

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the quarterly period ended March 31, 2014

OR

**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: 001-34269

**SHARPS COMPLIANCE CORP.**

(Exact name of registrant as specified in its charter)

<b>Delaware</b>	<b>74-2657168</b>
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

<b>9220 Kirby Drive, Suite 500, Houston, Texas</b>	<b>77054</b>
(Address of principal executive offices)	(Zip Code)

**(713) 432-0300**

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).  
Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Securities Exchange Act of 1934.

Large Accelerated Filer       Accelerated Filer       Non-accelerated Filer       Smaller reporting company   
(Do not check if a smaller reporting company)

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

As of May 5, 2014, there were 15,268,141 outstanding shares of the Registrant's common stock, par value \$0.01 per share.

**SHARPS COMPLIANCE CORP. AND SUBSIDIARIES**

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**PART I FINANCIAL INFORMATION**  
**ITEM 1. FINANCIAL STATEMENTS**

**SHARPS COMPLIANCE CORP. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(In thousands, except share and par value)

	<u>March 31,</u> <u>2014</u> <u>(Unaudited)</u>	<u>June 30,</u> <u>2013</u>
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$ 14,430	\$ 15,503
Restricted cash	111	111
Accounts receivable, net of allowance for doubtful accounts of \$23 and \$26, respectively	2,976	2,595
Inventory	1,376	1,632
Prepaid and other current assets	904	583
<b>TOTAL CURRENT ASSETS</b>	<b>19,797</b>	<b>20,424</b>
PROPERTY, PLANT AND EQUIPMENT, net	3,954	4,440
INTANGIBLE ASSETS, net of accumulated amortization of \$316 and \$275, respectively	729	668
<b>TOTAL ASSETS</b>	<b>\$ 24,480</b>	<b>\$ 25,532</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable	\$ 1,486	\$ 1,085
Accrued liabilities	1,196	1,345
Deferred revenue	1,174	1,351
<b>TOTAL CURRENT LIABILITIES</b>	<b>3,856</b>	<b>3,781</b>
LONG-TERM DEFERRED REVENUE	435	579
OTHER LONG-TERM LIABILITIES	50	102
<b>TOTAL LIABILITIES</b>	<b>4,341</b>	<b>4,462</b>
<b>COMMITMENTS AND CONTINGENCIES</b>		
<b>STOCKHOLDERS' EQUITY</b>		
Common stock, \$0.01 par value per share; 20,000,000 shares authorized; 15,429,942 and 15,370,320 shares issued and outstanding, respectively	155	154
Treasury stock, at cost, 161,801 and 25,360 shares repurchased, respectively	(681)	(74)
Additional paid-in capital	23,579	23,211
Accumulated deficit	(2,914)	(2,221)
<b>TOTAL STOCKHOLDERS' EQUITY</b>	<b>20,139</b>	<b>21,070</b>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$ 24,480</b>	<b>\$ 25,532</b>

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

**SHARPS COMPLIANCE CORP. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
(In thousands, except per-share data)

	Three-Months Ended March 31,	
	2014	2013
(Unaudited)		
REVENUES	\$ 5,553	\$ 5,410
Cost of revenues	4,144	3,894
GROSS PROFIT	<u>1,409</u>	<u>1,516</u>
Selling, general and administrative	2,225	2,351
Depreciation and amortization	<u>119</u>	<u>107</u>
OPERATING LOSS	(935)	(942)
OTHER INCOME		
Interest income	<u>6</u>	<u>6</u>
TOTAL OTHER INCOME	<u>6</u>	<u>6</u>
LOSS BEFORE INCOME TAXES	(929)	(936)
INCOME TAX EXPENSE		
Current	6	5
Deferred	-	14
TOTAL INCOME TAX EXPENSE	<u>6</u>	<u>19</u>
NET LOSS	<u>\$ (935)</u>	<u>\$ (955)</u>
NET LOSS PER COMMON SHARE		
Basic	<u>\$ (0.06)</u>	<u>\$ (0.06)</u>
Diluted	<u>\$ (0.06)</u>	<u>\$ (0.06)</u>
WEIGHTED AVERAGE SHARES USED IN COMPUTING NET LOSS PER COMMON SHARE:		
Basic	15,248	15,246
Diluted	15,248	15,246

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

**SHARPS COMPLIANCE CORP. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
**(In thousands, except per-share data)**

	<b>Nine-Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
	<b>(Unaudited)</b>	
REVENUES	\$ 19,474	\$ 16,280
Cost of revenues	13,052	11,512
GROSS PROFIT	<u>6,422</u>	<u>4,768</u>
Selling, general and administrative	6,756	6,451
Depreciation and amortization	<u>351</u>	<u>331</u>
OPERATING LOSS	(685)	(2,014)
OTHER INCOME		
Interest income	16	22
TOTAL OTHER INCOME	<u>16</u>	<u>22</u>
LOSS BEFORE INCOME TAXES	(669)	(1,992)
INCOME TAX EXPENSE		
Current	24	15
Deferred	-	15
TOTAL INCOME TAX EXPENSE	<u>24</u>	<u>30</u>
NET LOSS	<u>\$ (693)</u>	<u>\$ (2,022)</u>
NET LOSS PER COMMON SHARE		
Basic	<u>\$ (0.05)</u>	<u>\$ (0.13)</u>
Diluted	<u>\$ (0.05)</u>	<u>\$ (0.13)</u>
WEIGHTED AVERAGE SHARES USED IN COMPUTING NET LOSS PER COMMON SHARE:		
Basic	15,296	15,229
Diluted	15,296	15,229

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

**SHARPS COMPLIANCE CORP. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**  
(In thousands, except share data)

	Common Stock		Treasury Stock		Additional Paid-in Capital	Retained Earnings (Accumulated Deficit)	Total Stockholders' Equity
	Shares	Amount	Shares	Amount			
Balances, June 30, 2012	15,206,127	\$ 152	-	\$ -	\$ 22,537	\$ 491	\$ 23,180
Exercise of stock options	100,445	1	-	-	161	-	162
Stock-based compensation	-	-	-	-	514	-	514
Issuance of restricted stock	63,748	1	-	-	(1)	-	-
Shares repurchased	-	-	(25,360)	(74)	-	-	(74)
Net loss	-	-	-	-	-	(2,712)	(2,712)
Balances, June 30, 2013	15,370,320	154	(25,360)	(74)	23,211	(2,221)	21,070
Exercise of stock options*	13,125	1	-	-	46	-	47
Stock-based compensation*	-	-	-	-	322	-	322
Issuance of restricted stock*	46,497	-	-	-	-	-	-
Shares repurchased*	-	-	(136,441)	(607)	-	-	(607)
Net loss*	-	-	-	-	-	(693)	(693)
Balances, March 31, 2014*	15,429,942	\$ 155	(161,801)	\$ (681)	\$ 23,579	\$ (2,914)	\$ 20,139

\* unaudited

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

**SHARPS COMPLIANCE CORP. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(In thousands)

	Nine-Months Ended March 31,	
	2014	2013
	(Unaudited)	
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net loss	\$ (693)	\$ (2,022)
Adjustments to reconcile net loss to net cash used in operating activities		
Depreciation and amortization	835	827
Stock-based compensation expense	322	414
Deferred tax expense	-	15
Changes in operating assets and liabilities:		
Accounts receivable	(381)	(617)
Inventory	256	315
Prepaid and other current assets	(321)	(104)
Accounts payable and accrued liabilities	200	626
Deferred revenue	(321)	(135)
<b>NET CASH USED IN OPERATING ACTIVITIES</b>	<b>(103)</b>	<b>(681)</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchase of property, plant and equipment	(308)	(548)
Additions to intangible assets	(102)	(158)
<b>NET CASH USED IN INVESTING ACTIVITIES</b>	<b>(410)</b>	<b>(706)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds from exercise of stock options	47	42
Shares repurchased	(607)	(74)
<b>NET CASH USED IN FINANCING ACTIVITIES</b>	<b>(560)</b>	<b>(32)</b>
<b>NET DECREASE IN CASH AND CASH EQUIVALENTS</b>	<b>(1,073)</b>	<b>(1,419)</b>
CASH AND CASH EQUIVALENTS, beginning of period	15,503	17,498
CASH AND CASH EQUIVALENTS, end of period	<u>\$ 14,430</u>	<u>\$ 16,079</u>
<b>SUPPLEMENTAL CASH FLOW DISCLOSURES:</b>		
Income taxes paid	<u>\$ 11</u>	<u>\$ -</u>

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

**SHARPS COMPLIANCE CORP. AND SUBSIDIARIES**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(UNAUDITED)**

**NOTE 1 - ORGANIZATION AND BACKGROUND**

The accompanying unaudited condensed consolidated financial statements include the financial transactions and accounts of Sharps Compliance Corp. and its wholly owned subsidiaries, Sharps Compliance, Inc. of Texas (dba Sharps Compliance, Inc.), Sharps e-Tools.com, Inc. (“Sharps e-Tools”), Sharps Manufacturing, Inc., Sharps Environmental Services, Inc. (dba Sharps Environmental Services of Texas, Inc.) and Sharps Safety, Inc. (collectively, “Sharps” or the “Company”). All significant intercompany accounts and transactions have been eliminated upon consolidation.

**NOTE 2 - BASIS OF PRESENTATION**

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission (“SEC”) for interim financial information and with instructions to Form 10-Q and, accordingly, do not include all information and footnotes required under accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, these interim condensed consolidated financial statements contain all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of the consolidated financial position of the Company as of March 31, 2014, the results of its operations and cash flows for the three and nine months ended March 31, 2014 and 2013 and stockholders’ equity for the nine months ended March 31, 2014. The results of operations for the three and nine months ended March 31, 2014 are not necessarily indicative of the results to be expected for the entire fiscal year ending June 30, 2014. These unaudited condensed consolidated financial statements should be read in conjunction with the Company’s Annual Report on Form 10-K for the year ended June 30, 2013.

**NOTE 3 - SIGNIFICANT ACCOUNTING POLICIES**

**Revenue Recognition:** The Company recognizes revenue from product sales when goods are shipped or delivered, and title and risk of loss pass to the customer except for those sales via multiple-deliverable arrangements. Provisions for certain rebates, product returns and discounts to customers are accounted for as reductions in sales in the same period the related sales are recorded. Product discounts granted are based on the terms of arrangements with direct, indirect and other market participants, as well as market conditions, including prices charged by competitors. Rebates are estimated based on contractual terms, historical experience, trend analysis and projected market conditions in the various markets served.

The Company recognizes revenue in accordance with guidance on revenue recognition of multiple-deliverable arrangements. Under this guidance, certain products offered by the Company have revenue producing components that are recognized over multiple delivery points (Sharps Recovery System™ (formerly the Sharps Disposal by Mail Systems®) and various TakeAway Environmental Return Systems™ referred to as “Mailbacks” and Sharps® Pump and Asset Return Boxes, referred to as “Pump Returns”) and can consist of up to three separate elements, or units of measure, as follows: (1) the sale of the compliance and container system, (2) return transportation and (3) treatment service.

In accordance with the relative selling price methodology, an estimated selling price is determined for all deliverables that qualify for separate units of accounting. The actual consideration received in a multiple-deliverable arrangement is then allocated to the units based on their relative sales price. The selling price for the transportation revenue and the treatment revenue utilizes third party evidence. The Company estimates the selling price of the compliance and container system based on the product and services provided including compliance with local, state and Federal laws, adherence to stringent manufacturing and testing requirements, safety to the patient and the community as well as storage and containment capabilities.

Revenue for the sale of the compliance and container is recognized upon delivery to the customer, at which time the customer takes title and assumes risk of ownership. Transportation revenue is recognized when the customer returns the compliance and container system and the container has been received at the Company’s owned or contracted facilities. The compliance and container system is mailed or delivered by an alternative logistics provider to the Company’s owned or contracted facilities. Treatment revenue is recognized upon the destruction or conversion and proof of receipt and treatment having been performed on the container. Since the transportation element and the treatment elements are undelivered services at the point of initial sale of the compliance and container, transportation and treatment revenue is deferred until the services are performed. The current and long-term portions of deferred revenues are determined through regression analysis and historical trends. Furthermore, through regression analysis of historical data, the Company has determined that a certain percentage of all compliance and container systems sold may not be returned. Accordingly, a portion of the transportation and treatment elements are recognized at the point of sale.

**Income Taxes:** The liability method is used in accounting for deferred income taxes. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. A valuation allowance is established when it is more likely than not that some portion or all of the deferred tax assets will not be realized. The establishment of valuation allowances and development of projected annual effective tax rates requires significant judgment and is impacted by various estimates. Both positive and negative evidence, as well as the objectivity and verifiability of that evidence, is considered in determining the appropriateness of recording a valuation allowance on deferred tax assets.

**Accounts Receivable:** Accounts receivable consist primarily of amounts due to the Company from our normal business activities. Accounts receivable balances are determined to be delinquent when the amount is past due based on the contractual terms with the customer. The Company maintains an allowance for doubtful accounts to reflect the expected uncollectibility of accounts receivable based on past collection history and specific risks identified among uncollected accounts. Accounts receivable are charged to the allowance for doubtful accounts when the Company determines that the receivable will not be collected and/or when the account has been referred to a third party collection agency. The Company has a history of minimal uncollectible accounts.

#### **NOTE 4 – RECENTLY ISSUED ACCOUNTING STANDARDS**

There are no recently issued accounting pronouncements that will have a significant impact on the Company's consolidated financial statements as of March 31, 2014.

#### **NOTE 5 - INCOME TAXES**

The establishment of valuation allowances and development of projected annual effective tax rates requires significant judgment and is impacted by various estimates. Both positive and negative evidence, as well as the objectivity and verifiability of that evidence, is considered in determining the appropriateness of recording a valuation allowance on deferred tax assets. Under generally accepted accounting principles, the valuation allowance has been recorded to reduce the Company's net deferred tax asset to an amount that is more likely than not to be realized and is based upon the uncertainty of the realization of certain federal and state deferred assets related to net operating loss carryforwards and other tax attributes. The Company's net deferred tax assets have been fully reserved by valuation allowance.

The Company's effective tax rate for the nine months ended March 31, 2014 and 2013 was (3.6%) and (1.5%), respectively, reflecting estimated state income taxes. The Company's tax benefit associated with taxable losses during the nine months ended March 31, 2014 and the year ended June 30, 2013, was offset by a deferred tax valuation allowance.

#### **NOTE 6 - NOTES PAYABLE AND LONG-TERM DEBT**

On January 28, 2014, the Company entered into a credit agreement with a commercial bank ("Credit Agreement"). The Credit Agreement, which replaces the prior credit agreement executed effective April 30, 2013 with another commercial bank ("Prior Credit Agreement"), provides for a two-year, \$3.0 million line of credit facility, the proceeds of which may be utilized for working capital, letters of credit (up to \$500,000) and general corporate purposes. Indebtedness under the Credit Agreement is secured by the Company's accounts receivable and inventory with advances outstanding at any time limited to a Borrowing Base (as defined in the Credit Agreement) equal to 80% of eligible accounts receivable plus 50% of eligible inventory. Borrowings bear interest at WSJ Prime, which we estimate to be approximately 3.25% as of March 31, 2014. The Company will pay a fee of 0.25% per annum on the unused amount of the line of credit. As of March 31, 2014, the Company had no outstanding borrowings, other than \$335 thousand in letters of credit, which leaves \$2.7 million of credit available.

The Credit Agreement contains affirmative and negative covenants that, among other things, require the Company to maintain a minimum level of tangible net worth of \$10.5 million and minimum liquidity of \$5.0 million. The Company is in compliance with all the financial covenants as of March 31, 2014. The Credit Agreement, which expires on January 28, 2016, also contains customary events of default which, if uncured, may terminate the Credit Agreement and require immediate repayment of all indebtedness to the lenders.

The Prior Credit Agreement, which was effective through January 28, 2014, provided for a cash-collateralized \$200,000 line of credit facility with a maturity date of July 15, 2015. No amounts related to the Prior Credit Agreement were outstanding as of March 31, 2014 other than letters of credit of approximately \$110 thousand, which are in the process of being released.

**NOTE 7 – STOCK-BASED COMPENSATION**

Stock-based compensation cost is measured at the grant date, based on the calculated fair value of the award, and is recognized as an expense over the employee’s requisite service period (generally the vesting period of the equity grant). Reductions in taxes payable resulting from tax deductions that exceed the recognized tax benefit associated with compensation expense (excess tax benefits) are classified as financing cash flows and as an increase to additional paid in capital. During the three and nine months ended March 31, 2014 and 2013, stock-based compensation amounts are as follows (in thousands):

	<b>Three-Months Ended</b>		<b>Nine-Months Ended</b>	
	<b>March 31,</b>		<b>March 31,</b>	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
	<b>(Unaudited)</b>		<b>(Unaudited)</b>	
Stock-based compensation expense included in:				
Cost of revenue	\$ 4	\$ 6	\$ 14	\$ 14
General and administrative expense	118	85	308	400
<b>Total</b>	<b>\$ 122</b>	<b>\$ 91</b>	<b>\$ 322</b>	<b>\$ 414</b>

For the three and nine months ended March 31, 2014, excess tax benefits have been eliminated by the valuation allowance on the deferred tax assets.

**NOTE 8 - EARNINGS PER SHARE**

Earnings per share are measured at two levels: basic per share and diluted per share. Basic per share is computed by dividing net loss by the weighted average number of common shares outstanding during the period. Diluted per share is computed by dividing net loss by the weighted average number of common shares after considering the additional dilution related to common stock options and restricted stock. In computing diluted earnings per share, the outstanding common stock options are considered dilutive using the treasury stock method. Vested restricted shares are included in basic common shares outstanding, and unvested restricted shares are included in the diluted common shares outstanding, if the effect is dilutive.

The following information is necessary to calculate earnings per share for the periods presented (in thousands, except per-share data):

	<b>Three-Months Ended</b>		<b>Nine-Months Ended</b>	
	<b>March 31,</b>		<b>March 31,</b>	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
	<b>(Unaudited)</b>		<b>(Unaudited)</b>	
Net loss, as reported	\$ (935)	\$ (955)	\$ (693)	\$ (2,022)
Weighted average common shares outstanding	15,248	15,246	15,296	15,229
Effect of dilutive stock options	-	-	-	-
Weighted average diluted common shares outstanding	15,248	15,246	15,296	15,229
Net loss per common share				
Basic	\$ (0.06)	\$ (0.06)	\$ (0.05)	\$ (0.13)
Diluted	\$ (0.06)	\$ (0.06)	\$ (0.05)	\$ (0.13)
Employee stock options excluded from computation of dilutive loss per share amounts because their effect would be anti-dilutive	206	887	648	883

**NOTE 9 - EQUITY TRANSACTIONS**

During the three and nine months ended March 31, 2014 and 2013, stock options to purchase shares of the Company's common stock were exercised as follows:

	<b>Three-Months Ended</b>		<b>Nine-Months Ended</b>	
	<b>March 31,</b>		<b>March 31,</b>	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
	<b>(Unaudited)</b>		<b>(Unaudited)</b>	
Options exercised	13,125	46,945	13,125	50,445
Proceeds (in thousands)	\$ 47	\$ 40	\$ 47	\$ 42
Average exercise price per share	\$ 3.53	\$ 0.85	\$ 3.53	\$ 0.84

As of March 31, 2014, there was \$497 thousand of stock option and restricted stock compensation expense related to non-vested awards which is expected to be recognized over a weighted average period of 2.86 years.

On January 7, 2013, the Company announced that its Board of Directors approved a stock repurchase program effective January 3, 2013, authorizing the Company to repurchase in the aggregate up to \$3 million of its outstanding common stock over a two-year period. During the three and nine months ended March 31, 2014 and 2013, shares were repurchased as follows:

	<b>Three-Months Ended</b>		<b>Nine-Months Ended</b>	
	<b>March 31,</b>		<b>March 31,</b>	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
	<b>(Unaudited)</b>		<b>(Unaudited)</b>	
Shares repurchased	-	25,360	136,441	25,360
Cash paid for shares repurchased (in thousands)	\$ -	\$ 74	\$ 607	\$ 74
Average price paid per share	\$ -	\$ 2.93	\$ 4.45	\$ 2.93

Total shares repurchased under the program are 161,801 shares at a cost of \$0.7 million. As of March 31, 2014, approximately \$2.3 million remained of the Company's \$3.0 million repurchase program. Shares purchased all shares with cash resources.

**NOTE 10 – INVENTORY**

The components of inventory are as follows (in thousands):

	<b>March 31,</b>	<b>June 30,</b>
	<b>2014</b>	<b>2013</b>
	<b>(Unaudited)</b>	
Raw materials	\$ 821	\$ 887
Finished goods	555	745
<b>Total</b>	<b>\$ 1,376</b>	<b>\$ 1,632</b>

**NOTE 11 – FAIR VALUE OF FINANCIAL INSTRUMENTS**

The Company considers the fair value of all financial instruments, including cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, not to be materially different from their carrying values at March 31, 2014 due to their short-term nature.

**ITEM 2.**

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

**INFORMATION REGARDING FORWARD-LOOKING STATEMENTS**

*This quarterly report on Form 10-Q contains certain forward-looking statements and information relating to the Company and its subsidiaries that are based on the beliefs of the Company's management as well as assumptions made by and information currently available to the Company's management. When used in this report, the words "anticipate", "believe", "expect", "estimate", "project" and "intend" and words or phrases of similar import, as they relate to the Company or its subsidiaries or Company management, are intended to identify forward-looking statements. Such statements reflect the current risks, uncertainties and assumptions related to certain factors, including without limitations, competitive factors, general economic conditions, customer relations, relationships with vendors, governmental regulation and supervision, seasonality, distribution networks, product introductions and acceptance, technological change, changes in industry practices, onetime events and other factors described herein. Based upon changing conditions, should any one or more of these risks or uncertainties materialize, or should any underlying assumptions prove incorrect, actual results may vary materially from those described herein as anticipated, believed, expected, estimated or intended. The Company does not intend to update these forward-looking statements.*

**GENERAL**

Sharps Compliance Corp. is a leading full-service provider of solutions for the cost-effective management of medical waste, used health care materials and unused dispensed medications. Our solutions facilitate the proper collection, containment, transportation and treatment of numerous types of healthcare-related materials, including hypodermic needles, lancets and other devices or objects used to puncture or lacerate the skin, or sharps, and unused consumer dispensed medications and over-the-counter drugs. We serve customers in multiple markets such as home health care, retail clinics and immunizing pharmacies, pharmaceutical manufacturers, professional offices (physicians, dentists and veterinarians), assisted living and long-term care facilities (assisted living, continuing care, long-term acute care, memory care and skilled nursing), government (federal, state and local), consumers, commercial and agriculture, as well as distributors to many of the aforementioned markets. We assist our customers in determining which of our solution offerings best fit their needs for the collection, containment, return transportation and treatment of medical waste, used healthcare materials and unused dispensed medications. Our differentiated approach provides our customers the flexibility to return and properly treat medical waste, used healthcare materials or unused dispensed medications through a variety of solutions and products transported primarily through the United States Postal Service ("USPS"). For customers with facilities or locations that may generate larger quantities of medical waste, we integrate the Daniels Sharpsmart route-based pick-up service into our complete offering. The benefits of this comprehensive offering include single point of contact, consolidated billing, integrated manifest and proof of destruction repository in addition to our cost savings. Furthermore, we provide comprehensive tracking and reporting tools that enable our customers to meet complex medical waste disposal and unused dispensed patient medication compliance requirements. We believe the fully-integrated nature of our operations is a key factor leading to our success and continued recurring revenue growth. We continue to take advantage of the many opportunities in all markets served as we educate the market place and as prospective customers become more aware of alternatives to traditional methods of disposal (i.e., route-based pick-up services).

As a leading full-service provider of comprehensive medical waste management services throughout North America, our strategy is to capture a large part of the estimated \$3.8 billion untapped market for our solutions by targeting the major agencies that are interrelated with this medical waste stream, including pharmaceutical manufacturers, home healthcare providers, retail pharmacies and clinics, the U.S. government and the professional market which is comprised of physicians, dentists and veterinary practices. The Company's flagship product, the Sharps Recovery System™ is a comprehensive solution for the containment, transportation, treatment and tracking of medical waste and used healthcare materials. The Company has partnered with Daniels Sharpsmart in a joint marketing alliance ("JMA") to serve the entire U.S. medical waste market, addressing small and large quantity medical waste generators with highly cost-effective and compliant solutions. Our other solutions include Complete Needle™ Collection and Disposal System, TakeAway Environmental Return System™, ComplianceTRAC<sup>SM</sup>, Sharps Tracer®, Sharps Secure® Needle Collection and Containment System™, Pitch-It IV™ Poles, Trip LesSystem®, Sharps® Pump and Asset Return System, Sharps® MWMS™ (a Medical Waste Management System ("MWMS")) and Spill Kit TakeAway Recovery System™.

**RESULTS OF OPERATIONS**

The following analyzes changes in the consolidated operating results and financial condition of the Company during the three and nine months ended March 31, 2014 and 2013. The following table sets forth, for the periods indicated, certain items from the Company's Condensed Consolidated Statements of Operations, dollars in thousands and percentages expressed as a percentage of revenue:

	Three-Months Ended March 31,				Nine-Months Ended March 31,			
	2014	%	2013	%	2014	%	2013	%
	(Unaudited)				(Unaudited)			
<b>Revenues</b>	\$ 5,553	100.0%	\$ 5,410	100.0%	\$ 19,474	100.0%	\$ 16,280	100.0%
Cost of revenues	4,144	74.6%	3,894	72.0%	13,052	67.0%	11,512	70.7%
Gross profit	1,409	25.4%	1,516	28.0%	6,422	33.0%	4,768	29.3%
SG&A expense	2,225	40.1%	2,351	43.5%	6,756	34.7%	6,451	39.6%
Depreciation and amortization	119	2.1%	107	2.0%	351	1.8%	331	2.0%
<b>Operating loss</b>	(935)	(16.8%)	(942)	(17.4%)	(685)	(3.5%)	(2,014)	(12.4%)
Other income	6	0.1%	6	0.1%	16	0.1%	22	0.1%
Loss before income taxes	(929)	(16.7%)	(936)	(17.3%)	(669)	(3.4%)	(1,992)	(12.2%)
Income tax expense	6	0.1%	19	0.4%	24	0.1%	30	0.2%
<b>Net loss</b>	<u>\$ (935)</u>	<u>(16.8%)</u>	<u>\$ (955)</u>	<u>(17.7%)</u>	<u>\$ (693)</u>	<u>(3.6%)</u>	<u>\$ (2,022)</u>	<u>(12.4%)</u>

**THREE MONTHS ENDED MARCH 31, 2014 AS COMPARED TO THREE MONTHS ENDED MARCH 31, 2013**

Total revenues for the three months ended March 31, 2014 of \$5.6 million increased by \$0.2 million, or 2.6%, over the total revenues for the three months ended March 31, 2013 of \$5.4 million. Billings by market are as follows (in thousands):

	Three-Months Ended March 31,		
	(Unaudited)		
	2014	2013	Variance
<b><u>BILLINGS BY MARKET:</u></b>			
Home Health Care	\$ 1,793	\$ 1,539	\$ 254
Retail	737	1,744	(1,007)
Professional	1,101	875	226
Pharmaceutical Manufacturer	528	339	189
Assisted Living	434	408	26
Environmental	280	69	211
Core Government	119	96	23
Other	300	186	114
Subtotal	5,292	5,256	36
GAAP Adjustment *	261	154	107
Revenue Reported	<u>\$ 5,553</u>	<u>\$ 5,410</u>	<u>\$ 143</u>

\*Represents the net impact of the revenue recognition adjustment required to arrive at reported generally accepted accounting principles ("GAAP") revenue. Customer billings include all invoiced amounts associated with products shipped during the period reported. GAAP revenue includes customer billings as well as numerous adjustments necessary to reflect, (i) the deferral of a portion of current period sales and (ii) recognition of certain revenue associated with products returned for treatment and destruction. The difference between customer billings and GAAP revenue is reflected in the Company's balance sheet as deferred revenue. See Note 3 "Revenue Recognition" in "Notes to Condensed Consolidated Financial Statements".

This quarter-to-date table contains certain financial information not derived in accordance with GAAP, including customer billings information. The Company believes this information is useful to investors and other interested parties as customer billings represents all invoiced amounts associated with products shipped during the period reported. Such information should not be considered as a substitute for any measures derived in accordance with GAAP, and may not be comparable to other similarly titled measures of other companies. Reconciliation of this information to the most comparable GAAP measures is included above.

Billings for the three months ended March 31, 2014 were relatively flat compared to the three months ended March 31, 2013. Billings increased in the Home Health Care (\$0.3 million), Professional (\$0.2 million), Environmental (\$0.2 million), and Pharmaceutical Manufacturer (\$0.2 million) markets. These increases in billings were offset by decreased billings in the Retail (\$1.0 million) market. The increase in Home Health Care market billings is due to timing of distributor purchases. The increase in Professional market billings is a result of continued targeted telemarketing initiatives and promotional activities to educate doctors, dentists, veterinarians and other healthcare professionals about the significant cost advantage and convenience of the Company's Sharps® Recovery mailback system when compared with the traditional pick-up service for the small quantity generator sector. In addition, the Professional market was positively impacted by joint marketing alliance-related business during the three months ended March 31, 2014. The increase in Environmental market billings was driven by focused marketing initiatives around third party treatment services which are starting to gain traction. The increase in the Pharmaceutical Manufacturer market billings is due to increased fulfillment activity in several patient support programs. The programs include the direct fulfillment of the Sharps® Recovery System to the pharmaceutical manufacturers' program participants which provides the proper containment, return, and treatment of the needles or injection devices utilized in therapy. The decrease in Retail market billings is primarily related to the timing of large flu shot orders for the upcoming flu season, which the Company expects to recognize in the June 2014 quarter rather than in the March quarter as occurred last year.

Cost of revenues for the three months ended March 31, 2014 of \$4.1 million was 74.6% of revenues. Cost of revenues for the three months ended March 31, 2013 of \$3.9 million was 72.0% of revenues. The lower gross margin for the three months ended March 31, 2014 of 25.4% (versus 28.0% for the three months ended March 31, 2013) was related primarily to a change in product and market mix.

Selling, general and administrative ("SG&A") expenses for the three months ended March 31, 2014 and 2013 was \$2.23 million and \$2.35 million, respectively. SG&A for the three months ended March 31, 2013 was negatively impacted by severance costs of \$0.2 million associated with a former officer of the Company.

The Company generated an operating loss of \$0.9 million for the three months ended March 31, 2014 and 2013. The operating margin was (16.8%) for the three months ended March 31, 2014 compared to (17.4%) for the three months ended March 31, 2013.

The Company generated a loss before income taxes of \$0.9 million for the three months ended March 31, 2014 and 2013.

The Company's effective tax rate for the three months ended March 31, 2014 and 2013 was (0.6%) and (2.0%), respectively, reflecting estimated state income taxes. The Company's net deferred tax assets have been fully reserved by a tax valuation allowance. The Company's tax benefit associated with taxable losses during the three months ended March 31, 2014 and 2013 was offset by a deferred tax valuation allowance.

The Company generated a net loss of \$0.9 million for the three months ended March 31, 2014 compared to a net loss of \$1.0 million for the three months ended March 31, 2013.

The Company reported diluted loss per share of (\$0.06) for both the three months ended March 31, 2014 and 2013.

**NINE MONTHS ENDED MARCH 31, 2014 AS COMPARED TO NINE MONTHS ENDED MARCH 31, 2013**

Total revenues for the nine months ended March 31, 2014 of \$19.5 million increased by \$3.2 million, or 19.6%, over the total revenues for the nine months ended March 31, 2013 of \$16.3 million. Billings by market are as follows (in thousands):

	<b>Nine-Months Ended March 31,</b>		
	<b>(Unaudited)</b>		
	<b>2014</b>	<b>2013</b>	<b>Variance</b>
<b><u>BILLINGS BY MARKET:</u></b>			
Home Health Care	\$ 5,534	\$ 4,845	\$ 689
Retail	4,421	4,343	78
Professional	3,880	2,826	1,054
Pharmaceutical Manufacturer	2,586	1,811	775
Assisted Living	1,280	1,160	120
Environmental	432	80	352
Core Government	369	596	(227)
Other	734	563	171
Subtotal	<u>19,236</u>	<u>16,224</u>	<u>3,012</u>
GAAP Adjustment *	238	56	182
Revenue Reported	<u>\$ 19,474</u>	<u>\$ 16,280</u>	<u>\$ 3,194</u>

\*Represents the net impact of the revenue recognition adjustment required to arrive at reported generally accepted accounting principles (“GAAP”) revenue. Customer billings include all invoiced amounts associated with products shipped during the period reported. GAAP revenue includes customer billings as well as numerous adjustments necessary to reflect, (i) the deferral of a portion of current period sales and (ii) recognition of certain revenue associated with products returned for treatment and destruction. The difference between customer billings and GAAP revenue is reflected in the Company’s balance sheet as deferred revenue. See Note 3 “Revenue Recognition” in “Notes to Condensed Consolidated Financial Statements”.

This year-to-date table contains certain financial information not derived in accordance with GAAP, including customer billings information. The Company believes this information is useful to investors and other interested parties as customer billings represents all invoiced amounts associated with products shipped during the period reported. Such information should not be considered as a substitute for any measures derived in accordance with GAAP, and may not be comparable to other similarly titled measures of other companies. Reconciliation of this information to the most comparable GAAP measures is included above.

The increase in billings was primarily attributable to increased billings in the Professional (\$1.1 million), Pharmaceutical Manufacturer (\$0.8 million), Home Health Care (\$0.7 million) and Environmental (\$0.4 million) markets. The increase in billings was partially offset by decreased billings in the Core Government (\$0.2 million) market. The increase in Professional market billings is a result of continued targeted telemarketing initiatives and promotional activities to educate doctors, dentists, veterinarians and other healthcare professionals about the significant cost advantage and convenience of the Company’s Sharps® Recovery mailback system when compared with the traditional pick-up service for the small quantity generator sector. In addition, the Professional market was positively impacted by joint marketing alliance-related business during the nine months ended March 31, 2014. The increase in Pharmaceutical Manufacturer market billings is due to the timing of customer orders including resupply orders from several patient support programs. The programs include the direct fulfillment of the Sharps® Recovery System to the pharmaceutical manufacturer’s program participants which provides the proper containment, return, and treatment of the needles or injection devices utilized in therapy. The increase in Home Health Care market billings is due to the timing of distributor purchases. The increase in Environmental market billings was driven by focused marketing initiatives around third party treatment services which are starting to gain traction. The decrease in Core Government billings was due to distributor sales of \$0.2 million in the prior year to a major U.S. agency to facilitate the launch of our solutions in selected military bases.

Cost of revenues for the nine months ended March 31, 2014 of \$13.1 million was 67.0% of revenues. Cost of revenues for the nine months ended March 31, 2013 of \$11.5 million was 70.7% of revenues. The higher gross margin for the nine months ended March 31, 2014 of 33.0% (versus 29.3% for the nine months ended March 31, 2013) was due to the leverage gained from higher revenue.

Selling, general and administrative (“SG&A”) expenses for the nine months ended March 31, 2014 and 2013 was \$6.8 million and \$6.5 million, respectively. SG&A for the nine months ended March 31, 2014 was negatively impacted by legal expenses of \$0.3 million related to our claim to the CDC related to the termination of the government contract and severance costs of \$0.1 million for a former officer of the Company. SG&A for the nine months ended March 31, 2013 was negatively impacted by severance costs of \$0.2 million for a former officer of the Company. Excluding these unusual items, SG&A expense increased \$0.1 million due to increased sales and marketing-related spending.

The Company generated an operating loss of \$0.7 million for the nine months ended March 31, 2014 compared to an operating loss of \$2.0 million for the nine months ended March 31, 2013. The operating margin was (3.5%) for the nine months ended March 31, 2014 compared to (12.4%) for the nine months ended March 31, 2013. The improvement in operating loss is a result of higher billings in the nine months ended March 31, 2014 along with an improved gross margin as a result of greater operating leverage gained from higher revenue (discussed above).

The Company generated a loss before income taxes of \$0.7 million for the nine months ended March 31, 2014 versus a loss before tax of \$2.0 million for the nine months ended March 31, 2013. The improvement in the loss before income tax is a result of an improvement in operating loss (discussed above).

The Company's effective tax rate for the nine months ended March 31, 2014 and 2013 was (3.6%) and (1.5%), respectively, reflecting estimated state income taxes. The Company's net deferred tax assets have been fully reserved by a tax valuation allowance. The Company's tax benefit associated with taxable losses during the nine months ended March 31, 2014 and the year ended June 30, 2013, was offset by a deferred tax valuation allowance.

The Company generated a net loss of \$0.7 million for the nine months ended March 31, 2014 compared to a net loss of \$2.0 million for the nine months ended March 31, 2013. The improvement in the net loss is a result of an improvement in operating loss (discussed above).

The Company reported diluted loss per share of (\$0.05) for the nine months ended March 31, 2014 versus diluted loss per share of (\$0.13) for the nine months ended March 31, 2013. The improvement in diluted loss per share is a result of an improvement in net loss in the nine months ended March 31, 2014 as compared to the prior year (discussed above).

## **PROSPECTS FOR THE FUTURE**

The Company continues to take advantage of the many opportunities in the markets served as professional offices, retail pharmacies and clinics, communities, assisted living and long-term care facilities, home healthcare companies, consumers, pharmaceutical manufacturers, government agencies, health care facilities, individual self-injectors and commercial organizations become more aware of alternatives to the traditional methods of management of medical sharps waste, used healthcare materials and unused dispensed medications.

The Company's growth strategies are focused on the Retail, Pharmaceutical Manufacturer, Professional, Assisted Living, Home Health Care and Core Government markets. The Company believes its growth opportunities are supported by:

- An increase in the number of used needles improperly disposed of outside the large healthcare setting and into the solid waste system to 7.8 billion each year (tripled volume over the past ten years) and an increase in the number of self-injectors in the country to 13.5 million over the same period;
- An estimated 800,000 doctors, dentists, veterinarians, clinics, tattoo parlors and other businesses in the country that generate smaller quantities of medical waste, including used syringes to whom we offer a lower cost alternative to the traditional pick-up service. The Company addresses this market from two directions: (i) field sales which focuses on larger dollar and nation-wide opportunities where we can utilize the JMA with Daniels Sharpsmart to integrate the route-based pick-up service along with our mailback solutions to create a comprehensive medical waste management offering and (ii) inside and online sales which focus on the individual or small group professional offices;
- An estimated 40% of the four billion dispensed medication prescriptions which go unused every year in the United States generating an estimated 200 million pounds of unused medication waste;
- The pace of regulation of sharps and unused dispensed medications disposal which is gaining momentum at both the state and federal level; as of June 30, 2013, approximately 46 percent of U.S. citizens live in states that have enacted legislation or strict guidelines mandating the proper disposal of home generated used syringes while 67 percent live in states that have enacted or proposed legislation mandating the proper disposal of home generated dispensed unused medications. Further, since 2009, the federal government, nine states and several counties have introduced legislation requiring manufacturer responsibility for consumer generated unused medications. State regulatory agencies are also addressing this issue within the regulated industry. Multiple states now require healthcare providers to avoid sewer and trash disposal of non-hazardous unused medications within their facilities. States such as California, Washington and Minnesota have required assessment and proper treatment by a medical waste disposal company for years. However, other states such as Colorado and Florida are now requiring even small healthcare providers to segregate unused medications for proper disposal. In addition, states are beginning to more closely scrutinize generators returning through reverse distribution unused medications that are actually waste pharmaceuticals and should be disposed of as such;

- The number of U.S. retail clinics is projected to double between 2011 and 2015, expecting business to increase 20%-25% per year, driven by the increasing demand of newly insured patients under healthcare reform as well as patients looking for more convenient care. The two leading retail pharmacies in the country are emphasizing their efforts to grow their capability as a low cost provider of health care services for non-chronic conditions. The number of pharmacists nationwide trained to deliver vaccines has quadrupled since 2007. Vaccines offered in retail clinics include seasonal flu programs as well as year round programs for pneumococcus, shingles, pediatric immunizations, HPV and international travel;
- The changing demographics of the U.S. population - one out of five Americans will be 65 years or older by 2030, which will increase the need for cost-effective medical waste management solutions especially in the home healthcare and assisted living markets;
- The change in delivery of healthcare (more health care being administered in an alternate site) as well as uncertainty created by the current state of healthcare – facts which are driving more healthcare providers to increase efficiencies and reduce costs;
- The Company's JMA with Daniels Sharpsmart, announced in May 2012, to serve the entire U.S. medical waste market, offering clients a blended product portfolio to effectively target prospective customers with multi-site and multi-sized locations including those that generate larger quantities of medical waste. The JMA has had a significant positive impact on our pipeline of sales opportunities – over 60% of this pipeline is attributable to alliance-type opportunities providing comprehensive medical waste management service offerings where both the mailback and pick-up service are integrated into the offering;
- New solution offerings including the Complete Needle™ Collection and Disposal System (designed for the traditional under-served home self-injector), the TakeAway line of products for unused medications (including TakeAway Environmental Return System™), the Medical/Professional TakeAway Recovery System and enhanced patient support programs with pharmaceutical manufacturers; and
- The Company's strong financial position with a cash balance of \$14.4 million and no debt as of March 31, 2014.

## **LIQUIDITY AND CAPITAL RESOURCES**

### **Cash Flow**

Cash and cash equivalents decreased by \$1.1 million to \$14.4 million at March 31, 2014 from \$15.5 million at June 30, 2013. The decrease in cash and cash equivalents is primarily due to repurchased shares of \$0.6 million and capital expenditures and additions to intangible assets of \$0.4 million.

Accounts receivable increased by \$0.4 million to \$3.0 million at March 31, 2014 from \$2.6 million at June 30, 2013. The increase is due to timing of billings and collections.

Inventory decreased by \$0.2 million to \$1.4 million at March 31, 2014 from \$1.6 million at June 30, 2013. The decrease in inventory is due to timing of sales and adjustment of inventory levels to facilitate customer orders.

Working capital decreased \$0.7 million to \$15.9 million at March 31, 2014 from \$16.6 million at June 30, 2013. The decrease is primarily due to reductions in cash and cash equivalents and inventory offset by an increase to accounts receivable (discussed above).

Property, plant and equipment decreased \$0.5 million to \$3.95 million at March 31, 2014 from \$4.4 million at June 30, 2013. Depreciation expense was \$0.8 million, partially offset by capital expenditures of \$0.3 million. The capital expenditures are attributable primarily to treatment facility improvements of \$0.2 million.

Stockholders' equity decreased by \$1.0 million to \$20.1 million at March 31, 2014 from \$21.1 million at June 30, 2013. This decrease is primarily attributable to a net loss of \$0.7 million and stock repurchases of \$0.6 million offset in part by stock-based compensation of \$0.3 million.

## Off -Balance Sheet Arrangements

The Company was not a party to any off-balance sheet transactions as defined in Item 303 of Regulation S-K for the nine months ended March 31, 2014 and the year ended June 30, 2013.

## Credit Facility

On January 28, 2014, the Company entered into a credit agreement with a commercial bank (“Credit Agreement”). The Credit Agreement, which replaces the prior credit agreement executed effective April 30, 2013 with another commercial bank (“Prior Credit Agreement”), provides for a two-year, \$3.0 million line of credit facility, the proceeds of which may be utilized for working capital, letters of credit (up to \$500,000) and general corporate purposes. Indebtedness under the Credit Agreement is secured by the Company’s accounts receivable and inventory with advances outstanding at any time limited to a Borrowing Base (as defined in the Credit Agreement) equal to 80% of eligible accounts receivable plus 50% of eligible inventory. Borrowings bear interest at WSJ Prime, which we estimate to be approximately 3.25% as of March 31, 2014. The Company will pay a fee of 0.25% per annum on the unused amount of the line of credit. As of March 31, 2014, the Company had no outstanding borrowings, other than \$335 thousand in letters of credit, which leaves \$2.7 million of credit available.

The Credit Agreement contains affirmative and negative covenants that, among other things, require the Company to maintain a minimum level of tangible net worth of \$10.5 million and minimum liquidity of \$5.0 million. The Company is in compliance with all the financial covenants as of March 31, 2014. The Credit Agreement, which expires on January 28, 2016, also contains customary events of default which, if uncured, may terminate the Credit Agreement and require immediate repayment of all indebtedness to the lenders.

The Prior Credit Agreement, which was effective through January 28, 2014, provided for a cash-collateralized \$200,000 line of credit facility with a maturity date of July 15, 2015. No amounts related to the Prior Credit Agreement were outstanding as of March 31, 2014 other than letters of credit of approximately \$110 thousand, which are in the process of being released.

Management believes that the Company’s current cash resources (cash on hand) will be sufficient to fund operations for the twelve months ending March 31, 2015.

## CRITICAL ACCOUNTING ESTIMATES

**Revenue Recognition:** The Company recognizes revenue from product sales when goods are shipped or delivered, and title and risk of loss pass to the customer except for those sales via multiple-deliverable arrangements. Provisions for certain rebates, product returns and discounts to customers are accounted for as reductions in sales in the same period the related sales are recorded. Product discounts granted are based on the terms of arrangements with direct, indirect and other market participants, as well as market conditions, including prices charged by competitors. Rebates are estimated based on contractual terms, historical experience, trend analysis and projected market conditions in the various markets served.

The Company recognizes revenue in accordance with guidance on revenue recognition of multiple-deliverable arrangements. Under this guidance, certain products offered by the Company have revenue producing components that are recognized over multiple delivery points (Sharps Recovery System™ (formerly the Sharps Disposal by Mail Systems®) and various TakeAway Environmental Return Systems™ referred to as “Mailbacks” and Sharps® Pump and Asset Return Boxes, referred to as “Pump Returns”) and can consist of up to three separate elements, or units of measure, as follows: (1) the sale of the compliance and container system, (2) return transportation and (3) treatment service.

In accordance with the relative selling price methodology, an estimated selling price is determined for all deliverables that qualify for separate units of accounting. The actual consideration received in a multiple-deliverable arrangement is then allocated to the units based on their relative sales price. The selling price for the transportation revenue and the treatment revenue utilizes third party evidence. The Company estimates the selling price of the compliance and container system based on the product and services provided including compliance with local, state and Federal laws, adherence to stringent manufacturing and testing requirements, safety to the patient and the community as well as storage and containment capabilities.

Revenue for the sale of the compliance and container is recognized upon delivery to the customer, at which time the customer takes title and assumes risk of ownership. Transportation revenue is recognized when the customer returns the compliance and container system and the container has been received at the Company's owned or contracted facilities. The compliance and container system is mailed or delivered by an alternative logistics provider to the Company's owned or contracted facilities. Treatment revenue is recognized upon the destruction or conversion and proof of receipt and treatment having been performed on the container. Since the transportation element and the treatment elements are undelivered services at the point of initial sale of the compliance and container, transportation and treatment revenue is deferred until the services are performed. The current and long-term portions of deferred revenues are determined through regression analysis and historical trends. Furthermore, through regression analysis of historical data, the Company has determined that a certain percentage of all compliance and container systems sold may not be returned. Accordingly, a portion of the transportation and treatment elements are recognized at the point of sale.

**Income Taxes:** The liability method is used in accounting for deferred income taxes. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. A valuation allowance is established when it is more likely than not that some portion or all of the deferred tax assets will not be realized. The establishment of valuation allowances and development of projected annual effective tax rates requires significant judgment and is impacted by various estimates. Both positive and negative evidence, as well as the objectivity and verifiability of that evidence, is considered in determining the appropriateness of recording a valuation allowance on deferred tax assets.

## **RECENTLY ISSUED ACCOUNTING STANDARDS**

There are no recently issued accounting pronouncements that will have a significant impact on the Company's consolidated financial statements as of March 31, 2014.

## **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The Company does not have exposure to significant financial market risk including commodity price risk, foreign currency exchange risk or interest rate risk. Management does not use derivative instruments. The Company has limited exposure to changes in interest rates due to its lack of indebtedness. The Company maintains a credit agreement under which we may borrow funds in the future. Currently, the Company does not foresee any borrowing needs.

## **ITEM 4. CONTROLS AND PROCEDURES**

### **Evaluation of Disclosure Controls and Procedures**

The Company maintains "disclosure controls and procedures", as such term is defined in Rule 13a-15(e) under the Exchange Act, that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms, and that such information is accumulated and communicated to management, including, the Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO") as appropriate, to allow timely decisions regarding required disclosure.

As of March 31, 2014, the Company conducted an evaluation (the "Evaluation"), under the supervision and with the participation of the CEO and CFO, of the effectiveness of the design and operation of our disclosure controls and procedures ("Disclosure Controls"), pursuant to Rules 13a-15(e) and 15d-15(e) of the Exchange Act. Based upon this Evaluation, the CEO and CFO concluded that our Disclosure Controls were effective as of March 31, 2014.

### **Changes in Internal Control over Financial Reporting**

During the quarterly period ended March 31, 2014, there were no changes in the Company's internal controls over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act), that have materially affected, or are reasonably likely to materially affect the Company's internal control over financial reporting.

### **CEO and CFO Certifications**

Appearing immediately following the Signatures section of this report are certifications of the CEO and the CFO. The Certifications are required in accordance with Section 302 of the Sarbanes-Oxley Act of 2002 (the Section 302 Certifications). This item of this quarterly report on Form 10-Q, which you are currently reading, is the information concerning the Evaluation referred to in the Section 302 Certification and this information should be read in conjunction with the Section 302 Certifications for a more complete understanding of the topics presented.

## **PART II – OTHER INFORMATION**

### **ITEM 1. LEGAL PROCEEDINGS**

The Company is involved in legal proceedings and litigation in the ordinary course of business. In the opinion of management, the outcome of such matters will not have a material adverse effect on the Company's consolidated financial position or consolidated results of operations.

### **ITEM 1A. RISK FACTORS**

Refer to Item 1A. Risk Factors in the Company's annual report on Form 10-K for the year ended June 30, 2013 for the Company's risk factors. During the nine months ended March 31, 2014, there have been no changes to the Company's risk factors.

### **ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.**

#### **Recent Sales of Unregistered Securities.**

**None.**

#### **Issuer Purchases of Equity Securities.**

On January 7, 2013, the Company announced that its Board of Directors approved a stock repurchase program effective January 3, 2013, authorizing the Company to repurchase in the aggregate up to \$3 million of its outstanding common stock over a two-year period. The shares would be purchased from time to time on the open market or in privately negotiated transactions, at the Company's discretion, in each case, in compliance with Rule 10b-18 under the Securities Exchange Act of 1934, as amended, subject to market and business conditions, applicable legal requirements, explicit black-out dates and other factors. The purchases will be funded using the Company's available cash balances and cash generated from operations. The program does not obligate the Company to acquire any particular amount of common stock and may be modified, suspended or terminated at any time at the Company's discretion in accordance with Rule 10b-18.

During the three months ended March 31, 2014, Sharps repurchased no shares. As of March 31, 2014, approximately \$2.3 million remained of our \$3.0 million repurchase program.

### **ITEM 6. EXHIBITS**

(a) Exhibits:

[31.1](#) Certification of Chief Executive Officer in accordance with Section 302 of the Sarbanes-Oxley Act (filed herewith)

[31.2](#) Certification of Chief Financial Officer in accordance with Section 302 of the Sarbanes-Oxley Act (filed herewith)

[32.1](#) Certification of Chief Executive Officer in accordance with Section 906 of the Sarbanes-Oxley Act (filed herewith)

[32.2](#) Certification of Chief Financial Officer in accordance with Section 906 of the Sarbanes-Oxley Act (filed herewith)

101.INS XBRL Instance Document (filed herewith)

101.SCH XBRL Taxonomy Extension Schema Document (filed herewith)

101.CAL XBRL Taxonomy Extension Calculation Linkbase Document (filed herewith)

101.DEF XBRL Taxonomy Extension Linkbase Document (filed herewith)

101.LAB XBRL Taxonomy Extension Label Linkbase Document (filed herewith)

101.PRE XBRL Taxonomy Extension Presentation Linkbase Document (filed herewith)

**ITEMS 3, 4 AND 5 ARE NOT APPLICABLE AND HAVE BEEN OMITTED.**

## SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Dated: May 8, 2014

REGISTRANT:  
SHARPS COMPLIANCE CORP.

By: /s/ DAVID P. TUSA

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David P. Tusa  
Chief Executive Officer and President  
(Principal Executive Officer)

Dated: May 8, 2014

By: /s/ DIANA P. DIAZ

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Diana P. Diaz  
Vice President and Chief Financial Officer  
(Principal Financial and Accounting Officer)

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER  
IN ACCORDANCE WITH SECTION 302 OF THE SARBANES-OXLEY ACT**

I, David P. Tusa, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Sharps Compliance Corp.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Date: May 8, 2014

/s/David P. Tusa  
Chief Executive Officer and President  
(Principal Executive Officer)

**CERTIFICATION OF CHIEF FINANCIAL OFFICER  
IN ACCORDANCE WITH SECTION 302 OF THE SARBANES-OXLEY ACT**

I, Diana P. Diaz, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Sharps Compliance Corp.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Date: May 8, 2014

/s/Diana P. Diaz  
Vice President and Chief Financial Officer  
(Principal Financial and Accounting Officer)

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER  
IN ACCORDANCE WITH SECTION 906 OF THE SARBANES-OXLEY ACT**

In connection with the quarterly report of Sharps Compliance Corp. (the "Company") on Form 10-Q for the three and nine months ended March 31, 2014, as filed with the Securities and Exchange Commission on the date hereof, I, David P. Tusa, Chief Executive Officer and President of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to the best of my knowledge that:

- (1) The Form 10-Q report for the three and nine months ended March 31, 2014, filed with the Securities and Exchange Commission on May 8, 2014 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Form 10-Q report for the three and nine months ended March 31, 2014 fairly presents, in all material respects, the financial condition and results of operations of Sharps Compliance Corp.

Date: May 8, 2014

/s/David P. Tusa  
Chief Executive Officer and President

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**CERTIFICATION OF CHIEF FINANCIAL OFFICER  
IN ACCORDANCE WITH SECTION 906 OF THE SARBANES-OXLEY ACT**

In connection with the quarterly report of Sharps Compliance Corp. (the "Company") on Form 10-Q for the three and nine months ended March 31, 2014, as filed with the Securities and Exchange Commission on the date hereof, I, Diana P. Diaz, Vice President and Chief Financial Officer, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to the best of my knowledge that:

- (1) The Form 10-Q report for the three and nine months ended March 31, 2014, filed with the Securities and Exchange Commission on May 8, 2014, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Form 10-Q report for the three and nine months ended March 31, 2014 fairly presents, in all material respects, the financial condition and results of operations of Sharps Compliance Corp.

Date: May 8, 2014

/s/Diana P. Diaz  
Vice President and Chief Financial Officer