

RETRACTABLE TECHNOLOGIES INC
Form 10QSB
August 14, 2003
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-QSB

(Mark One)

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2003

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT

For the transition period from _____ to _____

Commission file number 000-30885

Retractable Technologies, Inc.

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

Texas

(State or other jurisdiction of
incorporation or organization)

75-2599762

(IRS Employer
Identification No.)

511 Lobo Lane

Edgar Filing: RETRACTABLE TECHNOLOGIES INC - Form 10QSB

Little Elm, Texas 75068-0009

(Address of principal executive offices)

(972) 294-1010

(Issuer's telephone number)

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

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

APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY

PROCEEDINGS DURING THE PRECEDING FIVE YEARS

Check whether the registrant filed all documents and reports required to be filed by Section 12, 13, or 15(d) of the Exchange Act after the distribution of securities under a plan confirmed by a court. Yes No

APPLICABLE ONLY TO CORPORATE ISSUERS

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: 21,435,314 shares of Common Stock, no par value, issued and outstanding on August 7, 2003.

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

Table of Contents

TABLE OF CONTENTS

PART I	FINANCIAL INFORMATION	
Item 1.	Financial Statements.	
	<u>CONDENSED BALANCE SHEETS</u>	3
	<u>CONDENSED STATEMENTS OF OPERATIONS</u>	4
	<u>CONDENSED STATEMENTS OF CASH FLOWS</u>	5
	<u>NOTES TO CONDENSED FINANCIAL STATEMENTS</u>	6
Item 2.	<u>Management's Discussion and Analysis or Plan of Operation.</u>	11
Item 3.	<u>Controls and Procedures.</u>	16
PART II	OTHER INFORMATION	
Item 1.	<u>Legal Proceedings.</u>	16
Item 2.	<u>Changes in Securities.</u>	16
Item 3.	<u>Defaults Upon Senior Securities.</u>	17
Item 5.	<u>Other Information.</u>	17
Item 6.	<u>Exhibits and Reports on Form 8-K.</u>	17
<u>SIGNATURES</u>		18

Table of Contents

PART I
FINANCIAL INFORMATION

Item 1. Financial Statements.

RETRACTABLE TECHNOLOGIES, INC.

CONDENSED BALANCE SHEETS

	<u>June 30, 2003</u>	<u>December 31, 2002</u>
	(unaudited)	
ASSETS		
Cash and cash equivalents	\$ 9,302,591	\$ 1,342,117
Accounts receivable, net	2,670,818	2,666,866
Inventories, net	4,142,827	2,779,554
Other current assets	246,843	276,524
	<u>16,363,079</u>	<u>7,065,061</u>
Total current assets	16,363,079	7,065,061
Property, plant, and equipment, net	10,071,659	10,515,480
Intangible assets, net	421,345	405,641
Other assets	40,710	72,671
	<u>26,896,793</u>	<u>18,058,853</u>
Total assets	\$ 26,896,793	\$ 18,058,853
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities:		
Accounts payable	\$ 3,132,463	\$ 4,229,396
Current portion of long-term debt	180,997	840,899
Accrued compensation	379,382	328,717
Marketing fees payable	1,735,133	1,874,571
Accrued royalties	276,529	602,777
Other accrued liabilities	121,546	145,116
	<u>5,826,050</u>	<u>8,021,476</u>
Total current liabilities	5,826,050	8,021,476
Long-term debt, net of current maturities	3,019,640	2,600,298
	<u>3,019,640</u>	<u>2,600,298</u>
Stockholders' equity		
Preferred stock \$1 par value		
Series A		1,056,000
Series I, Class B	249,400	259,400
Series II, Class B	418,500	431,000
Series III, Class B	147,745	150,745
Series IV, Class B	1,066,000	1,066,000
Series V, Class B	2,416,221	2,416,221
Common Stock, no par value		

Edgar Filing: RETRACTABLE TECHNOLOGIES INC - Form 10QSB

Additional paid-in capital	50,149,128	49,411,177
Accumulated deficit	(36,395,891)	(47,353,464)
	<hr/>	<hr/>
Total stockholders' equity	18,051,103	7,437,079
	<hr/>	<hr/>
Total liabilities and stockholders' equity	\$ 26,896,793	\$ 18,058,853
	<hr/>	<hr/>

See accompanying notes to the condensed financial statements.

Table of Contents**RETRACTABLE TECHNOLOGIES, INC.****CONDENSED STATEMENTS OF OPERATIONS****(unaudited)**

	Three	Three		
	Months	Months	Six Months	Six Months
	ended	ended	ended	ended
	June 30, 2003	June 30, 2002	June 30, 2003	June 30, 2002
Sales, net	\$ 4,437,600	\$ 4,867,634	\$ 8,915,308	\$ 8,983,997
Cost of sales	3,538,758	3,856,649	6,351,193	6,530,118
Product recall and recovery		481,637		481,637
Gross profit	898,842	529,348	2,564,115	1,972,242
Operating expenses:				
Sales and marketing	1,140,856	987,330	2,153,389	1,933,093
Research and development	157,436	71,071	260,230	164,572
General and administrative	1,789,654	885,948	2,920,392	1,999,227
Debt conversion expense		2,319,073		2,319,073
Total operating expenses	3,087,946	4,263,422	5,334,011	6,415,965
Loss from operations	(2,189,104)	(3,734,074)	(2,769,896)	(4,443,723)
Interest income	12,449	1,888	14,952	4,777
Interest expense	(88,042)	(139,219)	(166,994)	(301,760)
Litigation settlement, net	13,879,511		13,879,511	
Net income (loss)	11,614,814	(3,871,405)	10,957,573	(4,740,706)
Preferred stock dividend requirements	(660,246)	(498,434)	(1,326,769)	(977,163)
Net income (loss) applicable to common shareholders	\$ 10,954,568	\$ (4,369,839)	\$ 9,630,804	\$ (5,717,869)
Net income (loss) per share basic	\$ 0.53	\$ (0.22)	\$ 0.47	\$ (0.28)
Net income (loss) per share fully diluted	\$ 0.43	\$ (0.22)	\$ 0.41	\$ (0.28)
Weighted average common shares outstanding	20,516,683	20,303,433	20,419,892	20,286,350

See accompanying notes to the condensed financial statements.

Table of Contents**RETRACTABLE TECHNOLOGIES, INC.****CONDENSED STATEMENTS OF CASH FLOWS****(unaudited)**

	Six Months ended June 30, 2003	Six Months ended June 30, 2002
Cash flows from operating activities		
Net income (loss)	\$ 10,957,573	\$ (4,740,706)
Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities:		
Depreciation and amortization	658,546	726,797
Capitalized interest	(13,689)	(12,732)
Stock option compensation	115,538	
Provision for doubtful accounts	45,107	
Accreted interest	50,560	
Waiver of vacation pay		(100,936)
Debt conversion expense		2,319,073
Changes in assets and liabilities		
(Increase) decrease in inventories	(1,363,272)	(8,183)
(Increase) decrease in accounts receivable	(49,059)	(1,581,737)
(Increase) decrease in other current assets	43,696	(52,882)
Increase (decrease) in accounts payable	(1,096,933)	1,685,198
Increase (decrease) in marketing fees payable	(139,438)	(187,352)
Increase (decrease) in other accrued liabilities	(299,151)	389,111
Net cash provided (used) by operating activities	<u>8,909,478</u>	<u>(1,564,349)</u>
Cash flows from investing activities		
Purchase of property, plant, and equipment	(157,818)	(57,052)
Acquisition of patents, trademarks, licenses and intangibles	(24,713)	(2,372)
Net cash used by investing activities	<u>(182,531)</u>	<u>(59,424)</u>
Cash flows from financing activities		
Repayments of long-term debt and notes payable	(307,385)	(301,899)
Proceeds from the sale of preferred stock		1,554,600
Payment of dividends on Series A Convertible Preferred Stock	(459,088)	
Offering expense for Series V stock		(28,938)
Net cash provided (used) by financing activities	<u>(766,473)</u>	<u>1,223,763</u>
Net increase (decrease) in cash	7,960,474	(400,010)
Cash and cash equivalents at:		
Beginning of period	<u>1,342,117</u>	<u>1,220,244</u>
End of period	<u>\$ 9,302,591</u>	<u>\$ 820,234</u>

Edgar Filing: RETRACTABLE TECHNOLOGIES INC - Form 10QSB

Supplemental schedule of cash flow information:		
Interest paid	\$ 181,313	\$ 293,518
Supplemental schedule of noncash financing activities:		
Debt assumed to acquire assets	\$ 16,294	
Forgiveness of royalties by an officer	\$	\$ 1,500,000
Conversion of accounts payable into preferred stock	\$	\$ 1,500,000
Conversion of long-term debt into preferred stock	\$	\$ 3,679,284

See accompanying notes to the condensed financial statements.

Table of Contents

RETRACTABLE TECHNOLOGIES, INC.

NOTES TO CONDENSED FINANCIAL STATEMENTS

(unaudited)

1. BUSINESS OF THE COMPANY, BASIS OF PRESENTATION, AND RECENT DEVELOPMENTS

Business of the Company

Retractable Technologies, Inc. (the Company) was incorporated in Texas on May 9, 1994, to design, develop, manufacture, and market safety syringes and other safety medical products for the healthcare profession. The Company began to develop its manufacturing operations in 1995. The Company's manufacturing and administrative facilities are located in Little Elm, Texas. The Company's primary products are the VanishPoint® syringe in 1cc, 3cc, 5cc, and 10cc sizes and blood collection tube holders. The Company has conducted clinical evaluations and worked with national distributors to encourage healthcare facilities to transition from the use of standard syringes to the VanishPoint® syringe. Preliminary shipments, which commenced in February 1997, included syringes for hospital product evaluations as well as for sale in clinics and other healthcare settings.

Basis of presentation

The accompanying condensed financial statements are unaudited and, in the opinion of management, reflect all adjustments that are necessary for a fair presentation of the financial position and results of operations for the periods presented. All of such adjustments are of a normal and recurring nature. The results of operations for the periods presented are not necessarily indicative of the results to be expected for the entire year. The condensed financial statements should be read in conjunction with the financial statement disclosures contained in the Company's audited financial statements for the year ended December 31, 2002.

Recent developments

During the second quarter of 2003, the Company called for redemption of the remaining 1,021,000 shares of Series A Convertible Preferred Stock (Series A Stock) as provided in the certificate of designation. The certificate of designation also provides that the shareholder had the option to convert each share of Series A Stock into one share of the Company's Common Stock. All of the Series A Stock was converted into Common Stock of the Company. The Company also paid all accumulated dividends on the Series A Stock, which amounted to approximately \$460,000. On an annual basis, this transaction reduced the Company's preferred dividend requirement by \$122,520.

In the second quarter the Company reached settlement agreements with Premier Inc.; Premier Purchasing Partners, L.P.; VHA, Inc.; Novation, L.L.C.; Tyco International (US) Inc. and Tyco Healthcare Group L.P. in its federal antitrust lawsuit, Retractable Technologies, Inc. v. Becton Dickinson & Co. et al. As part of the settlements, the litigation against Premier, VHA, Novation, and Tyco has been dismissed.

Edgar Filing: RETRACTABLE TECHNOLOGIES INC - Form 10QSB

Although specific terms are confidential, the agreements include cash payments and other financial consideration as well as provisions that are intended to facilitate the sale of Retractable's VanishPoint® products to Premier and Novation member facilities. The financial terms were made on terms that Retractable considers favorable. The initial payment amount received by the Company is net of court costs, legal expenses, attorneys' fees and reserve funds set aside for future legal expenses. The Company received \$14,608,120 as the initial payment under the financial terms of these settlement agreements.

In exchange for the settlement provisions, Retractable has agreed to give up its claims against these companies. Other consideration provided through these settlement agreements will be disclosed periodically as required by SEC rules and regulations.

Pursuant to a Covenant Not to Sue agreement entered into on September 19, 2001, between the Company and Thomas J. Shaw, individually, Mr. Shaw has received \$728,609 of the initial payment proceeds to the Company under the settlement agreements. Under the terms of the Covenant Not to Sue, Mr. Shaw, as the licensor of the

Table of Contents

retractable technology manufactured by Retractable, agreed not to pursue claims for damages that he could pursue as an individual against the defendants in the antitrust litigation, Retractable Technologies, Inc. v. Becton Dickinson & Co. et al Cause No. 5:01-CV-036, in exchange for a percentage of any recovery obtained by Retractable in the lawsuit, net of court costs, litigation expenses and attorney's fees.

These agreements leave Becton Dickinson & Co. (B-D), the dominant U.S. maker of syringes and other needle products, as the sole remaining defendant in the case, which is currently scheduled for trial on February 3, 2004, in federal court in Texarkana, Texas. Among other allegations, Retractable asserts in the lawsuit that B-D has acquired and maintained monopoly power among hospitals and healthcare providers to eliminate or lessen competition.

On July 15, 2003, Katie Petroleum converted the remaining balance of \$250,003 of its note secured by land and building into 35,714 shares of Common Stock of the Company.

The Company has agreed to a loan proposal from 1st International Bank for \$2,500,000. The proceeds from the loan will be used to pay off the remaining \$475,000 of the revolving credit agreement and fund a new warehouse and related infrastructure. Payments on the new note will be interest only during construction. Upon completion, payments will be based on a twenty-year amortization with a five-year maturity. The exact terms will be based on the amount of funds kept on deposit with the bank. Accordingly, interest will vary from the Wall Street Journal Prime Rate (WSJPR) to the WSJPR plus 1 percent, with floors that may range from 4.25 percent to 6.50 percent. Compensating balances at 1 International affecting the interest rate will range from \$0 to \$500,000.

2. LIQUIDITY

The Company has been successful in raising funds through private equity financing totaling approximately \$52.6 million, including approximately \$5.2 million in conversion of debt and accounts payable, over the last seven and one-half years. However, the Company has incurred substantial losses and negative cash flows from operations in every fiscal period since inception. For the years ended December 31, 2002, 2001, and 2000, the Company incurred a loss from operations of approximately \$6.4 million, \$6.7 million, and \$10.4 million, respectively. For the six months ended June 30, 2003, the Company incurred a loss from operations of approximately \$2,189,104. For the years ended December 31, 2002, 2001, and 2000, the Company had negative cash flows from operating activities of approximately \$1.5 million, \$3.7 million, and \$8.6 million, respectively. For the six months ended June 30, 2003, the Company had cash flows from operating activities of \$8,909,478. As of June 30, 2003, and December 31, 2002, and 2001, the Company had accumulated deficits of approximately \$36.4 million, \$47.4 million, and \$40.5 million, respectively.

For the six months ended June 30, 2003, the Company had one distributor which accounted for more than 10 percent of our sales. Management expects to reach a break-even operating point when the Company has more access to the market. Management believes that the settlement agreements discussed in Note 1 will provide sufficient funds for our current needs and facilitate the sale of the Company's products.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Accounting estimates

Edgar Filing: RETRACTABLE TECHNOLOGIES INC - Form 10QSB

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management 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 revenues and expenses during the reporting period. Actual results could differ significantly from those estimates.

Cash and cash equivalents

For purposes of reporting cash flows, cash and cash equivalents include unrestricted cash and investments with original maturities of three months or less.

Table of Contents**Accounts receivable**

The Company records trade receivables when revenue is recognized. No product has been consigned to customers. The Company's allowance for doubtful accounts is primarily determined by review of specific trade receivables. Those accounts that are doubtful of collection are included in the allowance. An additional allowance has been established based on a percentage of receivables outstanding. These provisions are reviewed to determine the adequacy of the allowance for doubtful accounts. Trade receivables are charged off when there is certainty as to their being uncollectible. Trade receivables are considered delinquent when payment has not been made within contract terms.

Inventories

Inventories are valued at the lower of cost or market, with cost being determined using a standard cost method, which approximates average cost. Provision is made for any excess or obsolete inventories.

Property, plant, and equipment

Property, plant, and equipment are stated at cost. Expenditures for maintenance and repairs are charged to operations as incurred. Cost includes major expenditures for improvements and replacements which extend useful lives or increase capacity and interest cost associated with significant capital additions. For the six months ended June 30, 2003, and 2002, the Company capitalized interest of \$13,689 and \$12,732, respectively. Gains or losses from property disposals are included in income.

Depreciation and amortization are calculated using the straight-line method over the following useful lives:

Production equipment	3 to 13 years
Office furniture and equipment	3 to 10 years
Building	39 years
Building improvements	15 years
Automobiles	7 years

Long-lived assets

When events or changes in circumstances indicate that the carrying amount of long-lived assets may not be recoverable, the Company will review the net realizable value of the long-lived assets through an assessment of the estimated future cash flows related to such assets. In the event that assets are found to be carried at amounts which are in excess of estimated gross future cash flows, the assets will be adjusted for impairment to a level commensurate with a discounted cash flow analysis of the underlying assets.

Reclassifications

Certain prior period amounts have been reclassified to conform with the current period's presentation.

Intangible assets

Intangible assets are stated at cost and consist primarily of patents, a license agreement granting exclusive rights to use patented technology, and trademarks which are amortized using the straight-line method over 17 years.

Financial instruments

The fair market value of financial instruments is determined by reference to various market data and other valuation techniques as appropriate. The Company believes that the fair value of financial instruments approximate their recorded values.

Table of Contents

Concentrations of credit risk

The Company's financial instruments exposed to concentrations of credit risk consist primarily of cash, cash equivalents, and accounts receivable. Cash balances, which may exceed the federally insured limits, are maintained in financial institutions; however, management believes the institutions are of high credit quality. The majority of accounts receivable are due from companies which are well-established entities. As a consequence, management considers any exposure from concentrations of credit risks to be limited. The Company has a high concentration of sales with one significant customer. Net sales to this customer were \$4,605,750 and \$4,617,900 for the six months ended June 30, 2003, and 2002, respectively. For the six months ended June 30, 2003, and June 30, 2002, net sales to this customer accounted for 51.7 percent and 51.4 percent of net sales, respectively.

Revenue recognition

Revenue is recognized for sales to distributors when title and risk of ownership passes to the distributor, generally upon shipment. Revenue is recorded on the basis of sales price to distributors. Revenues on sales to distributors are recorded net of contractual pricing allowances. Revenue for shipments directly to end-users is recognized when title and risk of ownership passes from the Company. Any product shipped or distributed for evaluation purposes is expensed.

Marketing fees

The Company pays certain distributors marketing fees for services provided by distributors. These services include participation in promotional activities, development of educational and promotional materials, representation at trade shows, clinical demonstrations, inservicing and training, and tracking reports detailing the placement of the Company's products to end-users. Marketing fees are accrued at the time of the sale of product to the distributor. These fees are paid after the distributor provides the Company a tracking report of product sales to end-users. These costs are included in sales and marketing expense in the Condensed Statements of Operations.

Income taxes

The Company provides for deferred income taxes in accordance with Statement of Financial Accounting Standard No. 109, *Accounting for Income Taxes* (SFAS 109). SFAS 109 requires an asset and liability approach for financial accounting and reporting for income taxes based on the tax effects of differences between the financial statement and tax bases of assets and liabilities, based on enacted rates expected to be in effect when such basis differences reverse in future periods. Deferred tax assets are periodically reviewed for reliability. Valuation allowances are recorded when realizability of deferred tax assets is not likely.

Earnings per share

The Company has adopted Statement of Financial Accounting Standards No. 128, *Earnings Per Share*, which establishes standards for computing and presenting earnings per share. Basic earnings per share are computed by dividing net earnings for the period (adjusted for any

Edgar Filing: RETRACTABLE TECHNOLOGIES INC - Form 10QSB

cumulative preferred dividends for the period) by the weighted average number of common shares outstanding during the period. The weighted average number of shares outstanding was 20,419,892 and 20,286,350 for the six months ended June 30, 2003, and 2002, respectively. The Company's potentially dilutive Common Stock equivalents, including warrants, options, and convertible debt, are all dilutive for the current year periods and antidilutive for the prior year periods as the Company was in a loss position. Accordingly, basic loss per share is equal to diluted loss per share and is presented on the same line for income statement presentation. Cumulative preferred dividends of \$660,246 and \$498,434 have been added to net earnings (losses) for the quarters ended June 30, 2003 and 2002, respectively, to arrive at net earnings (loss) per share. Cumulative preferred dividends of \$1,326,769 and \$977,163 have been added to net earnings (losses) for the six months ended June 30, 2003, and 2002, respectively.

Research and development costs

Research and development costs are expensed as incurred.

Table of Contents**Stock-based compensation**

The Company has three stock-based director, officer, and employee compensation plans. Prior to 2002, the Company accounted for those plans under the recognition and measurement provisions (intrinsic value method) of APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and related Interpretations. Effective January 1, 2002, the Company adopted the fair value recognition provisions of SFAS No. 123, *Accounting for Stock-Based Compensation*, prospectively to all director, officer, and employee awards granted, modified, or settled after December 31, 2001. Awards under the Company's plans vest over periods up to three years. Therefore, the cost related to stock-based compensation included in the determination of net income after December 31, 2001, is less than what would have been recognized if the fair value method had been applied to all awards since the original effective date of SFAS No. 123. SFAS No. 123 indicates that the fair value method is the preferable method of accounting. The following table indicates the effect on net income and earnings per share if the fair value method had been applied to all outstanding and unvested awards in each period.

	Six Months Ended June 30, 2003	
	2003	2002
Net income (loss), as reported	\$ 10,957,573	\$ (4,740,706)
Add: Stock-based employee compensation		
expense included in reported net income,		
net of related tax effects	115,538	0
Deduct: Total stock-based employee		
compensation expense determined		
fair value based method for all awards,		
net of related tax effects	(188,193)	(77,645)
Pro forma net income	\$ 10,884,918	\$ (4,818,351)
Earnings (loss) per share (basic)-as reported	\$0.47	\$(0.28)
Earnings (loss) per share (fully diluted)-as reported	\$0.41	\$(0.28)
Earnings (loss) per share (basic)-pro forma	\$0.47	\$(0.28)
Earnings (loss) per share (fully diluted)-pro forma	\$0.40	\$(0.28)

Recent pronouncements

There are no recent accounting pronouncements that are expected to have a material impact on the Company.

Table of Contents

Item 2. Management's Discussion and Analysis or Plan of Operation.

FORWARD-LOOKING STATEMENT WARNING

Certain statements included by reference in this Form 10-QSB containing the words believes, anticipates, intends, expects, and similar such words constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act. Any forward-looking statements involve known and unknown risks, uncertainties, and other factors that may cause actual results, performance, or achievements of the Company to be materially different from any future results, performance, or achievements expressed or implied by such forward-looking statements. Such factors include, among others, the impact of dramatic increases in demand, our ability to quickly increase our capacity in the event of a dramatic increase in demand, our ability to access the market, our ability to successfully resolve our litigation with B-D, among others, our ability to continue to finance research and development as well as operations and expansion of production, and the recently increased interest of larger market players, specifically B-D, in providing safety needle devices. Given these uncertainties, undue reliance should not be placed on forward-looking statements.

The following discussion contains trend information and other forward-looking statements that involve a number of risks and uncertainties. Our actual future results could differ materially from our historical results of operations and those discussed in the forward-looking statements. Variances have been rounded for ease of reading. All period references are to the periods ended June 30, 2003, or June 30, 2002.

Comparison of Three Months Ended

June 30, 2003, and June 30, 2002

Net sales were \$4,437,600 and \$4,867,634 for the three months ended June 30, 2003 and 2002, respectively. The decrease of \$430,034 was due to a decrease in sales of 3cc, 5cc, and 10cc syringes and blood collection tube holders mitigated by an increase in sales of 1cc syringes. Sales to Abbott as a percentage of units sold decreased from 45.9 percent to 42.7 percent of total units sold. Unit sales to other distributors increased from 54.1 percent to 57.3 percent of units sold. Sales revenues from Abbott decreased about 15.4 percent whereas sales revenues to other distributors decreased 2.1 percent. No other distributor accounted for more than 10 percent of units sold.

Cost of sales decreased from \$3,856,649 in 2002 to \$3,538,758 in 2003, a decrease of \$317,891 or 8.2 percent. The decrease is due to reduced costs of manufacturing due to lower volumes and more efficient production. Bonuses were paid to the production and manufacturing employees in the amount of \$258,000.

The Company recorded an expense of \$481,637 in the second quarter of 2002 related to a recall and recovery of certain lots of its blood collection tube holders. The Company found that, in limited lots, upon testing, some blood collection tube holders retracted prior to activation. The premature retraction occurred during use as well as during shipping and handling. The Company has addressed the premature retraction through the manufacturing and design process.

Gross profit increased from \$529,348 in 2002 to \$898,842 in 2003, an increase of \$369,494. Gross profit as a percentage of net sales was 10.9 percent and 20.3 percent for the three months ended June 30, 2002, and 2003, respectively.

Edgar Filing: RETRACTABLE TECHNOLOGIES INC - Form 10QSB

Sales and marketing expense increased from \$987,330 in 2002 to \$1,140,856 in 2003, an increase of \$153,526 or 15.5 percent. The increase is principally due to bonuses of approximately \$100,000 and increased travel and entertainment.

Research and development costs increased from \$71,071 in 2002 to \$157,436 in 2003, an increase of \$86,365. The increase is principally due to increased labor costs of \$20,000 and bonuses of \$25,000. Research and experimental parts increased \$35,000.

Table of Contents

General and administrative costs increased from \$885,948 in 2002 to \$1,789,654 in 2003, an increase of \$903,706. Increases in wages were \$100,000, bonuses were \$240,000, legal expenses increased \$225,000 due principally to the NMT litigation, travel and entertainment increased \$95,000, and stock option expense for 2003 was \$115,000.

Debt conversion expense incurred in 2002 consists of \$1,821,246 for Series V Stock issued in excess of the original conversion term of the real estate note and working capital loan, \$440,000 for stock options issued in connection with the conversion, and \$57,827 of unamortized debt expenses.

Net interest expense declined from \$137,331 to \$75,593 due principally to the conversion of the Katie Petroleum note into Series V stock of the Company and higher invested cash balances.

Preferred stock dividend requirements were \$660,246 for 2003 compared to \$498,434 in 2002, an increase of \$161,812. The increase is due to an increase in the outstanding preferred stock as a result of sales of Series V Stock. Future dividend requirements will be reduced by approximately 30,000 for each quarter due to the conversion of the outstanding Series A stock.

Basic earnings (loss) per share was \$(0.22) per share in 2002 and \$0.53 in 2003 due principally to the settlements reached in litigation offset by the loss from operations. Fully diluted earnings per share were \$0.43 in 2003 assuming the conversion of debt securities, conversion of preferred stock, and exercise of dilutive stock options.

Comparison of Six Months Ended

June 30, 2003, and June 30, 2002

Net sales were \$8,915,308 and \$8,983,997 for the six months ended June 30, 2003 and 2002, respectively. The decrease of \$68,689 was due to a decrease in sales of 3cc, 5cc, and 10cc syringes and blood collection tube holders offset by an increase in sales of 1cc syringes. Sales to Abbott as a percentage of units sold decreased from 48.4 percent to 47.2 percent of total units sold. Unit sales to other distributors increased from 51.6 percent to 52.8 percent of units sold. Sales revenues from Abbott decreased about .03 percent whereas sales revenues to other distributors decreased 1.3 percent. No other distributor accounted for more than 10 percent of units sold.

Cost of sales decreased from \$6,530,118 in 2002 to \$6,351,193 in 2003, a decrease of \$178,925 or 2.7 percent. The decrease is due to reduced costs of manufacturing due to lower volumes and more efficient production. Bonuses were paid to the production and manufacturing employees in the amount of \$258,000.

The Company recorded an expense of \$481,637 in the second quarter of 2002 related to a recall and recovery of certain lots of its blood collection tube holders. The Company found that, in limited lots, upon testing, some blood collection tube holders retracted prior to activation. The premature retraction occurred during use as well as during shipping and handling. The Company has addressed the premature retraction through the manufacturing and design process.

Edgar Filing: RETRACTABLE TECHNOLOGIES INC - Form 10QSB

Gross profit increased from \$1,972,242 in 2002 to \$2,564,115 in 2003, an increase of \$591,873. Gross profit as a percentage of net sales was 22.0 percent and 28.8 percent for the six months ended June 30, 2002, and 2003, respectively.

Sales and marketing expense increased from \$1,933,093 in 2002 to \$2,153,389 in 2003, an increase of \$220,296 or 11.4 percent. The increase is principally due to bonus expense of \$100,000, an increase of travel and entertainment expense of \$78,412, and an increase in fees to distributors marketing fees of \$45,000.

Research and development costs increased from \$164,572 in 2002 to \$260,230 in 2003, an increase of \$95,658. The increase is principally due to an increase in payroll of \$30,000, bonuses of \$25,000, and increased costs of research and experimental parts.

General and administrative costs increased from \$1,999,227 in 2002 to \$2,920,392 in 2003, an increase of \$921,165. Increases in wages were \$125,000, bonuses increased \$235,000, legal expenses increased \$225,000 due

Table of Contents

principally to the NMT litigation, travel and entertainment increased \$95,000, and stock option expense for 2003 was \$115,000.

Debt conversion expense incurred in 2002 consists of \$1,821,246 for Series V Stock issued in excess of the original conversion term of the real estate note and working capital loan, \$440,000 for stock options issued in connection with the conversion, and \$57,827 of unamortized debt expenses.

Net interest expense declined from \$296,983 to \$152,042 due principally to the conversion of the Katie Petroleum note into Series V stock of the Company and higher invested cash balances.

Preferred stock dividend requirements were \$1,326,769 for 2003 compared to \$977,163 in 2002, an increase of \$349,606. The increase is due to an increase in the outstanding preferred stock as a result of sales of Series V Stock. Future dividend requirements will be reduced by approximately \$60,000 for each six months due to the conversion of the outstanding Series A stock.

Basic earnings (loss) per share was \$(0.28) per share in 2002 and \$0.47 in 2003 due principally to the settlements reached in litigation offset by the loss from operations. Fully diluted earnings per share were \$0.41 in 2003 assuming the conversion of debt securities, conversion of preferred stock, and exercise of dilutive stock options.

Cash flow increased from a negative \$400,010 for the six months ended June 30, 2002, to a positive \$7,960,474 for the six months ended June 30, 2003, an increase of \$8,360,484. The increase in cash flow was due to the settlements reached in litigation, offset by losses from operation, an increase in inventories, a decrease in payables, payment of dividends in 2003, and sales of Series V Stock in 2002.

Cash used in investing activities increased \$123,107 due to increased capital expenditures and acquisition of trademarks.

SIGNIFICANT ACCOUNTING POLICIES

The Company considers the following to be its most significant accounting policies. Careful consideration and Company review are given to these and all accounting policies on a routine basis to ensure that they are accurately and consistently applied.

Revenue Recognition

Revenue is recognized for sales to distributors when title and risk of ownership passes to the distributor, generally upon shipment. Revenue is recorded on the basis of sales price to distributors. Revenues on sales to distributors are recorded net of contractual pricing allowances. Revenue for shipments directly to end-users is recognized when title and risk of ownership passes from the Company. Any product shipped or distributed for evaluation purposes is expensed.

Accounts Receivable

The Company records trade receivables when revenue is recognized. No product has been consigned to customers. The Company's allowance for doubtful accounts is primarily determined by review of specific trade receivables. Those accounts that are doubtful of collection are included in the allowance. An additional allowance has been established based on a percentage of receivables outstanding. These provisions are reviewed to determine the adequacy of the allowance for doubtful accounts. Trade receivables are charged off when there is certainty as to their being uncollectible. Trade receivables are considered delinquent when payment has not been made within contract terms.

Table of Contents

Marketing Fees

The Company pays its distributors marketing fees for services provided by distributors. These services include participation in promotional activities, development of educational and promotional materials, representation at trade shows, clinical demonstrations, inservicing and training, and tracking reports detailing the placement of the Company's products to end-users. Marketing fees are accrued at the time of the sale of product to the distributor. These fees are paid after the distributor provides the Company a tracking report of product sales to end-users. These costs are included in sales and marketing expense in the Condensed Statements of Operations.

Stock-Based Compensation

Prior to 2002, the Company accounted for stock-based compensation under the recognition and measurement provisions (intrinsic value method) of APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and related Interpretations. Effective January 1, 2002, the Company adopted the fair value recognition provisions of SFAS No. 123, *Accounting for Stock-Based Compensation*, prospectively to all director, officer, and employee awards granted, modified, or settled after December 31, 2001. The prospective method is one of the alternative transition methods provided in FAS 148. Awards under the Company's plans vest over periods up to three years. Therefore, the cost related to stock-based compensation included in the determination of net income after December 31, 2001 is less than would have been recognized if the fair value method had been applied to all awards since the original effective date of SFAS No. 123. SFAS No. 123 indicates that the fair value method is the preferable method of accounting.

Recent Pronouncements

There are no recent accounting pronouncements that are expected to have a material impact on the Company.

LIQUIDITY AND FUTURE CAPITAL REQUIREMENTS

Historical Sources of Liquidity

We have historically funded operations primarily from proceeds from private placements and bank loans. We were capitalized with approximately \$52,600,000 raised from six separate private placement offerings. We sold 5,000,000 shares of Series A Stock at \$1 per share, for an aggregate of \$5,000,000 in cash. We sold 1,000,000 shares of Series I Class B Stock at \$5 per share for an aggregate of \$5,000,000 in cash. We sold 1,000,000 shares of Series II Class B Stock at \$10 per share for an aggregate of \$10,000,000 in cash. We sold 1,160,200 shares of Series III Class B Stock at \$10 per share for an aggregate of \$11,602,000 in cash. We sold 1,133,800 shares of Series IV Class B Stock at \$10 per share for an aggregate of \$11,338,000 in cash. We sold 2,416,221 of Series V Class B Stock at \$4 per share. Of the \$12,802,396 raised in this offering, \$4,435,600 was in cash; \$3,679,284 was in exchange for loans payable to Katie Petroleum; \$1,550,000 was in exchange of accounts payable; \$1,821,245 of debt conversion cost; and recognized a beneficial conversion feature aggregating \$1,316,267.

Edgar Filing: RETRACTABLE TECHNOLOGIES INC - Form 10QSB

We obtained \$1,200,000, \$710,000, and \$2,000,000 in 1996, 1997, and 2000, respectively, from bank loans. Additionally, we received a Small Business Administration loan of \$1,000,000 in 1996 to pay for portions of automated assembly equipment, multi-cavity molds, and other equipment. Furthermore, we borrowed \$5,000,000 in 2000 under our Credit Agreement with Abbott. In October 2002 we repaid the Abbott note with proceeds from a new note from Katie Petroleum, Inc. for \$3,000,000 and a portion of the proceeds from the Series V Class B offering.

Internal Sources of Liquidity

We believe we can achieve our break-even quarter utilizing our existing equipment. To achieve our break-even quarter we would need minimal access to hospital markets which has been difficult to obtain due to the monopolistic marketplace which is the subject of our lawsuit discussed in greater detail in our Form 10-KSB for 2002 and Form 10-QSB for the first quarter of 2003.

Table of Contents

Management believes that the settlement agreements discussed in Note 1 to the condensed financial statements will provide sufficient funds and facilitate the sale of the Company's products.

Unit sales increased 3.9 percent from 2002 to 2003. Abbott purchases comprised 48.4 percent and 47.2 percent of our unit sales in 2002 and 2003, respectively. Unit sales to Abbott increased 1.4 percent for the six month period from 2002 to 2003. Abbott distributes and markets our products into the acute care market.

Unit sales to customers other than Abbott were 51.6 percent and 52.8 percent of sales in 2002 and 2003, respectively. Unit sales to others increased 6.3 percent from 2002 to 2003. Sales to others consist primarily of sales into the alternate care market.

External Sources of Liquidity

We have obtained several loans over the past six years, which have, together with proceeds from sales of equities, enabled us to pursue development and production of our products.

The Company has agreed to a loan proposal from 1st International Bank for \$2,500,000. The proceeds from the loan will be used to pay off the remaining \$475,000 of the revolving credit agreement and fund a new warehouse and related infrastructure. Payments on the new note will be interest only during construction. Upon completion, payments will be based on a twenty-year amortization with a five-year maturity. The exact terms will be based on the amount of funds kept on deposit with the bank. Accordingly, interest will vary from the Wall Street Journal Prime Rate (WSJPR) to the WSJPR plus one percent, with floors that may range from 4.25 percent to 6.50 percent. Compensating balances at 1st International affecting the interest rate will range from \$0 to \$500,000.

Furthermore, we have 676,634 shares of Series V Class B stock and the shareholders have authorized an additional 5,000,000 shares of a Class C stock that could, if necessary, be used to raise equity funds.

In the event our claims against B-D are successfully resolved, it will likely have a further beneficial and material impact on our liquidity and demand for our products.

Contractual Obligations and Commercial Commitments

The following chart summarizes all of our material obligations and commitments to make future payments under contracts such as debt and lease agreements as of June 30, 2003:

Payments Due by Period

Edgar Filing: RETRACTABLE TECHNOLOGIES INC - Form 10QSB

<u>Contractual Obligations</u>	<u>Total</u>	<u>2003</u>	<u>2004-2006</u>	<u>2007-2008</u>	<u>After 2008</u>
Long-Term Debt	\$ 3,078,580	\$ 65,423	\$ 1,382,374	\$ 512,458	\$ 1,118,325
Capital Lease Obligations	122,057	59,916	62,141	0	0
Total Contractual Cash Obligations	\$ 3,200,637	\$ 125,339	\$ 1,444,515	\$ 512,458	\$ 1,118,325

Material Commitments for Expenditures

The Board of Directors has authorized the expenditure of \$2 million for the immediate construction of a warehouse. The Company has agreed to a loan proposal from 1st International Bank for \$2,500,000 which shall be the source for construction funds. Additional capital expenditures may include additional assembly lines, manufacturing space, warehousing, and related infrastructure. The expansion could include those products that have been developed but not yet marketed, as well as expanding manufacturing capacity for existing products. The amount of capital required would be dependent on our analysis of the extent of the potential market penetration if we are able to compete in a free market environment.

Table of Contents

We had \$ 198,825 in capital expenditures for the six months ended June 30, 2003.

Item 3. Controls and Procedures.

As of June 30, 2003, the Company carried out an evaluation, with the participation of the Company's principal executive, Thomas J. Shaw, and principal financial officer, Douglas W. Cowan, of the effectiveness of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) or Rule 15d-15(e) under the Securities and Exchange Act of 1934, as amended). Based on the evaluation of these controls and procedures required by paragraph (b) of Rule 13a-15 or Rule 15d-15 under the Exchange Act, the principal executive and principal financial officer determined that these procedures are effective in ensuring that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the United States Securities and Exchange Commission's rules and forms.

There were no changes in the Company's internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Rule 13a-15 or Rule 15d-15 under the Exchange Act that occurred during the second quarter of 2003 that has materially affected or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II

OTHER INFORMATION

Item 1. Legal Proceedings.

On January 29, 2001, we filed a lawsuit in the United States District Court for the Eastern District of Texas, Texarkana Division styled Retractable Technologies, Inc. v. Becton Dickinson & Co., Tyco International (U.S.), Inc., Tyco Healthcare Group, L.P., Novation, L.L.C., VHA, Inc., Premier, Inc. and Premier Purchasing Partners, L.P., Cause No. 501CV036. An update regarding material developments relating to a rescheduling of the trial date and a partial settlement of our claims was filed in our Form 10-QSB filed on May 15, 2003.

On February 1, 2002, the Company filed a patent infringement lawsuit alleging willful and intentional infringement of two patents directed to syringes having retractable needles in the United States District Court for the Eastern District of Texas, Sherman Division, styled Retractable Technologies, Inc. v. New Medical Technology, Inc.; New Medical Technology, Ltd.; and NMT Group PLC, Cause No. 4:02-CV-34. Thomas J. Shaw was subsequently added as a plaintiff in the suit. Additional information regarding this suit was previously reported in our Form 10-QSB filed on May 15, 2003.

We are not a party to any other material legal proceeding.

Item 2. Changes in Securities.

Edgar Filing: RETRACTABLE TECHNOLOGIES INC - Form 10QSB

The following discussion outlines all securities sold by us for cash or services rendered during the second quarter of 2003. All of the shares sold or granted were issued pursuant to the authority granted by the private offering exemption outlined in Section 4(2) and/or Rule 506 of Regulation D under the Securities Act to a limited number of persons and without a view toward distribution.

Effective as of July 15, 2003, Katie Petroleum, Inc. converted \$250,002.77 of debt into Common Stock of the Company at a rate of one share per \$7 of indebtedness. As a result, the Company issued 35,714 shares of Common Stock to Katie Petroleum, Inc. as well as paid a remaining principal amount of \$4.77 and interest of \$970.90.

Effective as of June 23, 2003, the Company issued Incentive Stock Options for the purchase of 349,560 shares of Common Stock and Non-Qualified Stock Options (NQSOs) for the purchase of 547,740 shares of

Table of Contents

Common Stock under the 1999 Stock Option Plan. The terms of the 1999 Stock Option Plan are set forth in the Plan as amended which has been filed as Exhibit No. 3.12 to the Company's Form 10-SB filed on June 23, 2000, and as Exhibit No. 10.13 to the Company's Form 10-KSB filed on March 31, 2003.

Item 3. Defaults Upon Senior Securities.

Series I Class B Convertible Preferred Stock

For the three months ended June 30, 2003, \$31,901 in dividends is in arrears. The total arrearage is \$2,499,494.

Series II Class B Convertible Preferred Stock

For the three months ended June 30, 2003, \$107,283 in dividends is in arrears. The total arrearage is \$4,277,536.

Series III Class B Convertible Preferred Stock

For the three months ended June 30, 2003, \$37,520 in dividends is in arrears. The total arrearage is \$2,366,778.

Series IV Class B Convertible Preferred Stock

For the three months ended June 30, 2003, \$266,500 in dividends is in arrears. The total arrearage is \$3,399,498.

Series V Class B Convertible Preferred Stock

For the three months ended June 30, 2003, \$192,768 is in arrears. The total arrearage is \$740,687.

Item 5. Other Information

The Company has agreed to a loan proposal from 1st International Bank for \$2,500,000. The proceeds from the loan will be used to pay off the remaining \$475,000 of the revolving credit agreement and fund a new warehouse and related infrastructure. Payments on the new note will be interest only during construction. Upon completion, payments will be based on a twenty-year amortization with a five-year maturity. The exact terms will be based on the amount of funds kept on deposit with the bank. Accordingly, interest will vary from the Wall Street Journal Prime Rate (WSJPR) to the WSJPR plus 1 percent, with floors that may range from 4.25 percent to 6.50 percent. Compensating balances at 1st International affecting the interest rate will range from \$0 to \$500,000.

Edgar Filing: RETRACTABLE TECHNOLOGIES INC - Form 10QSB

On July 15, 2003, Katie Petroleum converted the remaining balance of \$250,003 of its note secured by land and building into 35,714 shares of Common Stock of the Company.

From June 30 to July 9, 2003, an FDA Inspector conducted a baseline (comprehensive) inspection at the Company. The inspection included a review of our complaint handling system, MDR system, and CAPA system. The Inspector did not have any findings and a Form FDA 483 (list of findings) was not issued.

Item 6. Exhibits and Reports on Form 8-K.

(a) EXHIBITS

<u>Exhibit No.</u>	<u>Description of Document</u>
31.1	Certification of Principal Executive Officer
31.2	Certification of Principal Financial Officer
32	Certification Pursuant to 18 U.S.C. Section 1350

(b) REPORTS ON FORM 8-K

Table of Contents

On April 2, 2003, we filed a Form 8-K with an Item 5 disclosure regarding a press release filed on that same date of earnings information for the year ending December 31, 2002. The Form 8-K included Balance Sheets for the last two years and Statements of Operations for the last three years.

On May 12, 2003, we filed a Form 8-K with an Item 5 disclosure regarding a press release issued on May 7, 2003, announcing settlements with defendants Novation, L.L.C., VHA, Inc., Premier Inc., Premier Purchasing Partners, L.P., Tyco International (US) Inc., and Tyco Healthcare Group L.P., in our antitrust suit.

On May 20, 2003, we filed a Form 8-K with an Item 5 disclosure regarding a press release issued on May 19, 2003. The press release disclosed our earnings for the three months ended March 31, 2003, and contained a Balance Sheet and Condensed Statement of Operations.

On June 26, 2003, we filed a Form 8-K with an Item 5 disclosure regarding a press release issued on June 26, 2003. The release announced an agreement with a wholly owned subsidiary of B. Braun Melsunger AG. regarding distribution of needle devices in Africa.

SIGNATURES

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

DATE: August 14, 2003

RETRACTABLE TECHNOLOGIES, INC.

(Registrant)

By:

/s/ DOUGLAS W. COWAN

DOUGLAS W. COWAN

CHIEF FINANCIAL OFFICER