U S LIQUIDS INC
Form 10-Q
July 09, 2003

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2003

or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _________ to _________

Commission File Number: 001-13259

U S LIQUIDS INC.

(Exact name of registrant as specified in its charter)

Delaware	**76-0519797**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**

411 N. Sam Houston Parkway East, Suite 400, Houston, Texas 77060-3545
281-272-4500
(Address and telephone number of registrant s principal executive offices)

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. x Yes o No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). o Yes x No

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

Common Stock, $0.01 par value
16,233,149 shares as of June 25, 2003

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ITEM 1. FINANCIAL STATEMENTS

U S LIQUIDS INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except per share data)
(Unaudited)

	March 31, 2003	December 31, 2002
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 1,681	$ 4,068
Accounts receivable, less allowances of $1,046 and $1,018, respectively	27,147	32,165
Inventories	1,596	1,536
Prepayments and other current assets	4,510	5,062
Current assets of discontinued operations	2,270	2,853
Total current assets	37,204	45,684
PROPERTY, PLANT AND EQUIPMENT, net	84,193	86,295
GOODWILL, net	13,469	13,459
INTANGIBLE ASSETS, net	4,094	3,877
OTHER ASSETS	5,676	2,213
NONCURRENT ASSETS OF DISCONTINUED OPERATIONS	1,120	1,483
Total assets	$ 145,756	$ 153,011
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES:		
Current maturities of long-term obligations	$ 77,859	$ 78,474
Accounts payable	15,629	17,669
Accrued expenses and other current liabilities	20,787	23,376
Current liabilities of discontinued operations	2,408	2,084
Total current liabilities	116,683	121,603
LONG-TERM OBLIGATIONS, net of current maturities	2,536	2,672
PROCESSING RESERVE, net of current portion	2,803	3,007
CLOSURE AND REMEDIATION RESERVES, net of current portion	3,870	6,490
OTHER LONG-TERM LIABILITIES	744	882
NONCURRENT LIABILITIES OF DISCONTINUED OPERATIONS	427	427
Total liabilities	127,063	135,081
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS EQUITY:		
Preferred stock, $0.01 par value, 5,000,000 shares authorized, none issued or outstanding		
Common stock, $0.01 par value, 30,000,000 shares authorized, 16,233,149 and 16,095,222 shares issued and outstanding, respectively	162	161
Additional paid-in capital	177,213	177,166
Accumulated deficit	(158,692)	(159,407)
Accumulated other comprehensive income foreign currency translation adjustment	10	10

Total stockholders equity	18,693	17,930
Total liabilities and stockholders equity	$ 145,756	$ 153,011

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

U S LIQUIDS INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)
(Unaudited)

	Three Months Ended March 31, 2003	Three Months Ended March 31, 2002 (As Restated, see Note 12)
REVENUES	$36,830	$ 35,911
OPERATING EXPENSES	27,926	25,176
OPERATING MARGIN	8,904	10,735
DEPRECIATION AND AMORTIZATION	2,678	2,690
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	5,143	5,915
SPECIAL INCOME	(304)	
INCOME FROM OPERATIONS	1,387	2,130
INTEREST EXPENSE	3,332	1,662
OTHER INCOME, net	(67)	(162)
INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE INCOME TAXES AND CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE	(1,878)	630
PROVISION FOR INCOME TAXES	45	64
INCOME (LOSS) FROM CONTINUING OPERATIONS	(1,923)	566
DISCONTINUED OPERATIONS (NOTE 5):		
LOSS FROM DISCONTINUED OPERATIONS BEFORE INCOME TAXES	(70)	(1,480)
INCOME TAXES		(456)
LOSS FROM DISCONTINUED OPERATIONS	(70)	(1,024)
CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE	(2,708)	87,823
NET INCOME (LOSS)	$ 715	$(88,281)
BASIC EARNINGS (LOSS) PER COMMON SHARE:		
BASIC EARNINGS (LOSS) PER COMMON SHARE FROM CONTINUING OPERATIONS BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE	$ (0.12)	$ 0.03
DISCONTINUED OPERATIONS	(0.00)	(0.06)
CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE	0.17	(5.47)
BASIC EARNINGS (LOSS) PER COMMON SHARE	$ 0.04	$ (5.50)
DILUTED EARNINGS (LOSS) PER COMMON SHARE:		
DILUTED EARNINGS (LOSS) PER COMMON SHARE FROM CONTINUING OPERATIONS BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE	$ (0.12)	$ 0.03
DISCONTINUED OPERATIONS	(0.00)	(0.06)
CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE	0.17	(5.24)
DILUTED EARNINGS (LOSS) PER COMMON SHARE	$ 0.04	$ (5.27)

WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING	16,215	16,050
WEIGHTED AVERAGE NUMBER OF COMMON AND COMMON EQUIVALENT SHARES OUTSTANDING	16,318	16,747

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

U S LIQUIDS INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Three Months Ended March 31, 2003	Three Months Ended March 31, 2002 (As Restated, see Note 12)
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	$ 715	$ (88,281)
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Change in accounting principle	(2,708)	91,003
Depreciation and amortization	2,678	3,890
Net (gain) loss on sale of property, plant and equipment	30	(120)
Loss on discontinued operations	74	
Changes in operating assets and liabilities:		
Accounts receivable, net	4,113	4,349
Inventories	(59)	(83)
Prepayments and other current assets	551	(2,064)
Current assets of discontinued operations	410	
Intangible assets	(233)	(206)
Other assets	(3,453)	136
Long-term assets of discontinued operations	38	
Accounts payable, accrued liabilities and other current liabilities	(4,544)	(5,542)
Current liabilities of discontinued operations	330	
Closure, remediation and processing reserves	(330)	(543)
Other long-term liabilities	(138)	(54)
Deferred income taxes		(3,578)
Net cash used in operating activities	(2,526)	(1,093)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property, plant and equipment	(427)	(1,496)
Proceeds from sale of property, plant and equipment	1	365
Proceeds from sale of businesses	1,280	
Cash paid for acquisitions, net of subsequent purchase adjustments	(10)	
Net cash provided by (used in) investing activities	844	(1,131)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of long-term obligations	2,500	3,000
Principal payments on long-term obligations	(3,253)	(985)
Proceeds from exercise of stock options and employee stock purchase plan	48	25
Net cash provided by (used in) financing activities	(705)	2,040
NET DECREASE IN CASH AND CASH EQUIVALENTS	(2,387)	(184)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	4,068	1,498
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 1,681	$ 1,314

SUPPLEMENTAL DISCLOSURES:		
Cash paid for interest and related financing fees	$ 2,337	$ 4,491
Cash paid for income taxes	3	3
Cash received for income taxes	287	2

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

US LIQUIDS INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1. BUSINESS AND ORGANIZATION:

U S Liquids Inc. is a leading provider of liquid waste management services, including collection, processing, recovery and disposal services. The Company operates four divisions the Commercial Wastewater Division, the Industrial Wastewater Division, the Oilfield Waste Division and the Beverage Division. The Commercial Wastewater Division provides a variety of environmental services and collects, processes and disposes of various types of nonhazardous liquid waste. The Industrial Wastewater Division collects, processes and disposes of hazardous and nonhazardous liquid waste such as household hazardous wastes, industrial wastewater, petroleum fuels and antifreeze. The Beverage Division collects, processes and disposes of dated beverages and other consumer products containing alcohol or sugar. The Industrial and Beverage Divisions also generate revenue from the sale of by-products recovered from certain waste streams, including oils, ethanol, solvents, plastics, cardboard, aluminum, glass, industrial chemicals and recycled antifreeze products. The Oilfield Waste Division disposes waste that is generated in the exploration for and production of oil and natural gas primarily from the Gulf of Mexico and land-based rigs in Louisiana, Texas and northern Mexico. Prior to January 1, 2003, the Beverage Division s results were included in the results of the Commercial Wastewater Division. Effective January 1, 2003, the Beverage Division was separated as a fourth division. Prior year information has been reclassified to conform to the current year presentation. See Note 11.

2. BASIS OF PRESENTATION:

The interim condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures, normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America, have been condensed or omitted pursuant to those rules and regulations; although management believes that the disclosures made are adequate to make the information presented not misleading. In the opinion of management, all adjustments, consisting of only normal recurring adjustments, necessary to fairly present the financial position, results of operations and cash flows with respect to the interim condensed consolidated financial statements, have been included. The results of operations for the interim periods are not necessarily indicative of the results for the entire year. All intercompany accounts and transactions have been eliminated in consolidation.

Certain prior year amounts have been reclassified to conform to the current year presentation.

The interim condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company s Annual Report on Form 10-K/A for the year ended December 31, 2002, as filed with the SEC on July 3, 2003. Refer to Note 12 for the restatement information relating to the quarter ending March 31, 2002.

3. LIQUIDITY AND OUTLOOK:

The Company s capital requirements for continuing operations consist of general working capital needs, scheduled principal payments on its debt obligations and capital leases, funding of the Company s finite risk bonding program, certain contractual commitments and planned capital expenditures. The Company s capital resources consist of cash reserves, cash generated from operations and funds available under its revolving credit facility. On March 31, 2003, the Company received a short-term extension of the credit facility to provide for its near-term working capital needs and allow additional time to secure new financing. The facility, which matures on July 31, 2003, had an outstanding balance of $76.8 million at March 31, 2003.

The Company continues to review all of its alternatives to reduce its indebtedness. These alternatives include sales of assets or operating divisions or issuance of common stock or other securities. The proceeds of any such transaction would be used to reduce the Company s outstanding debt. There can be no assurance, however, that any such transaction will be successfully consummated. Any refinancing or business sale transaction is expected to result in either substantial dilution to current stockholders or significant reduction in the size of the Company.

US LIQUIDS INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(UNAUDITED)

The Company s recent performance has caused it to violate various financial covenants of its credit facility. Previously, the Company s lenders had been issuing short-term waivers. However, as of the date of this report, the Company is not in compliance with certain financial covenants set forth in the credit agreement. Noncompliance with these provisions permits the lenders to, among other things, accelerate the debt under the credit facility and foreclose on the collateral provided. The Company s lenders have not declared an event of default as a result of its noncompliance; however, they have retained the right to do so. The Company is in discussions with its lenders regarding amending the credit facility to, among other things, further extend the maturity date of the facility, provide for the Company s liquidity needs and bring the Company into compliance with the various financial covenants contained therein. There can be no assurance that the Company will be successful in obtaining an extension of the maturity date of the credit facility or amendments to any of the financial covenants or terms contained therein.

The report issued by the Company s auditors on the Company s December 31, 2002 financial statements stated that the working capital deficit caused by the close proximity of the maturity of the revolving credit facility, and the recent lack of compliance with the credit facility, raise substantial doubt about the Company s ability to continue as a going concern. If the Company is unable to successfully restructure its indebtedness, it may be required to seek protection under the bankruptcy laws.

During the first quarter of 2003, the terms of the credit facility were amended to change certain financial covenants, add additional weekly and monthly financial covenants, and make various enhancements to the collateral documentation securing the loans. The amendment also requires that the Company take certain steps to reduce its leverage, including the sale of one or more businesses that generated in 2002 or are expected to generate in 2003 at least $3.0 million in aggregate earnings before deduction for interest, taxes, depreciation and amortization. In exchange, the maturity date of the credit facility was extended to July 31, 2003, previously scheduled loan commitment reductions were eliminated, and, subject to weekly restrictions, availability under the credit facility was increased by approximately $3.5 million during the months of April through July 2003. As the Company sells certain businesses per the amendment above, the sale of such assets could result in an impairment below the current carrying value.

In July 2003, the terms of the credit facility were further amended to (1) renew until December 31, 2003 approximately $8.0 million of letters of credit issued on the Company s behalf, and (2) defer until July 31, 2003 the $0.6 million interest payment scheduled for payment on June 30, 2003. In return, the Company agreed to cash collateralize all obligations under the letters of credit described above on or before the termination of the credit facility. In addition, the Company agreed that it would not borrow any additional funds under the credit facility without the prior consent of its lenders.

The debt outstanding under the credit facility may be accelerated by the lenders if, among other things, a change in control of the Company occurs or certain individuals cease to serve as an executive officer of the Company and are not replaced within sixty days by an individual reasonably satisfactory to the lenders. The lenders have waived through July 31, 2003 an event of default arising from the resignation of Michael P. Lawlor, the Company s former Chief Executive Officer. On August 29, 2002, William DeArman, the Chairman of the Board of Directors, was appointed interim Chief Executive Officer. On October 31, 2002, the Board of Directors made his position permanent. The lenders have continued to waive the default arising from Mr. Lawlor s departure, but have not approved Mr. DeArman s appointment.

To address the Company s liquidity problems, the Board of Directors and Company management have taken the following actions:

- employed a new executive management team;
- engaged a financial advisor, as requested by the Company s lenders, to focus on financial restructuring plans;

US LIQUIDS INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(UNAUDITED)

implemented cost cutting measures such as reductions in workforce and a temporary freeze on previously authorized pay increases;

sold substantially all of the Texas and Northeast operations in the Commercial Wastewater Division, and used a substantial portion of the proceeds therefrom to reduce outstanding debt;

identified for sale or closure several additional underperforming businesses; and

acquired six oilfield waste transfer stations in Louisiana and Texas to replace the business lost from the non-renewal of the agreement with Newpark Resources, Inc.

Management is also:

pursuing the sale of certain businesses;

exploring the possibility of selling other non-core operations;

analyzing each of the Company s operations for opportunities to reduce costs, improve processes and increase efficiencies; and

actively seeking new financing.

As of March 31, 2003 and June 25, 2003, the Company had outstanding borrowings of $76.8 million and $79.8 million, respectively, under the credit facility. Letters of credit under the facility totaled $8.0 million as of both March 31, 2003 and June 25, 2003. Advances under the credit facility of up to $85.3 million currently bear interest at the prime rate plus 4.0% and advances above $85.3 million bear interest at the prime rate plus 6.0%. As of both of March 31, 2003 and June 25, 2003, amounts outstanding under the credit facility were accruing interest at approximately 8.3%, excluding amortization of financing costs. As of June 25, 2003, the unused portion of the credit facility was $1.2 million, none of which was available.

The condensed consolidated financial statements have been prepared on a basis which assumes that the Company will continue as a going concern and which contemplates the realization of assets and the satisfaction of liabilities and commitments in the normal course of business. The condensed consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

4. SPECIAL INCOME:

Reliance Insurance Company (Reliance) provided casualty insurance coverage for the Company. In October 2001, Reliance was declared insolvent by the Insurance Commissioner of the State of Pennsylvania. As a result, insurance coverage will not be available for any claims or lawsuits asserted against the Company for which insurance coverage was to be provided by Reliance and that were not resolved prior to Reliance being placed into liquidation. During the fourth quarter of 2001, an initial reserve of $3.5 million was established for any claims or lawsuits that were not resolved prior to Reliance being placed into liquidation. Subsequent adjustments have been made to the reserve based on settled obligations and known claims. During the first quarter of 2003, as a result of a review of potential claims and related costs, the reserve was reduced by $0.3 million resulting in special income of a like amount.

5. DISCONTINUED OPERATIONS:

Effective January 1, 2002, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, that addresses the financial accounting

US LIQUIDS INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(UNAUDITED)

and reporting for the impairment or disposal of long-lived assets. SFAS No. 144 requires that one accounting model be used for long-lived assets to be disposed of by sale and broadens the presentation of discontinued operations to include more disposal transactions. On November 6, 2002, the Company completed the sale of substantially all of its Texas businesses in the Commercial Wastewater Division. The transaction, structured as an asset sale, included businesses principally involved in the collection and processing of grease and grit trap waste, commercial wastewater treatment and field services in Houston, Dallas and San Antonio, Texas.

During the fourth quarter of 2002, the Company decided to divest of or suspend certain operations at several non-core and underperforming businesses in the Commercial Wastewater Division. Some operations were divested of or suspended during the fourth quarter of 2002 and the remaining operations are expected to be divested prior to December 31, 2003. During the first quarter of 2003, the remaining portions of the Company s Northeast operations were sold.

Under SFAS No. 144, the assets, liabilities and operating results of the businesses sold and the divested/suspended operations have been restated and presented separately as discontinued operations in both the Company s condensed consolidated balance sheet and statement of operations for all periods presented.

Assets and liabilities related to discontinued operations were as follows:

	March 31, 2003	December 31, 2002
	(In thousands) (Unaudited)	
Accounts receivable, net	$1,806	$ 2,326
Other current assets	464	527
Current assets of discontinued operations	$2,270	$ 2,853
Property, plant and equipment, net	$1,115	$ 1,477
Other long-term assets	5	6