NEXT INC/TN
Form 10-Q
July 13, 2007

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

[X]

Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the Quarterly Period Ended June 1, 2007

OR

[ ]

Transition Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission File Number: 0-25247

NEXT, INC.

(Exact name of small business issuer as specified in its charter)

Delaware	**95-4675095**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

7625 Hamilton Park Drive, Suite 12

Chattanooga, Tennessee 37421

(Address and zip code of principal executive offices)

Registrant s telephone number, including area code: **(423) 296-8213**

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act (Check one):

Large accelerated filer [ ] Accelerated filer [ ] Non-accelerated filer [X]

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

As of June 1, 2007 there were 19,271,150 shares of the registrant s common stock issued and outstanding.

NEXT, INC.

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Part I FINANCIAL INFORMATION

Item 1.

Financial Statements

NEXT, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

		June 1, 2007 (unaudited)		December 1, 2006 (audited)
Assets				
Current assets:				
Cash	$	40,432	$	80,700
Accounts receivable, net of allowances for doubtful accounts and contractual allowances of $216,909 and $235,876, respectively		1,373,505		6,705,812
Notes receivable		38,475		37,707
Inventories		4,448,964		4,026,565
Prepaid expenses		353,565		373,183
Other current assets		144,670		449,081
Deferred taxes, current				400,000

Total current assets	6,399,611	12,073,048
Property, plant and equipment, net	2,535,157	2,662,838
Goodwill	4,369,825	4,369,825
Notes receivable	15,378	32,504
Deferred taxes	1,195,345	176,628
Other assets, net	1,263,469	1,444,080
Total Assets	$ 15,778,785	$ 20,758,923
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 1,313,819	$ 3,217,014
Accrued expenses and other current liabilities	695,156	1,025,848
Short-term debt and current maturities	3,446,247	860,866
Loan from stockholders	200,000	200,000
Line of credit	3,023,754	4,217,238
Total current liabilities	8,678,976	9,520,966
Long-term debt, less current maturities		3,235,785

Loan from stockholders, less current maturities	300,000	300,000
Total liabilities	8,978,976	13,056,751
Stockholders equity	6,799,809	7,702,172
Total Liabilities and Stockholders Equity	$ 15,778,785	$ 20,758,923

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

NEXT, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended	
	June 1, 2007 (unaudited)	June 2, 2006 (unaudited)
Net sales	$ 2,157,310	$ 4,823,634
Cost of sales	1,661,962	3,000,633
Gross profit	495,348	1,823,001
General, administrative, and selling expenses	1,224,793	1,545,266
Operating income (loss)	(729,445)	277,735
Interest	(150,487)	(175,679)
Other expense	(56,681)	(42,623)
Income (loss) before income taxes	(936,613)	59,433
Provision (benefit) for income taxes	(365,968)	36,538
Net income (loss)	(570,645)	22,895
Net income (loss) per share, basic and diluted	$ (0.03)	$
Weighted average shares outstanding, basic	18,574,296	18,309,795

Weighted average shares outstanding, diluted	18,574,296	18,473,036

	Six Months Ended	
	June 1, 2007 (unaudited)	June 2, 2006 (unaudited)
Net sales	$ 5,783,233	$ 9,674,041
Cost of sales	4,197,038	6,637,146
Gross profit	1,586,195	3,036,895
General, administrative, and selling expenses	2,783,014	3,000,176
Operating income (loss)	(1,196,819)	36,719
Interest	(322,951)	(342,991)
Other expense	(60,548)	(53,501)
Loss before income taxes	(1,580,318)	(359,773)
Benefit for income taxes	(618,717)	(131,035)
Net loss	(961,601)	(228,738)
Net loss per share, basic and diluted	$ (0.05)	$ (0.01)

Weighted average shares outstanding, basic and diluted	18,590,506	18,409,257

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

NEXT, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Six Months Ended	
	June 1, 2007 (unaudited)	June 2, 2006 (unaudited)
Cash flows from operating activities:		
Net loss	$ (961,601)	$ (228,738)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	332,346	373,329
Noncash compensation	1,011	1,011
Noncash fees	43,654	7,192
Loss on sale of asset		38,922
Bad debt expense	(4,200)	(24,927)
Deferred taxes	(618,717)	(131,035)
Changes in operating assets and liabilities:		
Accounts receivable	5,336,507	1,481,450
Notes receivable	16,358	20,264
Inventories	(422,399)	975,816
Prepaid expenses	49,618	(391,189)
Other assets	(55,589)	(23,690)

Accounts payable	(1,903,195)	(790,941)
Accrued expenses and other liabilities	(330,692)	(243,027)
Total adjustments	2,444,702	1,293,175
Net cash provided by operating activities	1,483,101	1,064,437
Cash flows from investing activities:		
Purchases of property, plant and equipment	(13,767)	(31,714)
Cash received from proceeds on sale of asset		2,700
Cash paid for intangible assets	(10,287)	(55,292)
Net cash used in investing activities	(24,054)	(84,306)
Cash flows from financing activities:		
Revolving credit facility, net	(1,193,484)	(1,620,698)
Proceeds from loans and notes payable		912,000
Repayments of long term debt, loans and notes payable	(305,831)	(132,091)
Fees paid for investment transaction		(20,240)
Issuance of common stock for investment transaction		500
Net cash used in financing activities	(1,499,315)	(860,529)

Net increase (decrease) in cash		(40,268)		119,602
Cash, beginning of period		80,700		152,601
Cash, end of period	$	40,432	$	272,203
Supplemental Information:				
Cash paid during the period for interest	$	306,693	$	346,578
Cash paid during the period for income taxes	$	6,248	$	
Non-Cash Investing and Financing Activities:				
Equity securities issued in payment of debt	$	344,574	$	
Equity securities retired in payment of note receivable	$	360,000	$	510,000
Equity securities issued in payment of services	$	30,000	$	
Equity securities retired to reduce vendor obligation	$		$	23,570

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

NEXT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

1.

Organization and Operations of Company

Next, Inc. (the Company) is the parent company of two wholly owned subsidiaries: (i) Next Marketing, Inc. (Next Marketing), and (ii) Choice International, Inc. (Choice). The Company is a creative and innovative sales and marketing organization that designs, develops, markets and distributes licensed products and imprinted sportswear primarily through key licensing agreements and the Company s own proprietary designs.

2.

Basis of Presentation and Summary of Significant Accounting Policies

Basis of Presentation

The condensed consolidated financial statements contained herein have been prepared in accordance with generally accepted accounting principles for interim financial statements, the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. (Prior to 2007, the Company filed quarterly reports on Form 10-QSB and therefore, the condensed consolidated financial statements therein were prepared in accordance with the instructions to Form 10-QSB and Item 310 of Regulation S-B in addition to generally accepted accounting principles for interim financial statements.) Accordingly, these financial statements do not include all the information and footnotes required by generally accepted accounting principles for annual financial statements. In addition, certain comparative figures presented have been reclassified to conform the prior year s data to the Company s current financial statements. In the opinion of management, the accompanying condensed consolidated financial statements contain all the adjustments necessary (consisting only of normal recurring accruals and adjustments) to fairly present the financial position of the Company at June 1, 2007 and December 1, 2006, and its results of operations and cash flows for the three months and six months ended June 1, 2007 and June 2, 2006. Operating results for the three and six months ended June 1, 2007, are not necessarily indicative of the results that may be expected for the fiscal year ending November 30, 2007. It is suggested that these condensed financial statements be read in conjunction with the financial statements and the notes thereto included in the Company s latest shareholders annual report (Form 10-KSB).

Principles of Consolidation

The accompanying unaudited condensed consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All significant inter-company balances and transactions have been eliminated.

Customer Base and Credit Concentration

The Company has developed a large, diverse, and distinguished customer base of traditional retailers that include national as well as large regional chains, specialty retailers, corporate accounts, college bookstores, motor sports, souvenir and gift shops, and golf shops. This expansion has been achieved through the acquisitions of CMJ Ventures, Inc., Lil Fan, Inc., Choice International, Inc., Sports-2-Schools, LLC, and their respective customer bases, the introduction of additional major product lines and distribution channels, such as the Motor Sports Division, which sells to a national auto dealer market consisting of approximately 9,000 potential customers, as well as expansion of its traditional national retail merchant customer base. In the six months ended June 1, 2007, sales to the Company s two largest customers accounted for 65% of total sales. In the six months ended June 2, 2006, sales to the Company s top four customers accounted 69% of total sales. The Company s management believes that the Company s credit risk exposure is limited based on current information available with respect to the financial strength of its customers and previously recorded reserves. Such estimates could change in the future.

The Company is subject to seasonality in its sales cycle due to the amount of college-licensed products. The seasonality of sales results in the majority of the Company s revenues being generated in the third and fourth quarters.

New Pronouncements

The Securities and Exchange Commission has issued a final rule on the Internal Control over Financial Reporting in Exchange Act Periodic Reporting of Non-Accelerated Filers and newly Public Companies . The final rules set the dates to comply with the internal control reporting requirements mandated by Section 404 of the Sarbanes-Oxley Act of 2002. Non-accelerated filers must provide managements assessment regarding internal control over financial statements in its annual report for fiscal years ending after December 15, 2007 which will be the Company s November 28, 2008 fiscal year end and must comply with the auditor attestation requirement in fiscal years ending after December 15, 2008, which will be the Company s November 27, 2009 fiscal year end. The Company plans to be in full compliance with these internal control reporting requirements by the effective dates.

In February 2007, the FASB issued Statement No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB No. 115 (SFAS No. 159). This statement permits an entity to choose to measure many financial instruments and certain other items at fair value. The statement permits all entities to choose to measure eligible items at fair value at specified election dates. SFAS 159 is effective for fiscal years beginning after November 15, 2007. The Company does not believe that adoption of this statement will have a material impact on its consolidated financial position or result of operations.

In September 2006, the FASB issued Statement No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans An Amendment of FASB Statement No. 87, 88, 106 and 132(R) (SFAS No. 158). This statement requires an employer to recognize in its financial statements the funded status of a defined benefit plan, determine the funded status at the end of the employer s fiscal year and recognize changes in the fund status of a defined postretirement plan in the year a change occurs. SFAS No. 158 becomes effective in phases beginning with financial statements issued for the fiscal years beginning after December 15, 2006 and completed by financial statements issued for the fiscal years beginning after December 15, 2008. The Company does not believe that adoption of this statement will have a material impact on its consolidated financial position or result of operations.

In September 2006, the FASB issued Statement No. 157, Fair Value Measurements, (SFAS No. 157). SFAS No. 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. Accordingly, SFAS No. 157 does not require any new fair value measurements, but will change current practice for some entities. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company will apply this standard prospectively. The Company is studying this pronouncement, but currently believes it will not have a material effect on the Company s consolidated financial statements.

In June 2006, the FASB published Interpretation No. 48, Accounting for Uncertainty in Income Taxes, (Interpretation No. 48). This interpretation requires companies to determine whether it is more likely than not that a tax position will be sustained upon examination by the appropriate taxing authorities before any part of the benefit can be recorded in the financial statements. Interpretation No. 48 also provides guidance on derecognition classification, accounting in interim periods, and disclosure requirements for tax contingencies. This interpretation is effective for fiscal years beginning after December 15, 2006. The Company does not believe that the application of Interpretation No. 48 will have a material effect on the Company s results of operations or financial position.

In February 2006, the FASB issued SFAS No. 155, Accounting for Certain Hybrid Financial Instruments an amendment of FASB Statements No. 133 and 140 (SFAS No. 155). Among other things, SFAS No. 155 allows financial statement preparers to elect fair value measurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation. This statement also eliminates the exemption from applying SFAS No. 133 to interests in securitized financial assets. SFAS No. 155 is effective for all financial instruments acquired or issued by the Company after fiscal year 2008, beginning December 1, 2007. The Company does not believe that adoption of this statement will have a material impact on its consolidated financial position or result of operations.

3.

Inventories

Inventories are valued at the lower of cost or market. Cost is determined by the first-in, first-out method, and market represents the lower of replacement cost or net realizable value. Inventories as of June 1, 2007 and December 1, 2006, consisted of the following:

	June 1, 2007	December 1, 2006
Raw materials	$ 2,537,060	$ 2,657,611
Finished goods	1,911,904	1,368,954
	$ 4,448,964	$ 4,026,565

4.

Income Taxes

Income taxes have been computed in accordance with SFAS No. 109, Accounting for Income Taxes. This standard requires, among other things, recognition of future tax expenses or benefits, measured using enacted tax rates, attributable to taxable or deductible temporary differences between financial statements and income tax reporting bases of assets and liabilities.

The ultimate realization of deferred tax assets is dependent upon the attainment of forecasted results of operations. Management has taken these and other factors into consideration in recording the deferred tax estimate. The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and liabilities at June 1, 2007 and December 1, 2006, are as follows:

	June 1, 2007	December 1, 2006
Assets:		
Accounts receivable allowance	$ 16,850	$ 4,185
Net operating loss carryforwards	1,466,194	882,342
Total deferred tax assets	$ 1,483,044	$ 886,527
Liabilities:		
Property, plant and equipment	$ 228,750	$ 240,034
Goodwill and other intangibles	58,949	69,865
Total deferred tax liabilities	$ 287,699	$ 309,899
Deferred taxes, net	$ 1,195,345	$ 576,628
Current	$	$ 400,000
Noncurrent	$ 1,195,345	$ 176,628

5.

Short-Term and Long-Term Debt

Short-term and long-term debt at June 1, 2007 and December 1, 2006 consisted of the following:

	June 1, 2007		December 1, 2006	
	Short Term	Long Term	Short Term	Long Term
Revolving credit facility	$ 3,023,754	$	$ 4,217,238	$
Notes payable	3,646,247	300,000	1,060,866	3,535,785
Total	$ 6,670,001	$ 300,000	$ 5,278,104	$ 3,535,785

Various assets collateralize all of the Company s debt and certain amounts are guaranteed by its principal stockholders.

The Company signed a new credit facility with National City Bank on January 31, 2007 for two years, expiring on January 31, 2009. The new agreement increased the total line to $7,500,000, decreased the interest rate to prime plus or minus .25% (depending on certain financial ratios being met), increased the advance rates on accounts receivable to 85%, and established new quarterly financial covenants. The agreement provides for monthly payments of interest at the Bank s published prime rate plus .25% (8.25% was the published rate at June 1, 2007). The loan is collateralized by accounts receivable, inventory, and limited personal guarantees of the Company s Chief Executive Officer and one board member.

As of June 1, 2007, the Company was not in compliance with the new quarterly financial covenants, and has been advised by National City Bank that these violations will be waived with full reservation of rights so long as the Company meets revised and specific performance criteria which, as of the date of this Form 10-Q, have not been finalized. Additionally, First Federal Savings Bank of Wabash has agreed to the same waiver as National City Bank and on substantially identical terms. There are no covenants with any other lenders to the Company.

In accordance with EITF 86-30 and related guidance, the Company has evaluated the above referenced waivers and concluded that the related notes payable to First Federal Savings Bank of Wabash should be reclassified as current debt at this time. The Company has carried the National City Bank credit facility as a current liability since its inception.

On November 30, 2006, the Company entered into a subordinated loan agreement with Next Investors, LLC for $500,000, to replace an agreement originally executed on July 20, 2005. The purpose of this loan was to provide working capital to be repaid out of future cash flows. The loan has an interest rate of prime plus .25% and maturity date of November 30, 2008. Next Investors, LLC principal partners are comprised of one director and two major shareholders of the Company. As of June 1, 2007, interest expense on this loan totaled $10,743 and $21,486 for the three and six months then ended, respectively, and accrued interest was $21,341. As of June 2, 2006, interest expensed and accrued for this loan totaled $9,479 and $19,167, respectively, for the three and six months then ended.

On April 6, 2006, the Company entered into a Subscription Agreement for Convertible Notes and Warrants with the following investors: DKR Soundshore Oasis Holding Fund Ltd., Alpha Capital Aktiengesellschaft, Monarch Capital Fund, Ltd., Iroquois Master Fund, Ltd., and Bluegrass Growth Fund, LP (collectively, the Investors), pursuant to which the Company issued to the Investors, as a group, $984,960 in principal amount of convertible promissory notes (the Notes) and warrants (the Warrants) to purchase 849,103 shares of common stock of the Company (the Common Stock). The Notes require equal monthly payments of cash or stock in the amount of $86,184 over a 12-month period starting 115 days after closing and will be fully subordinated to the Company s senior lenders. The Notes are convertible into a total of 1,698,207 shares of Common Stock at a conversion rate of $.58 in principal amount of the Notes per share. The warrants have a three-year term and an exercise price of $.68 per share of Common Stock. The Company has filed a registration statement with the Securities and Exchange Commission for the offer and sale by the Investors of the Common Stock underlying both the Notes and Warrants. In connection with these transactions, the Company issued to JPC Capital Partners, Inc., as placement agent, warrants to purchase 152,838 shares of Common Stock on the same terms as the Warrants issued to the Investors. As of June 1, 2007 the balance outstanding on this debt obligation was $86,638, which is the final payment; five of the twelve required monthly payments were paid in stock and the remainder in cash since inception of this obligation.

6.

Contingencies

From time to time, the Company is a party to litigation arising in the normal course of its business operations. In the opinion of management, after consulting with legal counsel, it is not anticipated that the matters will have a material adverse impact on the Company s financial condition, liquidity or results of operations.

7.

Stockholders Equity

Stockholders equity was comprised of the following:

	June 1, 2007	December 1, 2006
Common stock, $.001 par value; 100,000,000 shares authorized, 19,271,150 and 18,626,029 shares issued and outstanding at June 1, 2007 and December 1, 2006, respectively	$ 19,271	$ 18,626
Additional paid-in capital	7,336,171	7,278,589
Retained earnings (deficit)	(528,838)	432,763
Unearned compensation	(26,795)	(27,806)
Total stockholders equity	$ 6,799,809	$ 7,702,172

On February 27, 2007, the Company s former Chief Executive Officer, William B. Hensley, III, remitted 600,000 shares of Next, Inc. common stock to satisfy a promissory note executed for $360,000 to purchase certain licenses. These shares were cancelled and taken out of circulation. The transaction was valued at the market price of the stock on November 28, 2006, pursuant to the terms of a purchase agreement dated November 28, 2006, as amended. Pursuant to the terms of the purchase agreement, Mr. Hensley elected on February 27, 2007, to deliver shares of common stock of the Company to satisfy the promissory note.

8.

Earnings (Loss) Per Share

The Company accounts for earnings (loss) per share (EPS) in accordance with SFAS No. 128, Earnings (Loss) Per Share. SFAS No. 128 requires the presentation of basic and fully diluted EPS. Basic and diluted EPS for the three and six months ended June 1, 2007 and June 2, 2006, are calculated on the basis of the weighted average number of common shares outstanding.

The following table sets forth the computation of basic and diluted earnings (loss) per share:

	Three months ended	
	June 1, 2007	June 2, 2006
Numerator:		
Net income (loss)	$ (570,645)	$ 22,895
Denominator:		
Basic weighted average common shares	18,574,296	18,309,795
Effect of dilutive stock options, warrants, and contingent acquisition related shares		163,241
Denominator for diluted earnings (loss) per share	18,574,296	18,473,036
Basic and diluted earnings (loss) per share	$ (0.03)	$

	Six months ended	
	June 1, 2007	June 2, 2006
Numerator:		
Net loss	$ (961,601)	$ (228,738)
Denominator:		
Basic weighted average common shares	18,590,506	18,409,257
Effect of dilutive stock options, warrants, and contingent acquisition related shares		
Denominator for diluted earnings (loss) per share	18,590,506	18,409,257
Basic and diluted earnings (loss) per share	$ (0.05)	$ (0.01)

Item 2.

Management s Discussion and Analysis of Financial Condition and Results of Operations.

You should read this section together with our condensed consolidated financial statements and related notes thereto included elsewhere in this report. In addition to the historical information contained herein, this report contains forward-looking statements that involve risks and uncertainties. Forward-looking statements are not based on historical information but relate to future operations, strategies, financial results or other developments. Forward-looking statements are necessarily based upon estimates and assumptions that are inherently subject to significant business, economic and com