ADA-ES INC
Form 10-Q
November 07, 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 September 30, 2007

or

¨ **TRANSITION REPORT PURSUANT TO 13 OR 15(d) OF THE EXCHANGE ACT OF 1934**
For the transition period from __________ to __________

Commission File Number: 000-50216

ADA-ES, INC.

(Exact name of registrant as specified in its charter)

Colorado	**84-1457385**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
8100 SouthPark Way, B, Littleton, Colorado	**80120**
(Address of principal executive offices)	**(Zip Code)**

(303) 734-1727

(Registrant s telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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 x Non-accelerated filer ¨

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

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS DURING THE PRECEDING

FIVE YEARS:

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes ¨ No ¨

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Class	Outstanding at November 2, 2007
Common Stock, no par value	**5,676,249**

PART I - FINANCIAL INFORMATION

Item 1. Condensed Financial Statements.

ADA-ES, Inc. and Subsidiaries

Condensed Consolidated Balance Sheets

(Amounts in thousands, except share data)

	September 30, 2007 (Unaudited)	December 31, 2006
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 14,389	$ 16,129
Trade receivables, net of allowance for doubtful accounts of $39 and $4, respectively	5,752	3,522
Investments in securities	2,080	2,427
Prepaid expenses and other	292	361
Total current assets	22,513	22,439
PROPERTY AND EQUIPMENT, at cost	2,557	1,830
Less accumulated depreciation and amortization	(1,264)	(1,033)
Net property and equipment	1,293	797
GOODWILL, net of $1,556 in amortization	2,024	2,024
INTANGIBLE ASSETS, net of $38 and $57, respectively, in amortization	248	241
INVESTMENTS IN SECURITIES	2,781	5,322
DEVELOPMENT PROJECTS AND OTHER ASSETS	6,309	931
TOTAL ASSETS	$ 35,168	$ 31,754
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 4,085	$ 2,352
Accrued payroll and related liabilities	681	618
Deferred revenue and other	1,777	922
Total current liabilities	6,543	3,892
LONG-TERM LIABILITIES:		
Deferred warranty and other	276	184
Total liabilities	6,819	4,076
MINORITY INTEREST	37	37
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS EQUITY:		
Preferred stock; 50,000,000 shares authorized, none outstanding		
Common stock; no par value, 50,000,000 shares authorized, 5,648,028 and 5,635,137 shares issued and outstanding	27,973	27,592
Accumulated other comprehensive income	210	167

Retained earnings (accumulated deficit)		129		(118)
Total stockholders equity		28,312		27,641
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$	35,168	$	31,754

See accompanying notes.

ADA-ES, Inc. and Subsidiaries

Condensed Consolidated Statements of Operations and Comprehensive Income

(*Amounts in thousands, except per share data*)

(Unaudited)

	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
Revenue:				
Mercury emission control	$ 5,144	$ 4,120	$ 13,382	$ 9,875
Flue gas conditioning and other	457	328	1,065	1,528
Total net revenues	5,601	4,448	14,447	11,403
Cost of Revenues:				
Mercury emission control	3,521	2,835	9,020	6,588
Flue gas conditioning and other	209	323	640	1,003
Total cost of revenues	3,730	3,158	9,660	7,591
Gross Margin	1,871	1,290	4,787	3,812
Other Costs and Expenses:				
General and administrative	1,419	974	4,075	2,736
Research and development	322	308	1,001	922
Depreciation and amortization	96	71	263	193
Total expenses	1,837	1,353	5,339	3,851
Operating Income (Loss)	34	(63)	(552)	(39)
Other Income:				
Minority interest in loss of consolidated subsidiary	34		129	
Other expense		(412)		(412)
Interest and other income	215	270	750	658
Total other income (expense)	249	(142)	879	246
Income (Loss) Before Tax	283	(205)	327	207
Provision for Tax Benefit (Expense)	(68)	77	(80)	(53)
Net Income (Loss)	215	(128)	247	154
Unrealized gains on Certain Investments in Debt and Equity Securities, net of tax	44	101	43	87
Comprehensive Income (Loss)	$ 259	$ (27)	$ 290	$ 241
Net Income (Loss) Per Common Share Basic and Diluted	$ 0.04	$ (0.02)	$ 0.04	$ 0.03
Weighted Average Common Shares Outstanding	5,642	5,627	5,641	5,622
Weighted Average Diluted Common Shares Outstanding	5,676	5,627	5,732	5,795

See accompanying notes.

ADA-ES, Inc. and Subsidiaries

Condensed Consolidated Statements of Changes in Stockholders Equity

Nine Months Ended September 30, 2007 and 2006

(Amounts in thousands)

(Unaudited)

	Common Stock		Accumulated Other Comprehensive	(Accumulated Deficit) Retained	
	Shares	Amount	Income	Earnings	Total
Balances, January 1, 2006	5,610	$ 26,318	$ 33	$ (495)	$ 25,856
Stock and stock options issued to consultant and directors for services	7	157			157
Stock-based compensation		249			249
Issuance of stock on exercise of options	10	81			81
Unrealized holding gains on investments			140		140
Income tax effect			(53)		(53)
Net income				154	154
Balances, September 30, 2006	5,627	$ 26,805	$ 120	$ (341)	$ 26,584
Balances, January 1, 2007	5,635	$ 27,592	$ 167	$ (118)	$ 27,641
Stock issued to consultant for services	2	20			20
Stock-based compensation		254			254
Issuance of stock on exercise of options	11	107			107
Unrealized holding gains on investments			69		69
Income tax effect			(26)		(26)
Net income				247	247
Balances, September 30, 2007	5,648	$ 27,973	$ 210	$ 129	$ 28,312

See accompanying notes.

ADA-ES, Inc. and Subsidiaries

Condensed Consolidated Statements of Cash Flows

(Amounts in thousands)

(Unaudited)

	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 247	$ 154
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	263	193
Loss on asset dispositions and securities	9	34
Deferred tax expense	80	53
Expenses paid with stock and stock options	274	406
Minority interest in loss of subsidiary	(129)	
Changes in operating assets and liabilities:		
Trade receivables, net	(2,230)	(86)
Prepaid expenses and other	69	(32)
Accounts payable	1,733	841
Deferred revenue and accrued expenses	836	(242)
Other liabilities	92	390
Net cash provided by operating activities	1,244	1,711
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures for equipment and other assets	(801)	(419)
Development project expenditures	(5,378)	(344)
Investment in securities	(2,970)	(5,485)
Proceeds from sale of securities and certificates of deposit	5,929	6,104
Net cash used in investing activities	(3,220)	(144)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payments on debt and notes payable		(4)
Minority interest capital contribution	129	
Exercise of stock options	107	81
Net cash provided by financing activities	236	77
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(1,740)	1,644
CASH AND CASH EQUIVALENTS, beginning of period	16,129	14,026
CASH AND CASH EQUIVALENTS, end of period	$ 14,389	$ 15,670
SUPPLEMENTAL SCHEDULE OF CASH FLOW INFORMATION:		
Cash payments for interest	$	$ 1
Cash payments for taxes	$ 219	$
SUPPLEMENTAL SCHEDULE OF NON-CASH FLOW FINANCING ACTIVITIES:		

Stock and stock options issued for services	$ 274	$ 406

See accompanying notes.

ADA-ES, Inc. and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Unaudited)

September 30, 2007

(1) Basis of Presentation

ADA-ES, Inc. (ADA), its wholly owned subsidiary, ADA Environmental Solutions, LLC (ADA LLC), Red River Environmental Products, LLC, Bowman Environmental Products, LLC and our 50% joint venture interest in Clean Coal Solutions, LLC (Clean Coal), collectively, are referred to as the Company. The Company is principally engaged in providing environmental technologies and specialty chemicals to the coal-burning utility industry. The Company generates a substantial part of its revenue from contracts co-funded by the government and industry. The Company s sales occur principally throughout the United States.

The accompanying condensed Balance Sheet as of December 31, 2006, was derived from audited financial statements and the unaudited interim condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial statements and with the instructions to Form 10-Q and Article 10 of Regulation S-X and, therefore, do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. The condensed consolidated financial statements include the financial statements of ADA, its subsidiaries and Clean Coal. We have eliminated all significant intercompany balances and transactions in consolidation.

In the opinion of management, the condensed consolidated financial statements include all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of the results of operations, financial position and cash flows for the interim periods presented. Operating results for the nine months ended September 30, 2007 are not necessarily indicative of the results that may be expected for the year ending December 31, 2007.

These statements should be read in conjunction with the consolidated financial statements and related notes to consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2006. Certain prior period amounts have been reclassified to be consistent with the current presentation. The accounting policies used in preparing these condensed consolidated financial statements are the same as those described in our Form 10-K.

We prepare our condensed consolidated financial statements in conformity with U.S. generally accepted accounting principles. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of sales and expenses during the reporting period. Actual results could differ from those estimates.

(2) Net Income Per Share

Basic net income per share is computed based on the weighted average common shares outstanding in the period. Diluted net income per share is computed based on the weighted average common shares outstanding in the period and the effect of dilutive securities (stock options and awards) except where the inclusion is anti-dilutive.

	Three Months Ended		**Nine Months Ended**	
	September 30,		**September 30,**	
	2007	**2006**	**2007**	**2006**
	(In thousands, except per share data)		***(In thousands, except per share data)***	
NET INCOME (LOSS):	$ 215	$ (128)	$ 247	$ 154
DETERMINATION OF SHARES:				
Average common shares outstanding	5,642	5,627	5,641	5,622
Incremental common shares issuable:				
Stock Options and awards	34		91	173

Diluted average common shares outstanding	5,676	5,627	5,732	5,795
Basic net income (loss) per common share	$ 0.04	$ (0.02)	$ 0.04	$ 0.03
Diluted net income (loss) per common share	$ 0.04	$ (0.02)	$ 0.04	$ 0.03

Stock options outstanding to purchase 146,550 and 19,900 shares of common stock for the three and nine months ended September 30, 2007, respectively, were excluded from the calculation of diluted shares because their effect would be anti-dilutive.

(3) Property and Equipment

Property and equipment consisted of the following at the dates indicated:

	Life in years	As of September 30, 2007	As of December 31, 2006
		(In thousands)	
Machinery and equipment	3-10	$ 1,823	$ 1,357
Leasehold improvements	3-7	506	326
Furniture and fixtures	3-7	228	147
		2,557	1,830
Less accumulated depreciation and amortization		(1,264)	(1,033)
Total property and equipment, net		$ 1,293	$ 797

Depreciation and amortization of property and equipment for the nine months ended September 30, 2007 and 2006 was $247,000 and $182,000, respectively.

(4) Stock Options and Equity

During 2003, the Company adopted the 2002 ADA-ES, Inc. Stock Option Plan, which was originally referred to as the 2002 Stock Option Plan (the 2003 Plan), and reserved 400,000 shares of Common Stock for issuance under the plan. In general, all options granted under the 2003 Plan expire ten years from the date of grant unless otherwise specified by the Company s Board of Directors. The exercise price of options was determined by the compensation committee of the board of directors at the time the option was granted of not less than 100% of the fair market value of a share of our Common Stock on the date the option is granted. During the first quarter of 2006, 19,900 options were granted under this plan. This plan was replaced by the 2007 Equity Incentive Plan described below, and as a result, 140,706 shares of Common Stock that were originally reserved for issuance upon exercise of options grantable under the 2003 Plan were removed from the 2003 Plan. As of September 30, 2007 and 2006, 9,550 and 6,557 options were exercisable, respectively.

During 2004, the Company adopted the 2004 Executive Stock Option Plan. This plan authorized the grant of up to 200,000 options to purchase shares of the Company s Common Stock to executive officers of the Company, all of which were granted in 2004. The option exercise price of $8.60 per share was the market price on the date of the grant. The options are exercisable over a 10-year period based on a vesting schedule that may be accelerated based on performance of the individual recipients as determined by the Board of Directors. In February 2007, the Board authorized vesting of 17,258 options under this plan with a fair value of $35,000. As of September 30, 2007 and 2006, 49,429 and 39,228 options were exercisable, respectively.

During 2004, the Company adopted a plan (the 2004 Plan) for the issuance of shares and the grant of options to purchase shares of the Company s Common Stock to the Company s non-management directors. The 2004 Plan provided for the award of stock of 603 shares per individual non-management director or 4,221 shares in total, and the grant of options to purchase 5,000 shares of common stock per individual non-management director, or 35,000 in total, all of which were formally granted and issued in 2005 after approval of the 2004 Plan by the shareholders. The option exercise price of $13.80 per share for the stock options granted on November 4, 2004 was the market price on the date of the grant. The options are exercisable over a period of five years and will vest over a three-year period, one-third each year for continued service on the Board. If such service is terminated, the non-vested portion of the option will be forfeited. During the second quarter of 2007, 4,015 were forfeited after the death of a director. As of September 30, 2007 and 2006, 8,333 and 6,668 options were vested and exercisable, respectively.

During 2005, the Company adopted the 2005 Directors Compensation Plan (the 2005 Plan), which authorized the issuance of shares of Common Stock and the grant of options to purchase shares of the Company s Common Stock to non-management directors. The 2005 Plan provides a portion of the annual compensation to non-management directors of the Company in the form of awards of shares of Common Stock and vesting of options to purchase Common Stock of the Company for services performed for the Company. Under the 2005 Plan, the award of stock is limited to not more than 1,000 shares per individual per year, and the grant of options is limited to 5,000 per individual in total. The aggregate number of shares of Common Stock reserved for issuance under the 2005 Plan totals 90,000 shares (50,000 in the form of stock awards and 40,000 in the form of options). The exercise price for options granted under the 2005 Plan will be the market price on the date of grant, the shares of Common Stock underlying the option will vest at a rate of no more than 1,667 shares per annual period per individual, and any unvested options that are outstanding at the date the individual is no longer a Director will be forfeited. The 2005 Plan, if not terminated earlier by the Board, will terminate ten years after the date of its adoption. As of September 30, 2007, 5,000 of the options were vested and exercisable.

Following is a table of options activity for the nine months ended September 30, 2007:

	Director & Employee Options	Non-Employee Options	Weighted Average Exercise Price
OPTIONS OUTSTANDING, January 1, 2007	344,969	80,000	$ 11.55
Granted			
Exercised	(11,396)		10.58
Expired	(4,015)	(21,000)	14.47
OPTIONS OUTSTANDING, September 30, 2007	329,558	59,000	$ 11.39
OPTIONS EXERCISABLE, September 30, 2007	177,749	59,000	$ 12.04

The aggregate intrinsic value of options exercisable at September 30, 2007 was $ 97,000 based on a market price of $12.45.

Stock options outstanding at September 30, 2007 are summarized in the table below:

	Options Outstanding		Options Exercisable		
Range of Exercise Prices	Number Outstanding	Weighted Average Exercise Price	Number Exercisable	Weighted Average Remaining Contractual Lives	Weighted Average Exercise Price
$2.80	11,665	$ 2.80	11,665	6.1	$ 2.80
$8.60 - $10.00	230,343	$ 8.90	113,109	6.7	$ 9.22
$13.80 - $15.25	103,250	$ 14.59	78,625	6.5	$ 14.49
$18.61 - $20.20	43,300	$ 19.34	33,350	8.1	$ 19.08
	388,558	$ 11.39	236,749	6.8	$ 12.04

No options were granted in the nine months ended September 30, 2007. The average fair value of each director and employee option granted in the nine months ended September 30, 2006 was approximately $5.52 and was estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions:

Expected volatility	55%
Risk-free interest rate	4.0%
Expected life of options (in years)	4.0
Expected dividends	

During 2007, the Company adopted the 2007 Equity Incentive Plan (the 2007 Plan), which replaces the 2003 Plan. The 2007 Plan authorizes the issuance to employees, directors and consultants of up to 600,000 shares of Common Stock, either as restricted stock grants or to underlie options to purchase shares of the Company s Common Stock. Under the 2007 Plan, the award of stock is limited to not more than 30,000 shares per individual per year with a maximum of 10,000 shares grantable in any year to non-management Directors. In general, all options granted under the 2007 Plan will expire ten years from the date of grant unless otherwise specified by the Company s Board of Directors. The exercise price for options granted under the 2007 Plan will be the market price on the date of grant and the shares of Common Stock underlying the option will vest on the passage of specified times following the date of grant, the occurrence of one of more events, the satisfaction of performance criteria or other conditions specified by the Company s Board of Directors. As of September 30, 2007, no options have been granted under the 2007 Plan.

On September 26, 2007, the Board of Directors awarded restricted stock under the 2007 Plan. All non-executive employees and certain officers were entitled to an award of restricted stock under the following conditions (1) employees that had not received stock options upon commencement of employment received a restricted stock award equal based on a percentage of their starting salaries, (2) employees that had received stock options upon commencement of employment had the option to exchange any remaining stock options outstanding for a restricted stock award based on their starting salary, and (3) employees with five or more years of service received a restricted stock award based on a percent of their current annual salary. The purchase price for restricted stock was $0.01 per share and the restricted stock vests over a five year period on an annual basis. The stock based compensation related to the restricted stock awards was determined using the fair value of the Company s stock on the date of grant, which was $12.60. In October 2007, seven employees opted to exchange 42,700 outstanding options for 3,389 shares of restricted stock. The exchange did not result in any stock option modification costs. Unvested shares of restricted stock are subject to forfeiture upon termination of employment with the Company. A total of 20,177 shares were granted with 313 shares vesting immediately. The total fair value of the grant was $212,000. For the nine months ended September 30, 2007, the Company recognized $4,000 of compensation expense relate to the vesting of restricted stock.

A summary of the status of the non-vested shares as of September 30, 2007, is presented below:

Non-vested Shares	**Shares**	**Weighted Average Grant Date Fair Value**
Non-vested at January 1, 2007		$
Granted	20,177	12.60
Vested	(313)	12.60
Forfeited		
Non-vested at September 30, 2007	19,864	$ 12.60

As of September 30, 2007, there was $438,000 of total unrecognized cost related to non-vested share-based compensation arrangements granted under the Company s equity incentive plans. This cost is expected to be recognized over 5.25 years. The total fair value of shares underlying stock options which vested during the nine months ended September 30, 2007 and 2006 was $209,000 and $215,000, respectively.

(5) <u>Capitalized Development Costs</u>

We are capitalizing all direct and identifiable incremental costs associated with our development efforts to build activated carbon facilities. As of September 30, 2007, such costs totaled $6.2 million, and are included in Development Projects and Other Assets on the accompanying condensed consolidated balance sheets. Such development costs are generally deferred and either (a) expensed when it has been determined they are no longer of future value, or (b) capitalized as part of long-term assets.

(6) <u>Commitments and Contingencies</u>

Under certain contracts to supply activated carbon injection systems, the Company may grant performance guarantees to the owner of the power plants that guarantee the performance of the associated equipment for a specified period. The Company may also guarantee the achievement of a certain level of mercury removal based upon the injection of a specified quantity of a qualified activated carbon at a specified rate given other plant operating conditions. In the event the equipment fails to perform as specified, the Company is obligated to correct or replace the equipment. In the event the level of mercury removal is not achieved, the Company has a make right obligation within the contract limits. The Company assesses the risks inherent in each applicable contract and accrues an estimate that is based on costs incurred over the performance period of the contract. In some cases a performance bond may be purchased and held for the period of the warranty that can be used to satisfy the obligation. No warranty claims have been made to date. Any warranty costs paid out in the future will be charged against the accrual. The adequacy of warranty accrual balances is assessed at least quarterly based on current facts and circumstances and adjustments are made as needed. As of September 30, 2007 and December 31, 2006, the accrual balances for such equipment warranties and performance guarantees were $232,000 and $120,000, respectively, and are included in deferred warranty and other liabilities in the accompanying balance sheets.

At September 30, 2007, the Company had a standby letter of credit for $40,000 related to a proposal for an ACI System. This commitment was not recorded on the Company s consolidated balance sheet as the Company does not expect the funds to be called upon under the letter of credit.

(7) Business Segment Information

The following information relates to the Company s two reportable segments: Mercury emission control (MEC) and Flue gas conditioning and other (FGC). All assets are located in the U.S. and are not evaluated by management on a segment basis. All significant customers are U.S. companies.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
	(In thousands)		(In thousands)	
REVENUE:				
MEC	$ 5,144	$ 4,120	$ 13,382	$ 9,875
FGC	457	328	1,065	1,528
Total	$ 5,601	$ 4,448	$ 14,447	$ 11,403
SEGMENT PROFIT:				
MEC	$ 1,207	$ 889	$ 3,106	$ 2,094
FGC	397	(93)	307	287
Total	$ 1,604	$ 796	$ 3,413	$ 2,381

A reconciliation of the reported total segment profit to net income for the periods shown above is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
	(In thousands)		(In thousands)	
Total segment profit	$ 1,604	$ 796	$ 3,413	$ 2,381
Non-allocated general and administrative expenses	(1,474)	(788)	(3,702)	(2,227)
Depreciation and amortization	(96)	(71)	(263)	(193)
Interest, other income (expense) and deferred income tax provision	181	(65)	799	193
Net income (loss)	$ 215	$ (128)	$ 247	$ 154

Non-allocated general and administrative expenses include costs that benefit the business as a whole and are not directly related to one of our segments. Such costs include but are not limited to accounting and human resources staff, information systems costs, facility costs, legal and audit fees and corporate governance expenses.

(8) Recently Issued Accounting Pronouncements

In June 2006, the FASB issued FIN 48, Accounting for Uncertainty in Income Taxes - An Interpretation of FASB Statement No. 109 (FIN 48) This interpretation was issued to clarify the accounting for uncertainty in income taxes recognized in the financial statements by prescribing a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 requires the recognition of penalties and interest on any unrecognized tax benefits. Our policy is to reflect penalties and interest related to FIN 48 issues as part of income tax expense as they become applicable. We adopted the provisions of FIN 48 on January 1, 2007. No unrecognized tax benefits were recorded as of the date of adoption. The Company files income tax returns in the U.S. federal and various state jurisdictions. We are no longer subject to U.S. federal and state and local examinations by tax authorities for years before 2004.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurement (SFAS 157), which defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. SFAS 157 focuses on creating consistency and comparability in fair value measurements. SFAS 157 is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We are evaluating its impact and do not expect that adoption of SFAS 157 will have a material impact on our financial statements.

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities. SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The provisions of SFAS 159 will be effective beginning January 1, 2008. We are in the process of determining the effect, if any, the adoption of SFAS 159 will have on our financial statements.

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations.

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, regarding future events and our anticipated future results, which are based on current expectations, estimates, forecasts, and projections about the industries in which we operate and the beliefs and assumptions of our management. Actual results may vary materially from such expectations. The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the audited consolidated financial statements and related notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2006.

Words or phrases such as will, hope, expect, anticipate, intend, plan, the negative expressions of such words, or similar expressions gener identify the forward-looking statements in this Report, and such forward-looking statements include, but are not limited to, statements or expectations regarding (a) the impact of national and state mercury control regulations on the nation s 1,100-plus coal-fired units, (b) capability of U.S. coal reserves to serve demand for the next 250 years, (c) future estimated costs to control mercury emissions, (d) the rapid development of the mercury emission control market, (e) amounts and timing of and changes in future revenues, research and development expenses, (f) costs of operating Clean Coal Solutions, LLC, (Clean Coal), (g) annual lease costs and other expenditures and gross margins, (h) our ability to meet contract delivery milestones, (i) the market and market potential (size) for Refined Coal and ADA-249M, (j) timing of completion of projects and future demonstrations, (k) our ability to qualify our Refined Coal products for Section 45 Tax Credits under applicable tax laws, (l) expected future bid requests and procession of outstanding bid requests for orders between now and 2010, (m) the range of costs for capital equipment expected to be required by each coal-fired unit and the range of sorbent requirements per unit, (n) the inability of the supply of activated carbon to meet market demand as early as 2010, (o) potential costs for development of a Greenfield activated carbon facility, (p) appropriation of funds by Congress for DOE projects, (q) immateriality of any future adjustments due to DOE audits, (r) our a