U S LIQUIDS INC
Form 10-Q
August 13, 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 June 30, 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 August 4, 2003

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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

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

	June 30, 2003	December 31, 2002
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 3,214	$ 4,068
Accounts receivable, less allowances of $1,063 and $1,018, respectively	25,296	32,165
Inventories	1,785	1,536
Prepayments and other current assets	3,400	5,062
Current assets of discontinued operations	2,238	2,853
Total current assets	35,933	45,684
PROPERTY, PLANT AND EQUIPMENT, net	82,105	86,295
GOODWILL, net	13,756	13,459
INTANGIBLE ASSETS, net	4,282	3,877
OTHER ASSETS	3,590	2,213
NON-CURRENT ASSETS OF DISCONTINUED OPERATIONS	1,239	1,483
Total assets	$ 140,905	$ 153,011
LIABILITIES AND STOCKHOLDERS EQUITY		
CURRENT LIABILITIES:		
Current maturities of long-term obligations	$ 80,674	$ 78,474
Accounts payable	13,690	17,669
Accrued expenses and other current liabilities	21,724	23,376
Current liabilities of discontinued operations	2,075	2,084
Total current liabilities	118,163	121,603
LONG-TERM OBLIGATIONS, net of current maturities	2,431	2,672
PROCESSING RESERVE, net of current portion	2,632	3,007
CLOSURE AND REMEDIATION RESERVES, net of current portion	3,838	6,490
OTHER LONG-TERM LIABILITIES	685	882
NON-CURRENT LIABILITIES OF DISCONTINUED OPERATIONS	427	427
Total liabilities	128,176	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	(164,656)	(159,407)
Accumulated other comprehensive income foreign currency translation adjustment	10	10

Total stockholders equity	12,729	17,930
Total liabilities and stockholders equity	$ 140,905	$ 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 June 30,		Six Months Ended June 30,	
	2003	2002	2003	2002
		(As Restated, see Note 13)		(As Restated, see Note 13)
REVENUES	$37,247	$39,311	$74,077	$ 75,222
OPERATING EXPENSES	28,561	26,024	56,487	51,200
OPERATING MARGIN	8,686	13,287	17,590	24,022
DEPRECIATION AND AMORTIZATION	2,598	2,725	5,276	5,415
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	9,504	5,684	14,647	11,599
SPECIAL INCOME	(121)	(110)	(425)	(110)
INCOME (LOSS) FROM OPERATIONS	(3,295)	4,988	(1,908)	7,118
INTEREST EXPENSE	2,624	2,269	5,956	3,931
OTHER INCOME, net	(40)	(40)	(107)	(202)
INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE INCOME TAXES AND CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE	(5,879)	2,759	(7,757)	3,389
PROVISION FOR INCOME TAXES	15	140	60	204
INCOME (LOSS) FROM CONTINUING OPERATIONS	(5,894)	2,619	(7,817)	3,185
DISCONTINUED OPERATIONS (NOTE 6):				
INCOME (LOSS) FROM DISCONTINUED OPERATIONS BEFORE INCOME TAXES	(63)	631	(133)	(849)
INCOME TAXES	7	1,408	7	952
LOSS FROM DISCONTINUED OPERATIONS	(70)	(777)	(140)	(1,801)
CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE			(2,708)	87,823
NET INCOME (LOSS)	$ (5,964)	$ 1,842	$ (5,249)	$(86,439)
BASIC EARNINGS (LOSS) PER COMMON SHARE:				
BASIC EARNINGS (LOSS) PER COMMON SHARE FROM CONTINUING OPERATIONS BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE	$ (0.37)	$ 0.16	$ (0.48)	$ 0.20
DISCONTINUED OPERATIONS	(0.00)	(0.05)	(0.01)	(0.11)
CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE			0.17	(5.47)
BASIC EARNINGS (LOSS) PER COMMON SHARE	$ (0.37)	$ 0.11	$ (0.32)	$ (5.38)
DILUTED EARNINGS (LOSS) PER COMMON SHARE:				
DILUTED EARNINGS (LOSS) PER COMMON SHARE FROM CONTINUING OPERATIONS BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE	$ (0.37)	$ 0.16	$ (0.48)	$ 0.19

DISCONTINUED OPERATIONS	(0.00)	(0.05)	(0.01)	(0.11)
CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE			0.17	(5.28)
DILUTED EARNINGS (LOSS) PER COMMON SHARE	$ (0.37)	$ 0.11	$ (0.32)	$ (5.20)
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING	16,233	16,080	16,224	16,065
WEIGHTED AVERAGE NUMBER OF COMMON AND COMMON EQUIVALENT SHARES OUTSTANDING	16,233	16,467	16,224	16,631

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)

	Six Months Ended June 30,	
	2003	**2002**
		(As Restated, see Note 13)
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$(5,249)	$(86,439)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Change in accounting principle	(2,708)	91,003
Depreciation and amortization	5,276	7,533
Net (gain) loss on sale of property, plant and equipment	53	(123)
Loss on discontinued operations	74	
Changes in operating assets and liabilities:		
Accounts receivable, net	5,964	3,939
Inventories	(248)	(345)
Prepayments and other current assets	1,661	(697)
Current assets of discontinued operations	442	
Intangible assets	(436)	(523)
Other assets	(1,362)	229
Long-term assets of discontinued operations	39	
Accounts payable, accrued liabilities and other current liabilities	(5,446)	(2,146)
Current liabilities of discontinued operations	(1)	
Closure, remediation and processing reserves	(533)	(3,982)
Other long-term liabilities	(197)	(108)
Deferred income taxes		(2,786)
Net cash provided by (used in) operating activities	(2,671)	5,555
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property, plant and equipment	(1,283)	(3,800)
Proceeds from sale of property, plant and equipment	1	429
Proceeds from sale of businesses	1,280	
Cash paid for acquisitions, net of subsequent purchase adjustments	(184)	
Net cash used in investing activities	(186)	(3,371)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of long-term obligations	5,500	3,319
Principal payments on long-term obligations	(3,545)	(6,905)
Proceeds from exercise of stock options and employee stock purchase plan	48	25
Net cash provided by (used in) financing activities	2,003	(3,561)
EFFECT OF FOREIGN CURRENCY TRANSLATION ON CASH AND CASH EQUIVALENTS		95
NET DECREASE IN CASH AND CASH EQUIVALENTS	(854)	(1,282)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	4,068	1,498

CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 3,214	$ 216
SUPPLEMENTAL DISCLOSURES:		
Cash paid for interest and related financing fees	$ 5,841	$ 6,192
Cash paid for income taxes	20	422
Cash received for income taxes	289	63

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

U S 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 12. On July 31, 2003, the Company sold its Oilfield Waste Division, its Beverage Division and its Romic Environmental Technologies business to ERP Environmental Services, Inc. (ERP Environmental). See Note 4 for a further description of the sale.

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 segment information has 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 13 for the restatement information relating to the three and six months ended June 30, 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, cash proceeds from planned asset sales and funds available under its revolving credit facility. On July 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 August 29, 2003, had an outstanding balance of $79.8 million at June 30, 2003.

The Company continues to review all of its alternatives to reduce or refinance its indebtedness. These alternatives include sales of assets or operating divisions or issuance of common stock or other securities. The proceeds of any such transactions would be used to reduce or replace the Company s outstanding debt. There can be

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

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 further reduction in the size of the Company.

On July 31, 2003, the Company sold three of its businesses (see Note 4) for total proceeds of $68.0 million. From these proceeds, and with the approval of its senior lenders, $59.7 million was used to reduce the Company s debt balance, $1.9 million was used to pay deferred interest and fees due on its credit facility, $2.1 million was used to pay various transaction expenses and $2.3 million was used to establish a fund for future severance of employees as the Company is restructured. In addition, an escrow of $2.0 million was established from the proceeds pending the determination of the final purchase price, which is subject to adjustment based upon the net worth of the acquired businesses on the closing date.

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 filing, 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. The Company is also attempting to re-negotiate the payment terms of certain non-essential unsecured contractual obligations. 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 or will be successful in re-negotiating the payment terms of any unsecured contractual obligation.

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 required 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) extend the maturity date of the credit facility to August 29, 2003, (2) renew until December 31, 2003 approximately $8.0 million of letters of credit issued on the Company s behalf, and (3) defer until the earlier of August 29, 2003 or the date of sale of various operations 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 and pay a $200,000 amendment fee. 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

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

waived through July 31, 2003 an event of default arising from the resignation of Michael P. Lawlor, the Company s former Chief Executive Of