INDUSTRIAL SERVICES OF AMERICA INC
Form 10-Q
November 10, 2016

FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE

SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2016

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE

SECURITIES EXCHANGE ACT OF 1934

For the Transition Period From _________ to ________

Commission File Number 0-20979

INDUSTRIAL SERVICES OF AMERICA, INC.

(Exact Name of Registrant as specified in its Charter)

Florida	59-0712746
(State or other jurisdiction of Incorporation or Organization)	(IRS Employer Identification No.)

7100 Grade Lane

Louisville, Kentucky 40213

(Address of principal executive offices)

(502) 368-1661

(Registrant's Telephone Number, Including Area Code)

Check whether the registrant (1) has filed all Reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

(Check one):	Large accelerated filer	Accelerated filer
	Non-accelerated filer	Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of November 9, 2016: 8,067,289.

INDUSTRIAL SERVICES OF AMERICA, INC. AND SUBSIDIARIES

PART I – FINANCIAL INFORMATION

ITEM 1: CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

INDUSTRIAL SERVICES OF AMERICA, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

ASSETS

	September 30, 2016	December 31, 2015
	(Unaudited)	
	(in thousands)	
Current assets		
Cash and cash equivalents	$ 492	$ 642
Income tax receivable	7	14
Accounts receivable – trade (after allowance for doubtful accounts of $35.0 thousand and $35.0 thousand in 2016 and 2015, respectively)	3,151	1,669
Receivables from related parties	57	208
Inventories	2,900	2,410
Prepaid expenses and other current assets	69	160
Total current assets	6,676	5,103
Net property and equipment	13,650	14,152
Other assets		
Deferred income taxes	27	97
Other non-current assets	226	82
Total other assets	253	179
Total assets	$ 20,579	$ 19,434

See accompanying notes to condensed consolidated financial statements.

INDUSTRIAL SERVICES OF AMERICA, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

CONTINUED

LIABILITIES AND SHAREHOLDERS' EQUITY

	September 30, 2016 (Unaudited)	December 31, 2015
	(in thousands, except par value and share information)	
Current liabilities		
Current maturities of long-term debt	$ —	$ 20
Current maturities of capital lease obligations	144	—
Bank overdrafts	41	—
Accounts payable	1,677	2,152
Payables and accrued expenses to related parties	670	1,922
Other current liabilities	615	194
Total current liabilities	3,147	4,288
Long-term liabilities		
Long-term debt, net of current maturities	2,321	—
Long-term debt, net of current maturities, related parties	1,504	—
Capital lease obligations, net of current maturities	1,118	—
Total long-term liabilities	4,943	—
Shareholders' equity		
Common stock, $0.0033 par value: 20.0 million shares authorized in 2016 and 2015; 8,097,979 and 8,049,622 shares issued in 2016 and 2015, respectively; 8,067,289 and 8,018,932 shares outstanding in 2016 and 2015, respectively	27	27
Additional paid-in capital	23,888	23,555
Stock warrants outstanding	1,025	1,025
Retained losses	(12,407)	(9,417)
Treasury stock at cost, 30,690 shares in 2016 and 2015	(44)	(44)
Total shareholders' equity	12,489	15,146
Total liabilities and shareholders' equity	$ 20,579	$ 19,434

See accompanying notes to condensed consolidated financial statements.

INDUSTRIAL SERVICES OF AMERICA, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015

(IN THOUSANDS, EXCEPT PER SHARE DATA)

(UNAUDITED)

	For the three months ended		For the nine months ended	
	September 30, 2016	September 30, 2015	September 30, 2016	September 30, 2015
Revenue from product sales	$ 9,896	$ 9,591	$ 26,015	$ 39,629
Cost of sales for product sales	9,810	9,887	25,391	41,459
Inventory adjustment for lower of cost or market	—	319	—	1,110
Impairment loss, property and equipment	—	—	—	637
Total cost of sales	9,810	10,206	25,391	43,206
Selling, general and administrative expenses	1,095	862	3,485	2,877
Loss before other income (expense)	(1,009)	(1,477)	(2,861)	(6,454)
Other income (expense)				
Interest expense, including loan fee amortization	(129)	(105)	(302)	(414)
Gain (loss) on sale of assets	—	—	—	322
Other income (expense), net	237	(7)	250	21
Total other income (expense)	108	(112)	(52)	(71)
Loss before income taxes	(901)	(1,589)	(2,913)	(6,525)
Income tax provision	37	7	77	15
Net loss from continuing operations	$ (938)	$ (1,596)	$ (2,990)	$ (6,540)
Income from discontinued operations, net of tax	—	409	—	1,052
Net loss	$ (938)	$ (1,187)	$ (2,990)	$ (5,488)
Net income (loss) per share of common stock:				
Basic:				
Continuing operations	$ (0.12)	$ (0.20)	$ (0.37)	$ (0.82)
Discontinued operations	—	0.05	—	0.13
Diluted:				
Continuing operations	$ (0.12)	$ (0.20)	$ (0.37)	$ (0.82)
Discontinued operations	—	0.05	—	0.13
Weighted average shares outstanding:				
Basic	8,067	8,000	8,042	7,979
Diluted	8,067	8,000	8,042	7,979

See accompanying notes to condensed consolidated financial statements.

INDUSTRIAL SERVICES OF AMERICA, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015

(UNAUDITED)

	For the three months ended		For the nine months ended	
	September 30, 2016	September 30, 2015	September 30, 2016	September 30, 2015
	(in thousands)		(in thousands)	
Net loss	$ (938)	$ (1,187)	$ (2,990)	$ (5,488)
Other comprehensive loss:				
Unrealized loss on derivative instruments	—	(3)	—	(9)
Comprehensive loss	$ (938)	$ (1,190)	$ (2,990)	$ (5,497)

See accompanying notes to condensed consolidated financial statements.

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INDUSTRIAL SERVICES OF AMERICA, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY

NINE MONTHS ENDED SEPTEMBER 30, 2016

(UNAUDITED)

	Common Stock		**Additional Paid-in Capital**	Stock Warrants	Retained Losses	Treasury Stock		**Total Shareholders' Equity**
	Shares	Amount				Shares	Cost	
	(in thousands, except share information)							
Balance as of December 31, 2015	8,049,622	$ 27	$ 23,555	$ 1,025	$ (9,417)	(30,690)	$ (44)	$ 15,146
Common stock	48,357	—	—	—	—	—	—	—
Share-based compensation	—	—	333	—	—	—	—	333
Net loss	—	—	—	—	(2,990)	—	—	(2,990)
Balance as of September 30, 2016	8,097,979	$ 27	$ 23,888	$ 1,025	$ (12,407)	(30,690)	$ (44)	$ 12,489

See accompanying notes to condensed consolidated financial statements.

INDUSTRIAL SERVICES OF AMERICA, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

NINE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015

(UNAUDITED)

	2016	2015
	(in thousands)	
Cash flows from operating activities		
Net loss from continuing operations	$ (2,990)	$ (6,540)
Adjustments to reconcile net loss to net cash from (used in) operating activities:		
Depreciation and amortization	1,715	1,755
Inventory write-down	—	1,110
Impairment loss, property and equipment	80	637
Share-based compensation expense	333	257
Gain on sale of property and equipment	—	(322)
Amortization of loan fees included in interest expense	100	46
Change in assets and liabilities		
Receivables	(1,482)	5,731
Receivables from related parties	151	174
Inventories	(490)	1,270
Income tax receivable/payable	7	(42)
Other assets	88	34
Deferred income taxes	70	—
Accounts payable	(475)	(112)
Payables to related parties	252	166
Other current liabilities	421	365
Net cash (used in) from operating activities	(2,220)	4,529
Cash flows from investing activities		
Proceeds from sale of property and equipment	—	2,223
Purchases of property and equipment	(8)	(21)
Net cash (used in) from investing activities	(8)	2,202
Cash flows from financing activities		
Loan fees capitalized	(241)	—
Change in bank overdrafts	41	(79)
Payments on long-term debt	(20)	(8,538)
Proceeds from long-term debt	—	291
Payments on capital lease obligations	(23)	—
Proceeds from revolving line of credit, net	2,321	—
Net cash from (used in) financing activities	2,078	(8,326)
Cash flows from discontinued operations		
Net cash provided by operating activities	—	1,399
Net cash used in investing activities	—	(313)
Net cash from discontinued operations	—	1,086

Net change in cash and cash equivalents	(150)	(509)
Cash and cash equivalents at beginning of period	642	1,059
Cash and cash equivalents at end of period	$ 492	$ 550

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INDUSTRIAL SERVICES OF AMERICA, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

CONTINUED

NINE MONTHS ENDED SEPTEMBER 30, 2016 AND 2015

(UNAUDITED)

	2016	2015
	(in thousands)	
Supplemental disclosure of cash flow information:		
Cash paid for interest	$ 186	$ 368
Tax refunds received	5	1
Cash paid for taxes	2	49
Supplemental disclosure of noncash investing and financing activities:		
Increase (decrease) in equipment purchases accrual	$ —	$ (30)
Equipment additions financed by capital lease obligations	1,285	—
Common stock issued for consideration of a reduction of accrued but unpaid bonus compensation	—	189

See accompanying notes to condensed consolidated financial statements.

INDUSTRIAL SERVICES OF AMERICA, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND GENERAL

During 2015, the Company's average selling price per unit of quantity decreased by 49.4% and 24.9% for ferrous and nonferrous material, respectively, compared to 2014. Due to these deteriorating metals commodity market conditions, ISA took significant steps to improve liquidity and pay down debt during 2015 and early 2016. Despite improvements in metal commodity markets during 2016, low prices combined with low volumes present a difficult ongoing metals recycling market.

In connection with the previously disclosed ongoing evaluation of strategic alternatives, on September 30, 2016, the Company and Algar, Inc. ("Algar") mutually agreed to terminate the Management Services Agreement between them dated as of December 1, 2013 (the "Management Agreement"), pursuant to the Agreement to Terminate Management Services among the Company, Algar, and Sean Garber dated as of September 30, 2016 (the "Termination Agreement"). See Note 6 - Related Party Transactions for further details.

Effective September 30, 2016, Mr. Garber resigned from all positions with the Company, including as President, and the Board appointed Todd Phillips as President. Mr. Phillips has been the Company's CFO since December 31, 2014 and will continue to serve in that role.

The Company's Response to 2015 Commodity Markets and Liquidity Conditions:

The Company took the below steps to address the challenging metal commodity market.

On February 27, 2015, the Company closed on the sale of its Seymour, Indiana property. Also, in conjunction with this decision, the Company signed a lease, effective December 1, 2014, to lease a facility in the Seymour area. See Note 4 - Lease Commitments for further lease information and Note 6 - Related Party Transactions for further related party details. Proceeds were used to reduce debt and improve liquidity.

On April 30, 2015, LK Property Investments, LLC ("LK Property"), an entity principally owned by Daniel M. Rifkin, CEO of MetalX LLC ("MetalX"), (a related party) a scrap metal recycling company headquartered in Waterloo, Indiana, and the principal owner of Recycling Capital Partners, LLC ("RCP") (a related party) purchased a 4.4 acre parcel of real estate located at 6709 Grade Lane, Louisville, KY from ISA Real Estate, LLC, a wholly-owned subsidiary of the Company, for a purchase price of $1.0 million. The Company realized a loss of $102.0 thousand from this sale. Also on April 30, 2015, the Company entered into a lease agreement with LK Property for a portion of the 4.4 acre parcel. See Note 4 - Lease Commitments for further lease details and Note 6 - Related Party Transactions. Proceeds were used to reduce debt and improve liquidity.

On May 13, 2015, the Company announced the warm idle of the Company’s auto shredder. This action was in response to market conditions, primarily related to ferrous price volatility and lower ferrous volumes. Management will continue to monitor and analyze market conditions and to review the Company’s long-term options for its shredder and related downstream processing operation. The costs of idling were recognized in the second quarter of 2015 financial statements. As a result of the continued operating losses from the shredder operations, management reviewed the carrying cost of the shredder, including the downstream processing system. The Company recognized an asset impairment charge during the first quarter of 2015 of approximately $636.6 thousand related to the shredder’s downstream processing system. This charge was recorded as an impairment charge on property and equipment within the cost of goods section in the September 30, 2015 condensed consolidated statement of operations. As of the date of this report, the shredder remains idled. The Company continues to depreciate the assets associated with the shredder. Working capital, which would otherwise have been utilized in operating the shredder, was used to reduce debt and improve liquidity.

In May 2015, ISA Real Estate, LLC sold to SG&D Ventures, LLC ("SG&D"), an entity owned by shareholders of Algar, Inc. ("Algar"), including Sean Garber, at that time the Company’s Vice Chairman of the Board and President, and the President of Algar, an approximately 1-acre parcel of non-essential real estate, located at 7017 Grade Lane, Louisville, KY, for an aggregate purchase price equal to independent third-party appraisal amount of $350.0 thousand. The purchase consideration consisted of $300.0 thousand in cash from the purchaser and a credit of $50.0 thousand against bonus compensation previously accrued but not paid to Algar as described in Note 6 - Related Party Transactions. The gain on sale of this asset was $1.1 thousand and was recognized during the second quarter of 2015. Proceeds were used to reduce debt and improve liquidity.

On November 6, 2015, the Company entered into a Forbearance Agreement and Third Amendment to Credit Agreement (the “Forbearance Agreement”) by and among the Company, certain of the Company’s subsidiaries, and Wells Fargo Bank, National Association ("Wells Fargo"). The Forbearance Agreement amended the Credit Agreement to reduce the Maximum Revolver Amount from $15.0 million to $5.0 million. The Forbearance Agreement also amended the Credit Agreement Maturity Date to March 15, 2016 from June 13, 2019. The Forbearance Agreement increased the interest rate on the outstanding indebtedness by approximately 100 basis points.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND GENERAL, Continued

Pursuant to the terms of the Forbearance Agreement, Wells Fargo agreed that it would forbear, until the Forbearance Termination Date (as defined below), from exercising certain rights and remedies with respect to or arising out of the existence and continuation of certain stipulated events of default under the Credit Agreement between the loan parties and Wells Fargo (as amended by the First Amendment to Credit Agreement dated January 15, 2015, the Second Amendment to Credit Agreement dated January 22, 2015, and the Forbearance Agreement, the “Credit Agreement”).

Under the Forbearance Agreement, the Forbearance Termination Date was the earlier to occur of (i) Wells Fargo’s election following the failure of the Loan Parties to satisfy any of the Forbearance Conditions, and (ii) March 15, 2016. See Note 3 - Long Term Debt and Notes Payable to Bank for further details.

On December 4, 2015, the Company and WESSCO, LLC, a wholly owned subsidiary of ISA ("WESSCO"), entered into an Asset Purchase Agreement (the "Asset Purchase Agreement") with Compactor Rentals of America, LLC ("Compactor Rentals") pursuant to which the Company sold its “Waste Services Segment,” consisting of substantially all of the assets used in (i) the Company’s commercial, retail and industrial waste and recycling management services business which the Company operated under the name “Computerized Waste Systems” or “CWS,” and (ii) the Company’s equipment sales, rental and maintenance business for the commercial and industrial waste and recycling industry which the Company operated under the name “Waste Equipment Sales and Service Company".

The Company received cash consideration at closing of $7.5 million, less $150.0 thousand retained by Compactor Rentals (the "Holdback"). Compactor Rentals assumed certain liabilities relating to the Waste Services Segment, including but not limited to, current liabilities, warranty liabilities, and post-closing liabilities incurred in connection with transferred contracts.

The sale included substantially all of the assets of the Waste Services Segment including, but not limited to, current assets, accounts receivable, tangible personal property, certain leases, inventory, intellectual property, rights under transferred contracts, rights of action and all associated goodwill and other intangible assets associated with the transferred assets.

The Asset Purchase Agreement contains a restrictive covenant under which the Company is prohibited from competing with the Waste Services Segment for five years following the closing.

In connection with the closing of the transaction, the Company entered into a transition services agreement with Compactor Rentals, pursuant to which the Company will provide certain services to Compactor Rentals until March 31, 2017.

See Note 10 - Discontinued Operations for further details related to the sale of the Waste Services Segment.

The Company used the proceeds from the transaction to pay transaction expenses, to repay in full the Company’s outstanding indebtedness with Bank of Kentucky, Inc., ("KY Bank") and to repay in full ISA’s term loan from Wells Fargo. The Company also used the proceeds to pay all outstanding amounts on ISA’s $5.0 million revolving line of credit with Wells Fargo which remained available following the closing.

On February 29, 2016, the Company entered into a Loan Agreement (the "2016 Loan") with MidCap Business Credit, LLC ("MidCap"). The 2016 Loan is secured by substantially all of the assets of the Company. Proceeds from this loan were used to pay transaction expenses and to pay off and close the remaining balance on the Wells Fargo revolving line of credit. See Note 3 - Long Term Debt and Notes Payable to Bank for further details.

Liquidity

The Company's sources of liquidity from 2014 to present have primarily consisted of proceeds from asset and equity sales as well as the idling of the auto shredder and refinancing of its working capital line of credit. Influenced primarily by the length and depth of the metals market downturn and the Company's ongoing operating losses, the Company may not be able to fund future capital needs, including necessary working capital, funds for capital expenditures or debt service, from operating cash flow. Consequently, the Company may have to rely on third-party sources to fund capital needs or may have to rely on further asset sales or similar actions. The Company may be unable to obtain third-party financing or conduct asset sales on favorable terms or at all, which could materially and adversely affect our operating results, cash flow and liquidity. Furthermore, the Company cannot provide assurance that sufficient liquidity can be raised from one or more of these sources or that a desired transaction could be consummated within the period needed to meet certain obligations.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND GENERAL, Continued

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America ("GAAP") for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete consolidated financial statements. The Accounting Standards Codification ("ASC") as produced by the Financial Accounting Standards Board ("FASB") is the sole source of authoritative GAAP. The information furnished includes all adjustments, which are, in the opinion of management, necessary to present fairly our financial position as of September 30, 2016 and the results of our operations and changes in our cash flows for the periods ended September 30, 2016 and 2015. Results of operations for the period ended September 30, 2016 are not necessarily indicative of the results that may be expected for the entire year. Additional information, including the audited December 31, 2015 consolidated financial statements and the Summary of Significant Accounting Policies, is included in our Annual Report on Form 10-K for the year ended December 31, 2015, on file with the Securities and Exchange Commission.

Estimates

In preparing the consolidated financial statements in accordance with GAAP for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X, management must make estimates and assumptions. These estimates and assumptions affect the amounts reported for assets, liabilities, revenues and expenses, as well as affecting the disclosures provided. Examples of estimates include the allowance for doubtful accounts, estimates of deferred income tax assets and liabilities, estimates of inventory balances, and estimates of stock option and warrant values. The Company also uses estimates when assessing fair values of assets and liabilities acquired in business acquisitions as well as any fair value and any related impairment charges related to the carrying value of inventory and machinery and equipment and other long-lived assets. Despite the Company’s intention to establish accurate estimates and use reasonable assumptions, actual results may differ from these estimates.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. Upon consolidation, all inter-company accounts, transactions and profits have been eliminated.

Reclassifications

The Company has reclassified certain items within the accompanying Condensed Consolidated Financial Statements and Notes to Condensed Consolidated Financial Statements for the prior year in order to be comparable with the current presentation. These reclassifications had no effect on previously reported income (loss) or shareholders' equity.

Discontinued Operations

Prior year financial statements have been recast to reflect the sale of the Company's Waste Services Segment assets in the fourth quarter of 2015 in accordance with the Financial Accounting Standards Board Accounting Standards Codification 205-20-55 within discontinued operations. Results of discontinued operations are excluded from the accompanying Notes to Condensed Consolidated Financial Statements for all periods presented, unless otherwise noted. See Note 10 - Discontinued Operations.

Fair Value

The Company carries certain of its financial assets and liabilities at fair value on a recurring basis. These financial assets and liabilities are composed of cash and cash equivalents and derivative instruments. Long-term debt is carried at cost, and the fair value is disclosed herein. In addition, the Company measures certain assets, such as long-lived assets, at fair value on a non-recurring basis to evaluate those assets for potential impairment. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

In accordance with applicable accounting standards, the Company categorizes its financial assets and liabilities into the following fair value hierarchy:

Level 1 – Financial assets and liabilities with values based on unadjusted quoted prices for identical assets or liabilities in an active market. Examples of Level 1 financial instruments include active exchange-traded securities.

Level 2 – Financial assets and liabilities with values based on quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the asset or liability. Examples of Level 2 financial instruments include various types of interest-rate and commodity-based derivative instruments, and various types of fixed-income investment securities. Pricing models are utilized to estimate fair value for certain financial assets and liabilities categorized in Level 2.

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NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND GENERAL, Continued

Level 3 – Financial assets and liabilities with values based on prices or valuation techniques that require inputs that are both unobservable in the market and significant to the overall fair value measurement. These inputs reflect management's judgment about the assumptions that a market participant would use in pricing the asset or liability, and are based on the best available information, some of which is internally developed.

When determining the fair value measurements for financial assets and liabilities carried at fair value on a recurring basis, the Company considers the principal or most advantageous market in which it would transact and consider assumptions that market participants would use when pricing the asset or liability. When possible, ISA looks to active and observable markets to price identical assets or liabilities. When identical assets and liabilities are not traded in active markets, the Company looks to market observable data for similar assets and liabilities. Nevertheless, certain assets and liabilities are not actively traded in observable markets, and uses alternative valuation techniques to derive fair value measurements.

The Company uses the fair value methodology outlined in the related accounting standards to value the assets and liabilities for cash, debt and derivatives. All of our cash is defined as Level 1 and all our debt and derivative contracts are defined as Level 2.

In accordance with this guidance, the following table represents our fair value hierarchy for Level 1 and Level 2 financial instruments at September 30, 2016 (in thousands):

	Fair Value at Reporting Date Using Quoted Prices in Active Markets for Identical Assets	Significant Other Observable Inputs	
Assets:	Level 1	Level 2	Total
Cash and cash equivalents	$ 492	$ —	$ 492
Liabilities:			
Long-term debt	$ —	$ (2,321)	$ (2,321)
Long term debt, related parties	—	(1,504)	(1,504)
Capital lease obligations	—	(1,262)	(1,262)

The Company had no transfers in or out of Levels 1 or 2 fair value measurements, and no activity in Level 3 (except impairment of property and equipment) fair value measurements for the nine month periods ended September 30, 2016 or 2015.

Common Stock and Share-based Compensation Arrangements

The Company has a Long Term Incentive Plan adopted in 2009 ("LTIP") under which it may grant equity awards for up to 2.4 million shares of common stock, which are reserved by the Board of Directors for issuance of equity awards. The Company provides compensation benefits by granting stock options and other share-based awards to employees and directors. The exercise price of each option is equal to the market price of our stock on the date of grant. The maximum term of the option is five years. The plan is accounted for based on FASB’s authoritative guidance titled "ASC 718 - Compensation - Stock Compensation." The Company recognizes share-based compensation expense for the fair value of the awards, on the date granted, on a straight-line basis over their vesting term. Compensation expense is recognized only for share-based payments expected to vest. The Company estimates forfeitures at the date of grant based on our historical experience and future expectations.

The Company uses the grant date stock price to value the Company's restricted stock units. The fair value of each restricted stock unit is estimated on the date of grant.

The Company uses the Modified Black-Scholes-Merton option-pricing model to value the Company's stock options for each employee stock option award. See Note 7 - Share Based Compensation. Using these option pricing models, the fair value of each stock option award is estimated on the date of grant.

There are two significant inputs into the stock option pricing models: expected volatility and expected term. The Company estimates expected volatility based on volatility of the Company's stock over a term equal to the expected term of the option granted. The expected term of stock option awards granted is derived from historical exercise experience under the Company's stock option plans and represents the period of time that stock option grants are expected to be outstanding.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND GENERAL, Continued

The expected term assumption incorporates the contractual term of an option grant, as well as the vesting period of an award. The risk-free interest rate is based on the implied yield on a U.S. Treasury constant maturity with a remaining term equal to the expected term of the option granted. The assumptions used in calculating the fair value of stock-based payment awards represent management's best estimates, but these estimates involve inherent uncertainties and the application of management's judgment. As a result, if factors change and different assumptions are used, stock-based compensation expense could be materially different in the future. In addition, the Company is required to estimate the expected forfeiture rate, and only recognize expense for those shares expected to vest. If the actual forfeiture rate is materially different from the estimate, the stock-based compensation expense could be significantly different from what was recorded in the current period.

Treasury shares or new shares are issued for exercised options. The Company does not expect to repurchase any additional shares within the following annual period to accommodate the exercise of outstanding stock options.

Under the LTIP, the Company may grant any of these types of awards: non-qualified and incentive stock options; stock appreciation rights; and other stock awards including stock units, restricted stock units, performance shares, performance units and restricted stock. The performance goals that the Company may use for such awards will be based on any one or more of the following performance measures: cash flow; earnings; earnings per share; market value added or economic value added; profits; return on assets; return on equity; return on investment; revenues; stock price; or total shareholder return.

The LTIP is administered by a committee selected by the Board consisting of two or more outside members of the Board. The Committee may grant one or more awards to our employees, including our officers, our directors and consultants, and will determine the specific employees who will receive awards under the plan and the type and amount of any such awards. A participant who receives shares of stock awarded under the plan must hold those shares for six months before the participant may dispose of such shares.

Subject to shareholder approval and restrictions on exercisability set forth in a Stock Option Agreement entered into on December 2, 2013 between the Company and Algar (the “Stock Option Agreement”), the Company granted Algar an option to purchase a total of 1.5 million shares (in four tranches) of Company common stock (the "Algar Options") at an exercise price per share of $5.00. The Algar Options were not issued under the LTIP. The Company's shareholders approved the Algar Options on October 15, 2014. On September 30, 2016, the Company and Algar mutually agreed to terminate the Management Agreement between them dated as of December 1, 2013. As part of the agreement to terminate the Management Agreement, the Stock Option Agreement was also terminated. See Note 6 - Related Party Transactions for further details.

The Company used the Lattice-Based model to value the Company's stock options for the Algar Options due to market and performance conditions prior to September 30, 2016. See Note 7 - Share Based Compensation. The fair value of the Algar Options was estimated at the end of each quarter for two of the tranches due to ongoing performance conditions. For the first two tranches, the performance conditions were met.

Other Income

In the third quarter of 2016, the Company received insurance proceeds in the amount of $571.4 thousand related to an insurance claim made for six roofs on certain of the Company's buildings due to weather related damage. The Company recognized a gain of $233.3 thousand, net of $80.0 thousand of impairment write-downs of the related roofs, consulting fees related to the claim, and amounts set aside in accrual for repairs on leased properties.

Subsequent Events

The Company has evaluated the period from September 30, 2016 through the date the financial statements herein were issued and noted no subsequent events requiring recognition or disclosure in the financial statements.

Impact of Recently Issued Accounting Standards

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606). The amendments in ASU 2014-09 affect any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets unless those contracts are within the scope of other standards (e.g., insurance contracts or lease contracts). The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The amendments are effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. The Company has not yet assessed the impact of the adoption of ASU 2014-09 on our Condensed Consolidated Financial Statements.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND GENERAL, Continued

In August 2014, the FASB issued ASU No. 2014-15, *Presentation of Financial Statements-Going Concern (Subtopic 205-40)*. The amendments in ASU 2014-15 are intended to define management’s responsibility to evaluate whether there is substantial doubt about an organization’s ability to continue as a going concern and to provide related footnote disclosures. The amendments are effective for annual periods ending after December 15, 2016, and interim periods thereafter. Early application is permitted for annual or interim reporting periods for which the financial statements have not previously been issued. The Company does not expect the standard to have a material impact on the Condensed Consolidated Financial Statements.

In April 2015, the FASB issued ASU 2015-03, Interest-Imputation of Interest: Simplifying the Presentation of Debt Issuance Costs. The guidance requires an entity to present debt issuance costs in the balance sheet as a direct reduction from the carrying amount of the debt liability, consistent with debt discounts, rather than as an asset. Amortization of debt issuance costs will continue to be reported as interest expense. Debt issuance costs related to revolving credit arrangements, however, will continue to be presented as an asset and amortized ratably over the term of the arrangement. ASU 2015-03 is effective for reporting periods beginning after December 15, 2015 including interim periods within those annual periods. Upon adoption, ASU 2015-03 should be applied on a retrospective basis. The Company adopted ASU 2015-03 in the first quarter of 2016 and presented debt issuance costs related to a revolving credit arrangement as an asset which will amortize ratably over the term of the arrangement.

In July 2015, the FASB issued ASU 2015-11, Inventory, which simplifies the measurement principle of inventories valued under the First-In, First-Out ("FIFO") or weighted average methods from the lower of cost or market to the lower of cost and net realizable value. ASU 2015-11 is effective for reporting periods beginning after December 15, 2016 including interim periods within those annual periods. The Company does not expect the standard to have a material impact on the Condensed Consolidated Financial Statements.

In November 2015, the FASB issued ASU 2015-17, Balance Sheet Classification of Deferred Taxes, which requires that deferred tax assets and liabilities be classified as noncurrent on the consolidated balance sheet. ASU 2015-17 is effective for annual periods beginning after December 15, 2016, including interim periods within those annual periods. Early adoption is permitted as of the beginning of an interim or annual reporting period. Upon adoption, ASU 2015-17 may be applied either prospectively or retrospectively. The Company does not expect the adoption of this guidance to have a material impact on the Condensed Consolidated Financial Statements.

In February 2016, the FASB issued ASU No. 2016-02, Leases, to improve financial reporting about leasing transactions. This ASU will require organizations that lease assets (“lessees”) to recognize a lease liability and a right-of-use asset on its balance sheet for all leases with terms of more than twelve months. A lease liability is a lessee’s obligation to make lease payments arising from a lease, measured on a discounted basis and a right-of-use asset represents the lessee’s right to use, or control use of, a specified asset for the lease term. The amendments in this ASU simplify the accounting for sale and leaseback transactions primarily because lessees must recognize lease assets and lease liabilities. This ASU leaves the accounting for the organizations that own the assets leased to the lessee ("lessor") largely unchanged except for targeted improvements to align it with the lessee accounting model and Topic 606, Revenue from Contracts with Customers.

The amendments in ASU 2016-02 are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Lessees (for capital and operating leases) and lessors (for sales-type, direct financing, and operating leases) must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The modified retrospective approach would not require any transition accounting for leases that expired before the earliest comparative period presented. Lessees and lessors may not apply a full retrospective transition approach. The Company is evaluating the potential impact of ASU 2016-02 on the Condensed Consolidated Financial Statements.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows, *Classification of Certain Cash Receipts and Cash Payments*, which provides guidance on eight specific cash flow issues. ASU 2016-15 is effective for annual periods beginning after December 15, 2017, including interim periods within those annual periods. Early adoption is permitted as of the beginning of an interim or annual reporting period. Upon adoption, ASU 2016-15 should be applied retrospectively. The Company is evaluating the potential impact of ASU 2016-15 on the Condensed Consolidated Financial Statements.

NOTE 2 – INVENTORIES

The Company's inventories primarily consist of ferrous and non-ferrous scrap metals, and are valued at the lower of average purchased cost or market based on the specific scrap commodity. Quantities of inventories are determined based on our inventory systems and are subject to periodic physical verification using estimation techniques including observation, weighing and other industry methods. The Company recognizes inventory impairment and related adjustments when the market value, based upon current market pricing, falls below recorded value or when the estimated volume is less than the recorded volume of the inventory. The Company records the loss in cost of sales in the period during which the loss is identified.

Management spent much of 2014 and early 2015 working to assess the Company's automobile shredder residue ("ASR") process. Significant process and strategy changes associated with the ASR process were made. These changes, combined with the significant metals market reduction in market demand and prices experienced in late 2014 and through 2015, caused management to perform a lower of cost-or-market assessment, which resulted in inventory write-downs during the nine months ended September 30, 2015 in the amount of $1.1 million charged to cost of sales as a result of impairment associated primarily with ferrous market price decreases. The Company did not have a lower of cost-or-market inventory write-down in the nine month period ended September 30, 2016.

Some commodities are in saleable condition at acquisition. The Company purchases these commodities in small amounts until it has a truckload of material available for shipment. Some commodities are not in saleable condition at acquisition. These commodities must be shredded, torched or baled. ISA does not have work-in-process inventory that needs to be manufactured to become finished goods. The Company includes processing costs in inventory for all commodities by weight.

Inventories as of September 30, 2016 and December 31, 2015 consist of the following:

	September 30, 2016 (unaudited)				December 31, 2015			
	Raw Materials	Finished Goods	Processing Costs	Total	Raw Materials	Finished Goods	Processing Costs	Total
	(in thousands)							
Ferrous and non-ferrous materials	$ 1,864	$ 614	$ 422	$ 2,900	$ 1,354	$ 649	$ 404	$ 2,407
Other	—	—	—	—	—	3	—	3
Total inventories for sale	$ 1,864	$ 614	$ 422	$ 2,900	$ 1,354	$ 652	$ 404	$ 2,410

NOTE 3 – LONG TERM DEBT AND NOTES PAYABLE TO BANK

Summary:

During 2014, the Company had certain loans with Wells Fargo and certain loans with KY Bank. As of December 31, 2014, the Company was in default under the Wells Fargo loans and during the second half of 2015 entered into a Forbearance Agreement with Wells Fargo whereby the due dates on the loans were accelerated and the Company was required to take certain actions. During 2015, as more fully described in Note 1 - Summary of Significant Accounting Policies and General, the Company took steps to pay down debt and increase liquidity. On December 4, 2015, in conjunction with the sale of substantially all assets of the Company's Waste Services Segment, the Company paid off the KY Bank loans and certain Wells Fargo loans. As of December 31, 2015, the Company had an outstanding balance of $19.7 thousand to Wells Fargo. Additionally, on February 29, 2016, the Company closed on new financing with MidCap and paid off in full remaining amounts due to Wells Fargo. Additionally on February 29, 2016, the Company converted certain amounts payable to related parties into unsecured term notes payable to the same related parties as more fully described in Note 6 - Related Party Transactions. See Note 1 - Summary of Significant Accounting Policies and General below for further details.

MidCap:

On February 29, 2016, the Company entered into the 2016 Loan, which is a $6.0 million senior, secured asset-based line of credit with MidCap. The Company may borrow up to the sum of (a) 85% of the value of its eligible domestic accounts receivable; (b) the lesser of (i) $2.5 million and (ii) 75% of the net orderly liquidation value of eligible inventory; and (c) the lesser of (i) $500,000 and (ii) 40% of appraised net forced liquidation value of eligible fixed assets (the "Equipment Sublimit"). The Equipment Sublimit shall amortize monthly on a straight line basis over sixty (60) months with no reduction to the overall line of credit availability.

Proceeds from this loan were used to pay transaction expenses, pay off and close the remaining balance on the Wells Fargo revolving line of credit and fund working capital requirements.

The interest rate on the 2016 Loan is equal to the prime rate (3.5% as of September 30, 2016) plus 250 basis points (2.50%). In the Event of a Default (as defined in the 2016 Loan Agreement), the interest rate will increase by 300 basis points (3.00%). The 2016 Loan also has a monthly collateral-monitoring fee equal to 27.5 basis points (0.275%) of the average daily balance, an annual facility fee of 100 basis points (1.00%) and an unused line fee equal to an annual rate of 50 basis points (0.50%) of the average undrawn portion of the 2016 Loan.

The 2016 Loan has a maturity date of February 28, 2018.

The Company is subject to a prepayment fee of $120.0 thousand if the 2016 Loan is terminated or prepaid prior to the one year anniversary of the loan. The Company is subject to a prepayment fee of $60.0 thousand if the 2016 Loan is terminated or prepaid subsequent to the one year anniversary of the loan, but prior to the maturity date. The $60.0 thousand fee is reduced to zero if the 2016 Loan is refinanced by an FDIC insured institution after eighteen months from February 29, 2016.

Interest and monthly fees under the 2016 Loan are payable monthly in arrears.

The 2016 Loan Agreement contains a minimum line availability covenant equal to $350.0 thousand. This covenant may be replaced by a Fixed Charge Coverage Ratio ("FCCR") covenant once the Company has achieved a FCCR of 1.0x on an annualized basis.

The Company granted MidCap a first priority security interest in all of the assets of ISA pursuant to a Security Agreement.

The Company is allowed to sell or refinance up to $3.0 million in fair market value of real property provided (i) the proceeds from such refinance or sale remain with the Company; and (ii) no event of default exists at the time of such refinance or sale.

The 2016 Loan had availability of $1.8 million as of September 30, 2016.

Wells Fargo:

On June 13, 2014, the Company entered into a senior, secured credit facility (the "Credit Agreement") with Wells Fargo pursuant to which Wells Fargo granted the Company a revolving line of credit of up to $15.0 million (the "Revolving Loan"), up to $1.0 million of which was available to the Company as a sub-facility for letters of credit. As of December 31, 2015, all loans under the credit agreement except the Revolving Loan had been paid in full. The Company was able to borrow up to 85% of the value of its eligible accounts receivable and 65% of the value of eligible inventory under the Revolving Loan. As of December 31, 2015, an availability block that limited borrowings under the revolver in the amount of $1.6 million was in place.

NOTE 3 – LONG TERM DEBT AND NOTES PAYABLE TO BANK, Continued

The Credit Agreement also provided the Company with a secured equipment term loan of $2.8 million (the "Term Loan"). The Company used the proceeds from the Credit Agreement to repay in full its prior credit facility and no further amounts can be borrowed.

As of December 31, 2015, the Company had $0.8 million available under the Revolving Loan.

The Bank of Kentucky:

Until December 4, 2015, WESSCO owed amounts under two promissory notes (collectively, the "KY Bank Notes") in favor of KY Bank, one in the amount of $3.0 million (the "Term Note") and one in the amount of $1.0 million (the "Line of Credit Note"). Additionally, on January 15, 2015, the Company signed a new line of credit ("2015 Line of Credit Note") in the amount of $1.0 million with KY Bank. The draw period for the 2015 Line of Credit Note was set to expire on January 14, 2016. All amounts under the KY Bank Notes were repaid on December 4, 2015 in conjunction with the sale of a majority of the assets of the Company's Waste Services Segment. The Company used the proceeds from the Term Note to pay $3.0 million against a previous Company loan. WESSCO used proceeds from the Line of Credit Note and the 2015 Line of Credit Note to purchase additional equipment. The Company signed a $3.0 million demand promissory note in favor of WESSCO in exchange for the proceeds of WESSCO's Term Note. All amounts owed to KY Bank were paid in full as of December 4, 2015 and no further amounts can be borrowed under the facilities.

Amounts owed to K&R, LLC and 7100 Grade Lane, LLC are more fully described in Note 6 - Related Party Transactions.

Long term debt as of September 30, 2016 and December 31, 2015 consisted of the following:

	2016	2015
	(Unaudited)	
	(in thousands)	
Revolving credit facility with MidCap at September 30, 2016 and Wells Fargo at December 31, 2015, see above description for additional details.	$ 2,321	$ 20
K&R, LLC related party note (See Note 6 - Related Party Transactions)	884	—
7100 Grade Lane, LLC related party note (See Note 6 - Related Party Transactions)	620	—
	3,825	20
Less current maturities	—	20
	$ 3,825	$ —

The annual maturities of long term debt (in thousands) for the next five twelve-month periods and thereafter ending September 30 of each year are as follows:

2017	$	—
2018	2,321	
2019	—	
2020	1,504	
2021	—	
Total	$	3,825

NOTE 4 - LEASE COMMITMENTS

Operating Leases:

The Company leases a portion of its Louisville, Kentucky facility from a related party (see Note 6 - Related Party Transactions) under an operating lease expiring December 31, 2017 (the 7100 Lease). The lease amount is $53.8 thousand per month. In addition, the Company is responsible for real estate taxes, insurance, utilities and maintenance expense.

As described in Note 1 - Summary of Significant Accounting Policies and General, the Company signed a lease, effective December 1, 2014, to lease a facility in the Seymour, Indiana area. This lease is for a period of three years. The Company has the option to extend the lease for three (3) additional three (3) year periods. Rent is $8.0 thousand per month and increases each year by $0.2 thousand per month. In the event ISA exercises the option to renew the lease for a second three-year term at the end of the second three-year term, ISA has the option to purchase the property.

The Company signed a lease, effective October 1, 2014, to lease three cranes for $28.9 thousand per month (the "Crane Lease"). This lease was for a period of five years. On May 1, 2016, the Company entered into an amendment to the Crane Lease, whereby the lease converted from an operating lease to a capital lease. See details below in Capital Leases section.

The Company previously leased equipment from a related party (see Note 6 - Related Party Transactions) under an operating lease for a monthly payment of $5.5 thousand. The lease expired November 2015.

The Company previously leased equipment from a related party (see Note 6 - Related Party Transactions) under an operating lease for a monthly payment of $5.0 thousand. The lease expired May 2016.

The Company previously leased office space in Dallas, Texas. The lease expired April 2015.

The Company leased a lot in Louisville, KY for a term that commenced in March 2012 and ended in February 2016. The monthly payment amount from March 2012 through February 2014 was $3.5 thousand. Beginning March 2014, the monthly payment amount increased to $3.8 thousand for the remaining term. As of August 31, 2015, the Company entered into a settlement to abandon the leased property and pay the remaining balance of scheduled payments over a 19 month period, ending March 31, 2017. As the lease was terminated and obligation recorded, future payments are not included in the future minimum lease payments table below.

As described in Note 1 - Summary of Significant Accounting Policies and General, on April 30, 2015, the Company entered into a lease agreement with LK Property (see Note 6 - Related Party Transactions), for a portion of the 4.4 acre parcel of real estate located at 6709 Grade Lane, Louisville, Kentucky in the amount of $3.0 thousand per month. The lease terminates on April 14, 2019, but the Company has the right to terminate the lease and vacate the leased premises upon 90 days notice. The Company is required to reimburse the lessor for 40% of the property taxes on the parcel during the term.

Future minimum lease payments for operating leases for the next five twelve-month periods ending September 30 of each year, in thousands, as of September 30, 2016 are as follows:

2017	$	557
2018	177	
2019	—	
2020	—	
2021	—	
Future minimum lease payments	$	734

Total lease expense for the nine months ended September 30, 2016 and 2015 was $775.7 thousand and $1.0 million, respectively.

NOTE 4 - LEASE COMMITMENTS, Continued

Capital Leases:

On May 1, 2016, the Company entered into an amendment to the Crane Lease, whereby the lease is extended through April 30, 2021. Payments are $14.5 thousand per month for the first twelve months following the amendment date, followed by monthly payments of $31.3 thousand thereafter for the reminder of the lease term. There is no bargain purchase option associated with the Crane Lease. Based on the new lease terms, the Company classified the Crane Lease as a capital lease. At inception, the Company recorded a capital lease obligation of $1.3 million. The Company used a weighted average cost of capital of 9.3% to calculate the capital lease obligation. For the nine months ended September 30, 2016, the Company has recorded $107.1 thousand in depreciation expense and $49.4 thousand in interest expense related to the Crane Lease.

Future minimum lease payments for the next five twelve-months periods ending September 30 of each year, in thousands, as of September 30, 2016 are as follows:

	Total	Principal	Interest
2017	$258	$144	$114
2018	375	283	92
2019	376	311	65
2020	375	341	34
2021	188	183	5
	$1,572	$1,262	$310

NOTE 5 – PER SHARE DATA

The computation for basic and diluted earnings (loss) per share is as follows:

Nine months ended September 30, 2016 compared to nine months ended September 30, 2015:

	2016	2015
	(in thousands, except per share information)	
Continuing operations:		
Basic loss per share		
Net loss	$ (2,990)	$ (6,540)
Weighted average shares outstanding	8,042	7,979

Basic loss per share	$ (0.37)	$ (0.82)
Diluted loss per share		
Net loss	$ (2,990)	$ (6,540)
Weighted average shares outstanding	8,042	7,979
Add dilutive effect of assumed exercising of stock options and warrants	—	—
Diluted weighted average shares outstanding	8,042	7,979
Diluted loss per share	$ (0.37)	$ (0.82)

	2016	2015
	(in thousands, except per share information)	
Discontinued operations:		
Basic income per share		
Net income	$ —	$ 1,052
Weighted average shares outstanding	8,042	7,979
Basic income per share	$ —	$ 0.13
Diluted income per share		
Net income	$ —	$ 1,052
Weighted average shares outstanding	8,042	7,979
Add dilutive effect of assumed exercising of stock options and warrants	—	—
Diluted weighted average shares outstanding	8,042	7,979
Diluted income per share	$ —	$ 0.13

NOTE 5 – PER SHARE DATA, Continued

Three months ended September 30, 2016 compared to three months ended September 30, 2015:

	2016	2015
	(in thousands, except per share information)	
Continuing operations:		
Basic loss per share		
Net loss	$ (938)	$ (1,596)
Weighted average shares outstanding	8,067	8,000
Basic loss per share	$ (0.12)	$ (0.20)
Diluted loss per share		
Net loss	$ (938)	$ (1,596)
Weighted average shares outstanding	8,067	8,000
Add dilutive effect of assumed exercising of stock options and warrants	—	—
Diluted weighted average shares outstanding	8,067	8,000
Diluted loss per share	$ (0.12)	$ (0.20)

	2016	2015
	(in thousands, except per share information)	
Discontinued operations:		
Basic income per share		
Net income	$ —	$ 409
Weighted average shares outstanding	8,067	8,000
Basic income per share	$ —	$ 0.05
Diluted income per share		
Net income	$ —	$ 409
Weighted average shares outstanding	8,067	8,000
Add dilutive effect of assumed exercising of stock options and warrants	—	—
Diluted weighted average shares outstanding	8,067	8,000
Diluted income per share	$ —	$ 0.05

NOTE 6 - RELATED PARTY TRANSACTIONS

During the periods ended September 30, 2016 and 2015, the Company was involved in various transactions with related parties. A summary of transactions and related balances are as follows. The table at the end of this note should be used in referencing all below paragraphs.

K&R, LLC ("K&R") and 7100 Grade Lane, LLC ("7100 LLC"):

The Company is involved in various transactions with K&R and 7100 LLC, which are wholly-owned by Kletter Holdings LLC, the sole member of which was Harry Kletter, the Company's founder and former Chief Executive Officer. After Mr. Kletter's passing in January 2014, the Company's Chairman of the Board and interim Chief Executive Officer, Orson Oliver, assumed the roles of executor of Mr. Kletter’s estate and President of Kletter Holdings LLC. As of September 30, 2016, Mr. Kletter’s estate, K&R and the Harry Kletter Family Limited Partnership collectively, beneficially own in excess of 20% of the Company's issued and outstanding shares.

The Company leases a portion of the Louisville, Kentucky facility from 7100 LLC (previously from K&R) under an operating lease, the "7100 Lease", expiring December 2017. Additionally, the Company leased equipment from K&R under operating leases that expired November 2015 and May 2016. See Note 4 - Lease Commitments for additional information relating to the rent and lease agreements with K&R. During 2015 and continuing into 2016, the Company deferred a portion of these lease payments. A portion of this deferral was converted into a term note during 2016 as described below.

On September 13, 2013, K&R made a $500.0 thousand refundable, non-interest bearing deposit with the Company related to K&R's potential purchase of the Company's formerly owned real property located at 1565 East 4th Street in Seymour, Indiana. The Company was permitted and used the deposited funds for general corporate purposes. K&R did not acquire the property. Under the Company's lending arrangements, a refund of the deposit to K&R would have to be approved by the Company's lenders. This amount was converted into a term note during 2016 as described below.

As of September 30, 2016 and 2015, the Company had balances related to K&R and 7100 LLC pertaining to refundable lease and property deposits due to and from the Company, rents payable from the Company, notes payable due from the Company, accrued interest due from the Company, interest expense, and rent expense.

On February 29, 2016, K&R assigned its interest in the 7100 Lease to another entity, 7100 LLC, also controlled by Mr. Kletter’s estate. At that time, the total amount due to the estate’s various entities, which amounted to approximately $1.5 million and is inclusive of the $500.0 thousand noted above, became a subordinated, unsecured debt (the "Kletter

Notes") owed by the Company. A portion of the amount, approximately $620.3 thousand, is owed to K&R, with the remaining amount, approximating $883.8 thousand, owed to 7100 LLC. Interest will accrue monthly at a per annum rate of 5.0%. Interest will accrue until April 30, 2017 at which time interest will be paid monthly. Until maturity on December 31, 2020, the Kletter Notes are subject to intercreditor agreements between the respective Note holder and MidCap. This amount of $1.5 million represents all net amounts due to Kletter estate entities as of February 29, 2016 with the exception of a $32.0 thousand deposit owed by K&R to the Company. If the Company sells property it owns at 7110 Grade Lane in Louisville, Kentucky, it shall make a principal payment to K&R of $500.0 thousand. Otherwise, all remaining principal is due at maturity.

Algar:

Management services payments to Algar:

On December 2, 2013, the Company and Algar entered into a Management Services Agreement (the "Management Agreement"). On September 30, 2016 (the "Termination Effective Date"), the Company and Algar mutually agreed to terminate the Management Agreement pursuant to the Termination Agreement. See the details below.

Under the Management Agreement, Algar provided the Company with day-to-day senior executive level operating management services. Algar also provided business, financial, and organizational strategy and consulting services, as the Company's board of directors reasonably requested from time to time.

In connection with the Management Agreement, the Company's Board of Directors appointed Sean Garber as President and as a member of the Board of Directors.

Under the Management Agreement, the Company reimbursed Algar for the portion of Mr. Garber's salary that was attributable to Algar's services under the Management Agreement in an amount not exceeding $20.8 thousand per month, or $250.0 thousand per year plus other expenses. Also, under the Management Agreement, Algar was to be paid a bonus in an amount equal to 10.0% of any year-over-year increase in the Company's adjusted pre-tax income during the term. The term of the Management Agreement was effective December 1, 2013 and originally expired on December 31, 2016, subject to earlier termination upon mutual agreement or upon circumstances set forth in the agreement. On September 30, 2016, the Company and Algar mutually agreed to terminate the Management Agreement.

NOTE 6 - RELATED PARTY TRANSACTIONS, Continued

For the year ended December 31, 2014, Algar earned a bonus of $428.0 thousand. This amount was reduced by $50.0 thousand related to the real estate sale to SG&D described below. The bonus payable was further reduced on August 5, 2015, when the Company entered into a Stock Purchase Agreement with Algar, whereby the Company issued 50.7 thousand shares of its common stock to Algar for aggregate consideration equal to $189.0 thousand based on the fair value of the Company's common stock. The consideration was payable in the form of a reduction of the Company’s $378.0 thousand accrued but unpaid bonus compensation due to Algar as of August 5, 2015. For the nine month period ended September 30, 2016, the Company paid Algar the remaining $189.0 thousand related to the accrued but unpaid bonus compensation related to the bonus earned in 2014.

As of the Termination Effective Date, the Company and Algar mutually terminated the Management Agreement. The Termination Agreement provides that in satisfaction of all amounts owed to Algar under the Management Agreement, the Company will pay Algar: (i) $20,880 on the Termination Effective Date, (ii) an aggregate amount equal to $50,000, payable in three equal monthly installments on the last day of October, November and December 2016 (full amount accrued at September 30, 2016), and (iii) an amount equal to ten percent of the decrease, if any, in reported “Loss before income taxes” for the nine months ended September 30, 2016 as reported on the Condensed Consolidated Statements of Operations in the Company’s Quarterly Report on Form 10-Q for the period ended September 30, 2016, (the “3Q 2016 Form 10-Q”) as filed with the U.S. Securities and Exchange Commission, over the Company’s reported “Loss before income taxes” for the nine months ended September 30, 2015 as reported in the 3Q 2016 Form 10-Q (the "Accrued Bonus Payment"). The Accrued Bonus Payment will be payable as follows: subject to the availability of cash under applicable law and loan covenants, the Company will pay the Accrued Bonus Payment to Algar upon the first to occur of March 31, 2017, or the date of closing of a Change of Control Transaction, as defined. The Company accrued $180.0 thousand in bonus expense to Algar for the nine months ended September 30, 2016 related to the Accrued Bonus Payment. The Termination Agreement also provided for the cancellation of the Stock Option Agreement as of the Termination Effective Date. Mr. Garber and Mr. Oliver have agreed to the termination of the Irrevocable Proxies that were received in connection with the Management Agreement as of the Termination Effective Date. Mr. Garber has resigned all offices with the Company and his director position as of the Termination Effective Date.

Other transactions with Algar:

During 2016 and 2015, the Company participated in various other transactions with Algar. The Company sold scrap to Algar, bought scrap from Algar, leased equipment to and from Algar, and provided logistical and IT services to Algar. Related to these transactions, the Company has accounts receivable balances from Algar, an accounts payable balance to Algar, along with related income and expense as of September 30, 2016 and 2015.

Board of Directors' fees and consulting fees:

The Company pays board and committee fees to non-employee directors. Additionally, the Company paid financial consulting fees to one of its directors in 2015. Related to these transactions, the Company has accounts payable balances to the Board of Directors for fees and consulting fees, along with related expense at and as of September 30, 2016 and 2015.

LK Property Investments, LLC:

On April 30, 2015, ISA Real Estate LLC sold to LK Property, an entity principally owned by Daniel M. Rifkin, CEO of MetalX and the principal owner of RCP, a 4.4 acre parcel of real estate, located at 6709 Grade Lane, Louisville, Kentucky, for a purchase price of $1.0 million. The Company used the proceeds from the sale primarily for debt reduction and working capital. The loss on sale of this asset was $102.0 thousand.

On April 30, 2015, the Company entered into a lease agreement with LK Property, for a portion of the 4.4 acre parcel of real estate located at 6709 Grade Lane, Louisville, Kentucky in the amount of $3.0 thousand per month. The lease terminates on April 14, 2019, but the Company has the right to terminate the lease and vacate the leased premises upon 90 days notice. The Company is required to reimburse the lessor for 40% of the property taxes on the parcel during the term.

MetalX:

During 2016 and 2015, the Company held accounts receivables balances from MetalX related to scrap sales. For additional information regarding MetalX, see Note 9 - Financing and Related Matters.

SG&D Ventures, LLC.:

In May 2015, ISA Real Estate LLC sold to SG&D, an entity owned by shareholders of Algar, including Mr. Garber, an approximately 1-acre parcel of non-essential real estate, located at 7017 Grade Lane, Louisville, Kentucky, for an aggregate purchase price equal to independent third-party appraisal amount of $350.0 thousand. The Company received this appraisal before the sale. The purchase consideration consisted of $300.0 thousand in cash from SG&D and a credit of $50.0 thousand against bonus compensation previously accrued but not paid to Algar as described above. The gain on sale of this asset was $1.1 thousand.

NOTE 6 - RELATED PARTY TRANSACTIONS, Continued

Related party balances are as follows, in thousands:

		2016	2015
K&R, LLC and 7100 LLC:			
Deposit amounts owed to the Company by related parties	(1)	$ 42	$ 74
Property deposit payable to related parties	(2)	—	500
Note payable to related parties	(3)	1,504	—
Accrued interest to related parties	(2)	44	—
Facility rent payable to related parties	(2)	120	821
Equipment rent payable to related parties	(2)	15	132
Facility rent expense to related parties	(4)	484	484
Equipment rent expense to related parties	(4)	25	95
Interest expense to related parties	(4)	44	—
Algar, Inc.:			
Accounts receivable from Algar for scrap transactions	(1)	$ —	$ 93
Accounts receivable from Algar for logistical services	(1)	12	19
Accounts payable to Algar	(2)	50	28
Bonus payable to Algar	(2)	180	189
Revenue from scrap sales to Algar	(4)	7	94
Revenue from logistical services to Algar	(4)	48	42
Revenue from IT services to Algar	(4)	16	18
Scrap material purchases from Algar	(4)	1,204	883
Management fee expense	(4)	238	187
Bonus expense to Algar	(4)	180	—
Net rental income from Algar	(4)	16	—
Other expenses to Algar	(4)	14	32
Board of Directors: *			
Accounts payable to the Board of Directors for fees	(2)	$ 261	$ 250
Board of director fee expense	(4)	168	160
LK Property Investments, LLC:			
Lease deposit to LK Property	(1)	$ 3	$ 3
Accounts payable to LK Property	(2)	—	2
Rent expense to LK Property**	(4)	27	15
Loss on the sale of assets to LK Property	(4)	—	(102)
Metal X, LLC:			
Accounts receivable from Metal X	(1)	$ —	$ 19
Revenue from product sales to Metal X	(4)	116	1,817
SG&D Ventures, LLC:			
Gain on the sale of assets to SG&D	(4)	$ —	$ 1

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* Excludes insignificant amount of travel reimbursement.

**Excludes amounts reimbursed to LK Properties for utilities and property tax.

(1) Included in receivable from related parties on the Condensed Consolidated Balance Sheets; balances are as of September 30, 2016 and December 31, 2015.

(2) Included in payable to related parties on the Condensed Consolidated Balance Sheets; balances are as of September 30, 2016 and December 31, 2015.

(3) Included in long-term liabilities on the Condensed Consolidated Balance Sheets; balance is as of September 30, 2016 and December 31, 2015.

(4) Included in the Condensed Consolidated Statements of Operations; balances are for the nine months ended September 30, 2016 and September 30, 2015.

NOTE 7– SHARE-BASED COMPENSATION AND OTHER COMPENSATION AGREEMENTS

Following is a summary of stock option activity and number of shares reserved for outstanding options:

Options	**Number of shares** (in thousands)	Weighted Average Exercise Price per Share	Weighted Average Remaining Contractual Term	Weighted Average Grant Date Fair Value
Outstanding at December 31, 2014	2,152	$ 5.02	2.7 years	$ 2.23
Granted	20	5.71		