal year that begins on or before November 15, 2007, provided the entity also elects to apply the provisions of SFAS No. 157. The Company expects to adopt SFAS 159 beginning July 1, 2008. The Company is currently evaluating the impact that this pronouncement may have on our consolidated financial statements.

### NOTE 5 - INCOME TAXES

During the three and nine months ended March 31, 2007 the Company recorded a provision of \$3,134 and \$21,180, respectively, for estimated Alternative Minimum Tax ("AMT"). During the three and nine months ended March 31, 2006 the Company recorded a provision of \$0 and \$8,815, respectively, for the AMT. The Company expects to utilize its net operating loss carry forwards to offset any ordinary taxable income for the year ending June 30, 2007.

### NOTE 6 - ACCOUNT RECEIVABLE

During September and October 2003, the Company secured judgments against Ameritech Environmental, Inc. ("Ameritech") totaling \$176,958 related to the non-payment by Ameritech for incineration services provided by the Company in 2002. In November 2003, Ameritech sold its assets representing collateral for the judgments to MedSolutions, Inc. of Dallas, Texas ("MedSolutions"). During 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%, subject to the terms of the agreement by which MedSolutions purchased the Ameritech assets. A balloon payment of \$137,721 due November 7, 2004, under the Garnishment Order, was not made by MedSolutions to the Company. This represented the then outstanding remaining amount due to the Company.

In August 2006, the Company filed an amended suit against Ameritech, its officers and directors (Jasper S. Howard, Alton H. Howard and Jonathon S. Howard) alleging fraudulent conveyance, fraud on creditors, civil conspiracy, breach of court order and conversion. In October 2006, the Company sold certain assets secured by the above noted Garnishment Order for \$50,000 cash, \$17,500 of which was paid to an attorney under a contingency fee arrangement. The net proceeds of \$32,500 were recorded as other income during the quarter ended December 31, 2006. In conjunction with this partial recovery, the Company and MedSolutions entered into a mutual release whereby the Company dismissed MedSolutions from the litigation.

Prior to the year ended June 30, 2003, the Company wrote-off all outstanding amounts due from Ameritech. Any recovery that may be received by the Company will be reduced by collection-related legal fees computed at thirty-five percent of any amounts collected plus expenses. Although the Company will continue to aggressively pursue collection of the remaining outstanding amount of approximately \$90,000 (plus interest and attorney fees), no assurances can be made regarding ultimate collection.

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### NOTE 7 - NOTES PAYABLE AND LONG-TERM DEBT

Effective February 5, 2007, the Company entered into an Amended Credit Agreement with JPMorgan Chase Bank, N.A. ("Credit Agreement") which provides for a \$2.5 million Line of Credit Facility the proceeds of which may be utilized for, (i)

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working capital, (ii) letters of credit (up to \$200,000), (iii) acquisitions (up to \$500,000) and (iv) general corporate purposes. Indebtedness under the Credit Agreement is secured by substantially all of the Company's assets. Borrowings bear interest at a fluctuating rate per annum equal to either, (i) prime rate or (ii) LIBOR plus a margin of 2.75%. Any outstanding revolving loans, and accrued and unpaid interest, will be due and payable on March 27, 2009, the maturity date of the facility. The aggregate principal amount of advances outstanding at any time under the Facility shall not exceed the Borrowing Base which is equal to, (i) 80% of Eligible Accounts Receivable (as defined) plus (ii) 50% of Eligible Inventory (as defined). The Credit Agreement contains affirmative and negative covenants that, among other items, require the Company to maintain a specified tangible net worth and fixed charge coverage ratio. The Credit Agreement also contains customary events of default. Upon the occurrence of an event of default that remains uncured after any applicable cure period, the lenders' commitment to make further loans may terminate and the Borrower may be required to make immediate repayment of all indebtedness to the lenders. The lender would also be entitled to pursue other remedies against the Company and the collateral. As of March 31, 2007, there were no borrowings under this Line of Credit Facility and the Company was in compliance with all loan covenants. Under the Credit Agreement and based upon the Company's March 31, 2007 level of accounts receivable and inventory, the amount available to borrow at quarter end was \$1.3 million.

NOTE 8 - OBLIGATIONS UNDER CAPITAL LEASES

Capital lease obligations consist of the following:

	March 31, 2007	June 30, 2006
	-----	-----
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 .....	\$ --	\$ 30,160
Capital lease for purchase of phone system due in monthly installments of \$455, interest imputed at 12% through August 2007 .....	2,209	5,916
Capital lease for purchase of copier/printer due in monthly installments of \$157, interest imputed at 21% through August 2006 .....	--	155
Capital lease for purchase of phone system upgrades due in monthly installments of \$157, interest imputed at 16% through December 2007 .....	1,342	2,530
Capital lease for purchase of forklift due in monthly installments of \$290, interest imputed at 11% through June 2007 .....	861	3,308
	-----	-----
	4,412	42,069
Less: current portion .....	4,412	40,260
	-----	-----
	\$ --	\$ 1,809
	=====	=====

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### NOTE 9 - STOCK-BASED COMPENSATION

The Company sponsors the 1993 Stock Plan (the "Plan") covering employees, consultants and non-employee directors. The Plan is more fully described in Note 9 in the Company's 2006 Annual Report on Form 10-KSB. Prior to July 1, 2006, awards granted under the Plan were accounted for under the recognition and measurement principles of Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees," ("APB 25") and related interpretations. Under APB 25, no compensation expense was reflected in the Consolidated Statement of Operations for the Company's stock options, as all options granted under the plan had an exercise price equal to the market value of the underlying common shares on the date of grant. The pro forma effects on income for stock options were instead disclosed in a footnote to the unaudited consolidated financial statements.

Effective July 1, 2006, the Company adopted the fair value recognition provisions for FASB Statement of Financial Accounting Standard No. 123(R), "Share-Based Payment," ("SFAS 123(R)"), using the modified prospective transition method. Under this transition method, the Company is required to record compensation expense for all stock option awards granted after the date of adoption as well as any unvested portion of previously granted options. There is no compensation expense related to the unvested portion of previously granted stock option awards that remain outstanding at the date of adoption since the Company's Board of Directors approved, in June 2006, the acceleration of all unvested stock options previously awarded. Stock based compensation expense of \$1,762 was recorded in the Company's unaudited condensed consolidated statement of income for the three and nine months ended March 31, 2007.

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The most significant difference between the fair value approaches prescribed by SFAS No. 123 and SFAS No. 123(R) and the intrinsic value method prescribed by APB No. 25 relates to the recognition of compensation expense for stock option awards based on their grant date fair value. Under SFAS No. 123, the Company used the following weighted-average assumptions for the quarter ended March 31, 2006 as follows: risk-free interest rates of 4.7% expected annual dividend yield of 0%; volatility factors of the expected market price of the Company's common stock of approximately 122%; and a weighted-average expected life of the options of 2.0 years. The Company estimates the fair value of stock option grants using the Black-Scholes option-pricing model. The fair value of each option award is estimated on the date of grant using the Black-Scholes option-pricing model that uses the assumptions for the risk-free interest rate, volatility, dividend yield and the expected term of the options. The risk-free interest rate is based on the U.S. Treasury interest rates in effect at the time of grant for a period equal to the expected term of the option. Expected volatilities are based on implied volatilities from historical trades of the Company's common shares and other applicable factors. Historical data is used to estimate the expected term of the options and employee terminations within the option-pricing model; separate groups of employees that have similar historical exercise behavior are considered separately for valuation purposes. The expected term of the options represents the period of time that the options granted are expected to be outstanding.

The following table reflects the pro forma effect on net income (loss) and income (loss) per share for the three and nine months ended March 31, 2006 as if we had applied the fair value recognition provision of SFAS 123(R):

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	Three Months Ended March 31, ----- 2006 ----- (Unaudited)	Nine Months Ended March 31, ----- 2006 ----- (Unaudited)
Net income (loss), as reported .....	\$ (2,513)	\$ 328,992
Less: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects .....	\$ (77,270) -----	\$ (227,380) -----
Net income (loss), pro forma .....	\$ (79,783) =====	\$ 101,612 =====
Basic and diluted net income per share, as reported ....	\$ -- =====	\$ 0.03 =====
Basic and diluted net income (loss) per share, pro forma	\$ (0.01) =====	\$ 0.01 =====

NOTE 10 - EARNINGS PER SHARE

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

	Nine Months Ended March 31, ----- 2007                      2006 ----- (Unaudited)	
Net income, as reported .....	\$ 794,754	\$ 328,992
Weighted average common shares outstanding .....	10,918,402	10,547,481
Effect of Dilutive stock options .....	1,053,318	266,538
Weighted average diluted common shares outstanding	11,971,720	10,814,019
Net income per common share		
Basic .....	\$ 0.07	\$ 0.03
Diluted .....	\$ 0.07	\$ 0.03

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Employee stock options excluded from computation of diluted per share amounts because their effect would be anti-dilutive .....	--	2,478,890
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### NOTE 11 - STOCK TRANSACTIONS

During the quarter ended March 31, 2007, stock options to purchase 992,802 of common shares were exercised. Total proceeds to the Company were \$748,767 (average price of \$0.75 per share).

During the nine months ended March 31, 2007 stock options to purchase 1,153,790 shares of common stock were exercised. Total proceed to the Company were \$869,407 (average price of \$0.75 per share).

### NOTE 12 - SPECIAL CHARGE

During the three months ended March 31, 2007, the Company recorded a special charge of \$138,000, \$0.01 per diluted share, related to the re-alignment of the leadership in the Company's sales and marketing department. The charge includes a severance accrual of \$102,000 and an executive recruiter fee of \$36,000.

### ITEM 2.

#### MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

##### INFORMATION REGARDING FORWARD-LOOKING STATEMENTS

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

Sharps is a leading developer and manufacturer of cost effective solutions for improving safety, efficiency and costs related to the proper disposal of medical waste by industry and consumers. Sharps primary markets include healthcare, retail, agriculture, hospitality, professional, industrial, commercial, governmental and pharmaceutical. The Company's products and services represent solutions for industries and consumers dealing with the complexity of managing regulatory compliance, environmental sensitivity, employee and customer safety, corporate risk and operating costs related to medical waste disposal. Sharps is a leading proponent and participant in the development of public awareness and

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solutions for the safe disposal of needles, syringes and other sharps in the community setting.

The Company's primary products include Sharps Disposal by Mail System(R), Pitch-It(TM) IV Poles, Trip LesSystem(R), Sharps Pump Return Box, Sharps Enteral Pump Return Box, Sharps Secure(R), Sharps SureTemp Tote(R), IsoWash(R) Linen Recovery System, Biohazard Spill Clean-Up Kit and Disposal 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.

### RESULTS OF OPERATIONS

The following analyzes changes in the consolidated operating results and financial condition of the Company during the three and nine months ended March 31, 2007 and 2006.

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

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2007	2006	2007	
Net revenues .....	100%	100%	100%	100%
Costs and expenses:				
Cost of revenues .....	(58%)	(58%)	(57%)	(57%)
Selling, general and administrative	(33%)	(40%)	(31%)	(31%)
Special Charge .....	(5%)	0%	(2%)	(2%)
Depreciation and amortization .....	(2%)	(2%)	(2%)	(2%)
Total operating expenses .....	(98%)	(100%)	(92%)	(92%)
Income from operations .....	2%	0%	8%	8%
Total other income (expense) .....	1%	0%	1%	1%
Net income .....	3%	0%	9%	9%

THREE MONTHS ENDED MARCH 31, 2007 AS COMPARED TO THREE MONTHS ENDED MARCH 31, 2006

Total revenues for the three months ended March 31, 2007 of \$2,893,651 increased by \$362,441, or 14.3%, over the total revenues for the three months ended March 31, 2006 of \$2,531,210. Billings by market are as follows:

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	Three Months Ended March 31,		
	2007	2006	Variance
	(Unaudited)	(Unaudited)	(Unaudited)
Billings by Market:			
Health Care .....	\$ 1,650,912	\$ 1,687,148	\$ (36,236)
Pharmaceutical .....	450,678	--	450,678
Hospitality .....	330,403	127,843	202,560
Professional .....	157,706	110,579	47,127
Commercial/Industrial ...	100,882	65,718	35,164
Agriculture .....	98,073	118,063	(19,990)
Protec .....	93,424	104,575	(11,151)
Retail .....	49,413	64,395	(14,982)
Government .....	43,158	42,417	741
Other .....	23,056	51,525	(28,469)
Subtotal .....	2,997,705	2,372,263	625,442
GAAP Adjustment* .....	(104,054)	158,947	(263,001)
Revenue Reported .	\$ 2,893,651	\$ 2,531,210	\$ 362,441

\*Represents the net impact of the revenue recognition adjustment required to arrive at reported GAAP revenues. Customer billings includes all invoiced amounts associated with products shipped during the period reported. GAAP revenue includes customer billings as well as numerous adjustments necessary to reflect, (i) the deferral of a portion of current period sales and (ii) recognition of certain revenue associated with product returned for treatment and destruction. The difference between customer billings and GAAP revenue is reflected in the Company's balance sheet as deferred revenue. See Note 3 "Revenue Recognition" in Part I; "Notes to Condensed Consolidated Financial Statements".

The increase in revenues is primarily attributable to increased billings in the Pharmaceutical (\$450,678), Hospitality (\$202,560), Professional (\$47,127) and Commercial/Industrial (\$35,164) markets. These increases were partially offset by decreased billings in the Health Care (\$36,236), Agriculture (\$19,990) and Retail (\$14,982) markets. The increase in the billings in the Pharmaceutical market is a result of the initial portion of the Company's first major pharmaceutical order of the Sharps Disposal by Mail System(R). The increase in the Hospitality market is a result of a large order for the Sharps Disposal by Mail System(R) from a national hair care chain that will use the product to dispose of razor blades. The increase in the Professional and Commercial/Industrial markets is being driven by higher demand for the Company's products as industry and consumers become more aware of the proper disposal of medical sharps (syringes, lancets, etc.).

Cost of revenues for the three months ended March 31, 2007 of \$1,681,437 was 58% of revenues, which is consistent with the corresponding period of the prior year.

Selling, general and administrative ("S, G & A") expenses for the three months ended March 31, 2007 of \$952,608, decreased by \$71,897, or 7%, lower than S, G & A expenses for the three months ended March 31, 2006. The decrease in S, G & A expense is primarily due to lower, (i) travel expenses (\$21,124), (ii)

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compensation expense (\$20,242) and (iii) professional fees (\$19,120). The decrease in professional fees is related to the July 2006 settlement of the Attentus Medical litigation. The decrease in travel expense and compensation is due to the decrease in employed sales persons and travel related expenses.

During the three months ended March 31, 2007, the Company recorded a special charge of \$138,000, \$0.01 per diluted share, related to the re-alignment of the leadership in the Company's sales and marketing department. The charge includes a severance accrual of \$102,000 and an executive recruiter fee of \$36,000.

The Company generated operating income of \$69,293 for the three months ended March 31, 2007 versus an operating loss of \$2,830 for the corresponding period of the prior year. The improvement in operating income is due to higher revenue and gross profit, partially offset by the special charge noted above.

The Company generated income before tax of \$85,104 for the three months ended March 31, 2007 versus a pre-tax loss of \$2,513 for the three months ended March 31, 2006. The improvement of the income before tax is a result of the higher operating income (discussed above) coupled with the higher interest income (result of higher cash balances).

The Company reported earnings per share of \$0.01 for the three months ended March 31, 2007 versus earnings per share of \$0.00 for the three months ended March 31, 2006. The improvement of the earnings per share is a result of the higher net income (discussed above).

Excluding the special charge, the Company generated operating income, net income and earnings per diluted share for the quarter ended March 31, 2007 of \$207,293, \$217,210 and \$0.02, respectively.

### NINE MONTHS ENDED MARCH 31, 2007 AS COMPARED TO NINE MONTHS ENDED MARCH 31, 2006

Total revenues for the nine months ended March 31, 2007 of \$9,066,312 increased by \$1,211,613, or 15.4%, over the total revenues for the nine months ended March 31, 2006 of \$7,854,699. Billings by market are as follows:

	Nine Months Ended March 31,		
	2007	2006	Variance
	-----	-----	-----
(Unaudited) (Unaudited) (Unaudited)			
Billings by Market:			
Health Care .....	\$ 5,367,774	\$ 5,309,558	\$ 58,216
Pharmaceutical .....	507,611	95,172	412,439
Hospitality .....	638,320	443,974	194,346
Professional .....	432,758	321,781	110,977
Commercial/Industrial .....	417,736	205,586	212,150
Agriculture .....	439,978	474,783	(34,805)
Protec .....	311,497	310,250	1,247
Retail .....	921,265	513,002	408,263
Government .....	148,324	53,021	95,303
Other .....	103,888	102,939	949
	-----	-----	-----
Subtotal .....	9,289,151	7,830,066	1,459,085
GAAP Adjustment* .....	(222,838)	24,633	(247,471)
	-----	-----	-----
Revenue Reported .....	\$ 9,066,313	\$ 7,854,699	\$ 1,211,614
	=====	=====	=====

\*Represents the net impact of the revenue recognition adjustment required to



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arrive at reported GAAP revenues. Customer billings includes all invoiced amounts associated with products shipped during the period reported. GAAP revenue includes customer billings as well as numerous adjustments necessary to reflect, (i) the deferral of a portion of current period sales and (ii) recognition of certain revenue associated with product returned for treatment and destruction. The difference between customer billings and GAAP revenue is reflected in the Company's balance sheet as deferred revenue. See Note 3 "Revenue Recognition" in Part I; "Notes to Condensed Consolidated Financial Statements".

The increase in revenues is primarily attributable to increased billings in the Pharmaceutical (\$412,439), Retail (\$408,263), Commercial/Industrial (\$212,150), Hospitality (\$194,346), Professional (\$110,977), Government (\$95,303), and Health Care (\$58,216) markets. These increases were partially offset by decreased billings in the Agriculture market of \$34,805. The increase in the billings in the Pharmaceutical market is a result of the initial portion of the Company's first major pharmaceutical manufacturing order of the Sharps Disposal by Mail System(R). The increase in the Hospitality market billings is a result of a large order for the Sharps Disposal by Mail System(R) from a national hair care chain that will use the product to dispose of razor blades. The increase in the Retail market billings is a result of the increased use of the Company's Sharps Disposal By Mail System (R) products in grocery stores and retail pharmacies to properly dispose of syringes utilized to administer flu and other inoculations. The increase in the Commercial/Industrial and Professional markets is being driven by higher demand for the Company's products as industry and consumers become more aware of the proper disposal of medical sharps (syringes, lancets, etc.). The increase in the Government market is attributable to the billings associated with a three year award received by the Company during mid - March in the third quarter of FY 2006 by an agency of the United States Government.

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Cost of revenues for the nine months ended March 31, 2006 of \$5,194,825 was 57% of revenues, which is consistent with the corresponding period of the prior year.

Selling, general and administrative ("S, G & A") expenses for the nine months ended March 31, 2007 of \$2,831,152 decreased by \$48,203, or 1.7%, lower than the S, G & A expenses for the nine months ended March 31, 2006. The decrease in S, G & A expenses is primarily a result of a decrease in professional fees of \$55,918. The decrease in professional fees is related to the July 2006 settlement of the Attentus Medical litigation.

During the nine months ended March 31, 2007, the Company recorded a special charge of \$138,000, \$0.01 per diluted share, related to the re-alignment of the leadership in the Company's sales and marketing department. The charge includes a severance accrual of \$102,000 and an executive recruiter fee of \$36,000.

The Company generated operating income of \$760,333 for the nine months ended March 31, 2007 versus \$340,095 for the corresponding period of the prior year. The improvement in operating income is due to higher revenue and gross profit, partially offset by the special charge noted above.

The Company generated income before tax of \$815,934 for the nine months ended March 31, 2007 versus a pre-tax income of \$337,807 for the nine months ended March 31, 2006. The improvement of the income before tax is a result of the higher operating income (discussed above) coupled with the higher interest income (result of higher cash balances).

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The Company reported earnings per share of \$0.07 for the nine months ended March 31, 2007 versus earnings per share of \$0.03 for the nine months ended March 31, 2006. The improvement of the earnings per share is a result of the higher net income (discussed above).

Excluding the special charge, the Company generated operating income, net income and earnings per diluted share for the nine months ended March 31, 2007 of \$898,333, \$929,994 and \$0.08, respectively.

### PROSPECTS FOR THE FUTURE

The Company continues to take advantage of the many opportunities in the markets served as communities, consumers and industries become more aware of the proper disposal of medical sharps (syringes, lancets, etc.). This education process was enhanced in March 2004 when the U. S. Environmental Protection Agency ("EPA") issued its new guidelines for the proper disposal of medical sharps (see [www.epa.gov/epaoswer/other/medical/sharps.htm](http://www.epa.gov/epaoswer/other/medical/sharps.htm)). Additionally, in July 2006 both the states of California and Massachusetts passed legislation designed to mandate appropriate disposal of sharps waste necessary to protect the general public and workers from potential exposure to contagious diseases and health and safety risks. Among the methods of disposal recommended as part of the above noted regulatory actions are mail-back programs such as those marketed by the Company. The Company estimates that there are an estimated 2 billion used syringes disposed of in the United States outside of the hospital setting. Additionally, the Company estimates that it would require 30 - 40 million Sharps Disposal by Mail System(R) products to properly disposal of all such disposed syringes, which would equate to a \$1 billion small quantity generator market opportunity. Based upon the current level of sales, the Company estimates that this \$1 billion market has only been penetrated by approximately 1% or less.

The Company continues to develop new products for its Sharps Disposal by Mail System(R), and Sharps SureTemp Tote(R) product lines. The Company believes its future growth will be driven by, among other items, (i) the positive impact and awareness created by the above noted regulatory actions as well as additional potential future legislation and (ii) the effects of the Company's extensive direct marketing efforts. The result of these direct marketing efforts was recognized with the receipt of the first major pharmaceutical manufacturer order, valued at \$1.4 million, from a recognized and leading pharmaceutical manufacturer. The initial \$0.45 million order was billed during March 2007 with fulfillment services to patients expected to begin in May 2007. The remaining portion of the order is expected to be completed in calendar year 2007.

### LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents increased by \$1,294,155 to \$1,591,114 at March 31, 2007 from \$296,959 at June 30, 2006. The increase in cash and cash equivalents is primarily a result of cash generated from operations of \$714,710 plus proceeds from the exercise of stock options of \$869,407, partially offset by additions to property and equipment of \$250,098 and payments on capital lease obligations of \$37,657.

Accounts receivable increased by \$392,557 to \$1,327,840 at March 31, 2007 from \$935,283 at June 30, 2006. The increase is a direct result of the increase in billings generated by the Company for the quarter ended March 31, 2007 versus the quarter ended June 30, 2006. Additionally, the increase in accounts receivable was attributable to the above noted pharmaceutical manufacturing

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billing in mid-March of \$450,000 (less a prepayment previously received of \$225,000).

Property and equipment increased by \$108,656 to \$582,043 at March 31, 2007 from \$473,387 at June 30, 2006 due to capital expenditures of \$250,098 partially offset by depreciation expense of \$141,443. The capital expenditures consisted of, (i) custom software programming of \$36,952, (ii) computer equipment of \$30,442, (iii) incinerator facility improvements of \$26,715 and (iv) office equipment of \$59,818 and assembly / warehouse-related equipment of \$24,982. The custom software program was incurred to accommodate the change from FedEx to UPS and an upgrade to the Company's financial and operations system including the Sharps Tracer (TM) system. The computer equipment was purchased to facilitate the upgrade of outdated equipment. Office and other equipment purchased were related to equipment necessary to accommodate the in-house assembly of the Company's products and the move to the new facility including office furniture and equipment (\$31,471), a new phone system (\$28,347) and warehouse equipment and racks (\$24,982).

Stockholder's equity increased by \$1,665,923 from \$251,900 to \$1,917,823. This increase is attributable to net income for the nine months ended March 31, 2007 of \$794,754 and the effect of stock options to purchase 1,153,790 common stock exercised with proceeds of \$869,407 (average exercise price of \$0.75 per share).

Management believes that the Company's current cash resources (cash on hand and cash generated from operations) along with its \$2.5 million line of credit will be sufficient to fund operations for the twelve months ending March 31, 2008.

### OFFICE LEASE

On July 13, 2006 Sharps executed a new lease agreement for 18,231 square feet of rentable (office and warehouse) space ("New Lease") located near the previous leased facility in Houston, Texas ("New Premises"). The New Lease commenced and the prior lease was terminated on March 1, 2007. The New Lease will expire on February 28, 2012. The move to a larger facility enables the Company to, (i) facilitate the transition of its product assembly operations from an outsourced vendor to an in-house function (estimated to be completed by May 31, 2007) and (ii) accommodate its recent and planned future growth.

### TRENDS

Consistent with the recent growth in billings and revenue (26% and 14% for the three months ended March 31, 2007, respectively) and increased operating margins and net income, the trend of earnings and cash from operations continue to be positive. The Company's internal plans contemplate additional growth in all of its markets served led by growth in the Pharmaceutical Manufacturer and Retail (flu shot and non-emergency clinics in the retail setting).

In May 2007, the USPS will implement an increase in postage. The Company utilized the USPS to facilitate the transportation of the Sharps Disposal by Mail System(R) products from the end user to the Company's incineration facility in Carthage, Texas. In preparation for this increase in postage the Company has announced to its customers a price increase for the Sharps Disposal by Mail System(R) products designed to increase revenue necessary to compensate for the increased transportation costs.

While the Company has no material expected change in the level of capital expenditures in the near-term, it may incur significant capital costs should it decide to upgrade its current incineration facility in Carthage, Texas consistent with the November 2005 amended EPA Clean Air Act (see Government Regulation - Operations and Incinerator below). The Company could avoid such upgrade and the associated capital costs should it decide to install alternative technology (at a much lower cost) or outsource its incineration needs (no

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additional capital costs). The Company has studied the amended EPA Clean Air Act and its options, but has not yet made a decision. It is important to note that should the Company decide to upgrade its incineration facility to comply with the new regulations or install alternative technology, it would open up the opportunity for additional revenue sources including medical waste disposal. As noted below, the new regulation allows a minimum period of three years and a maximum of five years to comply.

### 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.

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### Governmental Regulation

#### Operations and Incinerator

Sharps is required to operate within guidelines established by federal, state, and/or local regulatory agencies. Such guidelines have been established to promote occupational safety and health standards and certain standards have been established in connection with the handling, transportation and disposal of certain types of medical and solid wastes, including mailed sharps. Sharps believes that it is currently in compliance in all material respects with all applicable laws and regulations governing its business. However, in the event additional guidelines are established to more specifically control the business of Sharps, including the environmental services subsidiary, additional expenditures may be required in order for Sharps to be in compliance with such changing regulations. Furthermore, any material relaxation of any existing regulatory requirements governing the transportation and disposal of medical sharps products could result in a reduced demand for Sharps' products and services and could have a material adverse effect on Sharps' revenues and financial condition. The scope and duration of existing and future regulations affecting the medical and solid waste disposal industry cannot be anticipated and are subject to change due to political and economic pressures.

In November 2005, the EPA amended the Clean Air Act which will affect the operations of the leased incineration facility located in Carthage, Texas. The regulation modifies the emission limits and monitoring procedures required to operate an incineration facility. The new rules will necessitate changes to the Company's leased incinerator and pollution control equipment at the facility or require installation of an alternative treatment method to ensure compliance. Such change would require the Company to incur significant capital expenditures in order to meet the requirements of the regulations. The regulation allows a minimum period of three years and a maximum of five years to comply after the date the final rule was published. The Company has studied the amended EPA Clean Air Act and its options, but has not yet made a decision regarding how it will

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comply with the new rules. Should the Company decide to upgrade its incineration facility to comply with the new regulations or install alternative technology, it would do so not only to comply with the new regulations but also to potentially generate additional revenue sources including medical waste disposal (in addition to the incineration of sharps, syringes, lancets, etc.).

### Proper Disposal of Medical Sharps

The first significant regulatory development occurred in December 2004 with the improved guidance issued by the Environmental Protection Agency ("EPA") regarding the safe disposal of medical sharps (needles, syringes and lancets). This new guidance is a result of disposal problems created by 3 billion syringes discarded annually by self-injectors of medicines in homes and non-healthcare commercial facilities. Until December 2004, the EPA guidance has instructed consumers to place used sharps in a household container and to place the container in the household garbage. New guidance posted on the EPA website reflects information about alternative disposal methods including mail-back programs. The improved guidance issued by the EPA is a significant step toward the removal of needles, syringes and other sharps from the solid waste stream, consistent with the current practice in healthcare facilities. The Company's products and services, which are included in the EPA list of recommended solutions, are designed to improve safety, efficiency and patient concerns related to the proper disposal of medical sharps.

The next regulatory development was the enactment of California Senate Bill 1362, "The Safe Needle Disposal Act of 2004." This legislation authorizes California agencies to expand the scope of their existing household hazardous waste plans to provide for the safe disposal of medical sharps including hypodermic needles and syringes. Authorized disposal programs include the mail-back programs currently marketed by the Company.

In July 2006, the State of California passed Senate Bill 1305 ("SB 1305"), an amendment to The Medical Waste Management Act. The new law requires the proper disposal of home-generated sharps waste (syringes, needles, lancets, etc.) and acknowledges mail-back programs as one of the most convenient alternatives for the collection and destruction of home-generated sharps. Effective January 1, 2007 (with enforcement beginning September 1, 2008), SB 1305 addresses the need to meet the changing demands of healthcare provided in alternate sights that currently allows hundreds of millions of home-generated sharps waste to be disposed in solid waste and recycling containers. The new law is designed to ensure appropriate disposal of sharps waste necessary to protect the general public and workers from potential exposure to contagious diseases and health and safety risks.

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Also in July 2006, The Massachusetts Legislature enacted Senate Bill 2569 which requires the Massachusetts department of public health, in conjunction with other relevant state and local agencies and government departments, to design, establish and implement a program for the collection and disposal of non-commercially generated, spent hypodermic needles and lancets. Recommended disposal methods include mail-back products approved by the U.S. Postal Service such as the Sharps Disposal By Mail Systems(R). The Massachusetts legislation addresses the need for proper disposal of used syringes, needles and lancets outside of the traditional healthcare setting.

Several other states are considering legislation similar to California and Massachusetts.

RECENTLY ISSUED ACCOUNTING STANDARDS

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In July 2006, the FASB issued FIN No. 48, "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109." This interpretation clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements in accordance with SFAS No. 109, "Accounting for Income Taxes." It prescribes a recognition threshold and measurement attribute for financial statement disclosure of tax positions taken or expected to be taken on a tax return. This interpretation is effective for fiscal years beginning after December 15, 2006. The Company will be required to adopt this interpretation in the first quarter of fiscal year 2008. Management is currently evaluating the requirements of FIN No. 48.

In September 2006, the SEC released Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements," which provides interpretive guidance on the SEC's views regarding the process of quantifying materiality of financial statement misstatements. SAB 108 is effective for fiscal years ending after November 15, 2006, with early application for the first interim period ending after November 15, 2006. The Company does not expect that the application of SAB 108 will have any material impact on its financial position and results of operations.

In September 2006, the FASB issued Statement No. 157, "Fair Value Measurements." SFAS 157 defines fair value, establishes a framework and gives guidance regarding the methods used for measuring fair value, and expands disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company does not expect the new standard to have a material impact on its financial position and results of operations.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities -- Including an Amendment of FASB Statement No. 115." This statement permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value and establishes presentation and disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities. SFAS 159 is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. Early adoption is permitted as of the beginning of a fiscal year that begins on or before November 15, 2007, provided the entity also elects to apply the provisions of SFAS No. 157. The Company expects to adopt SFAS 159 beginning July 1, 2008. The Company is currently evaluating the impact that this pronouncement may have on our consolidated financial statements.

### ITEM 3. CONTROLS AND PROCEDURES

As of 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 13(a)-15(e) and 15(d) - 15(e). 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.

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### PART II - OTHER INFORMATION

#### ITEM 1. LEGAL PROCEEDINGS

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Ameritech Environmental, Inc.

During September and October 2003, the Company secured judgments against Ameritech Environmental, Inc. ("Ameritech") totaling \$176,958 related to the non-payment by Ameritech for incineration services provided by the Company in 2002. In November 2003, Ameritech sold its assets representing collateral for the judgments to MedSolutions, Inc. of Dallas, Texas ("MedSolutions"). During 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%, subject to the terms of the agreement by which MedSolutions purchased the Ameritech assets. A balloon payment of \$137,721 due November 7, 2004, under the Garnishment Order, was not made by MedSolutions to the Company. This represented the then outstanding remaining amount due to the Company.

In August 2006, the Company filed an amended suit against Ameritech, its officers and directors (Jasper S. Howard, Alton H. Howard and Jonathon S. Howard) alleging fraudulent conveyance, fraud on creditors, civil conspiracy, breach of court order and conversion. In October 2006, the Company sold certain assets secured by the above noted Garnishment Order for \$50,000 cash, \$17,500 of which was paid to an attorney under a contingency fee arrangement. The net proceeds of \$32,500 were recorded as other income during the quarter ended December 31, 2006. In conjunction with this partial recovery, the Company and MedSolutions entered into a mutual release whereby the Company dismissed MedSolutions from the litigation.

Prior to the year ended June 30, 2003, the Company wrote-off all outstanding amounts due from Ameritech. Any recovery that may be received by the Company will be reduced by collection-related legal fees computed at thirty-five percent of any amounts collected plus expenses. Although the Company will continue to aggressively pursue collection of the remaining outstanding amount of approximately \$90,000 (plus interest and attorney fees), no assurances can be made regarding ultimate collection.

Ronald E. Pierce Matter

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 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

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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.

Attentus Medical Sales, Inc.

In March 2005, the Company's wholly-own subsidiary Sharps Compliance, Inc., filed a lawsuit in Harris County District Court, Texas against Mr. Jodway (a former employee) and Attentus Medical Sales, Inc. ("Attentus"). The lawsuit claimed, (i) breach of a confidentiality agreement, (ii) misappropriation of trade secrets and (iii) tortuous interference with the Company's existing and prospective contracts and business relationships. On April 7, 2005, the defendant filed its answer and counter claims against Sharps Compliance, Inc. asserting breach of contract, quantum meruit and violation of the Texas Payday Act. On September 19, 2005, the Company amended its pleadings and added claims asserting conversion, unjust enrichment, unfair competition and trademark infringement in violation of the Lanham Act, false advertising in violation of the Lanham Act, trademark dilution under the Texas Business and Commerce Code, and tortuous interference with existing and/or prospective customers. On July 6, 2006, the Company, Attentus and Mr. Jodway reached settlement on all matters related to this litigation and dismissed all claims against each other. In conjunction with the resolution of the matter, the Company entered into a business relationship whereby Attentus now markets and sells the Company's Sharps Disposal By Mail Systems(R) to its current and future customers.

Sylvia Haist Matter

In July 2006, the Company received a Notice of Charge of Discrimination from the U.S. Equal Employment Opportunity Commission ("EEOC") filed by a former employee, Sylvia Haist. The charge alleged sex discrimination and retaliation. Sylvia Haist was an employee of the Company from July 1998 until her termination in January 2006. The Company believes the charges to be totally without merit and frivolous.

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On March 1, 2007, the Company received notice from the EEOC dismissing all charges against the Company. Ms. Haist has ninety (90) days to file a lawsuit against the Company should she so choose. The Company will vigorously defend itself against the erroneous allegations should Ms. Haist file suit.

Patent Infringement Litigation

In May 2007, the Company filed patent infringement lawsuits in the United States District Court for the Southern District of Texas in Houston against MediSupply, Inc. (a/k/a or f/k/a Medi-Supply Alliance, LLC and Medi-Supply, Inc. "MediSupply") and Drive Medical Design & Manufacturing ("Drive Medical") for infringement of three U.S. patents. The complaints allege that MediSupply and Drive Medical infringe the patents by making, selling, and offering for sale disposable IV poles which are identical to the Company's Pitch-It (TM) IV Pole. In its cases against MediSupply and Drive Medical, the Company is seeking injunctions and damages or other monetary relief, including pre-judgment interest and awarding of attorney fees.

### ITEM 6. EXHIBITS

(a) Exhibits:



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- 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 2, 3, 4 AND 5 ARE NOT APPLICABLE AND HAVE BEEN OMITTED.

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SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

REGISTRANT:

SHARPS COMPLIANCE CORP.

Dated: May 9, 2007

By: /s/ Dr. Burton J. Kunik

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Chairman of the Board of Directors,  
Chief Executive Officer and President

Dated: May 9, 2007

By: /s/ David P. Tusa

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Executive Vice President,  
Chief Financial Officer,  
Business Development and  
Corporate Secretary

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