HUDSON TECHNOLOGIES INC /NY
Form 10-Q
November 04, 2008

UNITED STATES

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 September 30, 2008

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 1-13412

Hudson Technologies, Inc.

(Exact name of registrant as specified in its charter)

New York	13-3641539
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
P.O. Box 1541 One Blue Hill Plaza Pearl River, New York	10965
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code (845) 735-6000

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes [X] No [ ]

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

Large accelerated filer	[ ]	Accelerated filer	[ ]
Non-accelerated filer (do not check if a smaller reporting company)	[ ]	Smaller reporting company	[X]

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

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date:

Common stock, $0.01 par value	19,416,187 shares
Class	Outstanding at October 31, 2008

Hudson Technologies, Inc.

Index

Part I - FINANCIAL INFORMATION

Hudson Technologies, Inc. and subsidiaries

Consolidated Balance Sheets

(Amounts in thousands, except for share and par value amounts)

	September 30, 2008 (unaudited)	December 31, 2007
Assets		
Current assets:		
Cash and cash equivalents	$ 740	$ 283
Trade accounts receivable - net of allowance for doubtful accounts of $323 and $276	2,641	1,746
Inventories	18,877	12,602
Prepaid expenses and other current assets	376	242
Total current assets	22,634	14,873
Property, plant and equipment, less accumulated depreciation and amortization	2,972	2,881
Other assets	110	46
Deferred tax assets	4,120	1,520
Intangible assets, less accumulated amortization	66	66
Total Assets	$29,902	$19,386
	========	========
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable and accrued expenses	$ 3,644	$ 3,568
Accrued payroll	794	638
Short-term debt and current maturities of long-term debt	6,118	3,124
Total current liabilities	10,556	7,330
Long-term debt, less current maturities	5,932	6,493
Total Liabilities	16,488	13,823
Commitments and contingencies		
Stockholders' equity:		
Preferred stock shares authorized 5,000,000		
Series A Convertible Preferred stock, $.01 par value ($100 liquidation preference value); shares authorized 150,000	--	--
Common stock, $0.01 par value; shares authorized 50,000,000 issued and outstanding 19,416,187 and 19,072,264	194	191
Additional paid-in capital	35,708	35,349
Accumulated deficit	(22,488)	(29,977)
Total Stockholders' Equity	13,414	5,563

Total Liabilities and Stockholders' Equity	$29,902	$19,386
	=========	=========

See accompanying Notes to the Consolidated Financial Statements.

Hudson Technologies, Inc. and subsidiaries

Consolidated Statements of Operations

(unaudited)

(Amounts in thousands, except for share and per share amounts)

	Three month period ended September 30,		Nine month period ended September 30,	
	2008	2007	2008	2007
Revenues	$5,841	$4,738	$30,296	$24,162
Cost of sales	3,917	3,131	19,632	18,048
Gross Profit	1,924	1,607	10,664	6,114
Operating expenses:				
Selling and marketing	510	352	1,629	1,240
General and administrative	772	664	2,531	2,237
Compensation expense for stock purchases	--	--	--	4,338
Total operating expenses	1,282	1,016	4,160	7,815
Operating income (loss)	642	591	6,504	(1,701)
Other income (expense):				
Interest expense	(299)	(235)	(868)	(540)
Interest income	1	4	3	15
Total other income (expense)	(298)	(231)	(865)	(525)
Income (loss) before income taxes	344	360	5,639	(2,226)
Income tax provision (benefit)	(2,395)	3	(1,851)	(1,251)
Net income (loss)	$2,739	$ 357	$7,490	($ 975)
	=========	=========	=========	=========
Net income (loss) per common share - Basic	$0.14	$0.02	$0.39	($0.04)
	======	======	======	======

Net income (loss) per common share - Diluted	$0.13	$0.02	$0.36	($0.04)
	======	======	======	======
Weighted average number of shares outstanding - Basic				
	19,409,761	20,234,664	19,262,425	24,021,864
	==========	==========	==========	==========
Weighted average number of shares outstanding - Diluted				
	20,979,713	20,400,704	20,523,254	24,021,864
	==========	==========	==========	==========

See accompanying Notes to the Consolidated Financial Statements

Hudson Technologies, Inc. and subsidiaries

Consolidated Statements of Cash Flows

Increase (Decrease) in Cash and Cash Equivalents

(unaudited)

(Amounts in thousands)

	Nine month period ended September 30,	
	2008	2007
Cash flows from operating activities:		
Net income (loss)	$7,490	($975)
Adjustments to reconcile net income (loss)		
to cash provided (used) by operating activities:		
Depreciation and amortization	407	408
Allowance for doubtful accounts	61	37
Issuance of stock options for services	17	74
Compensation expense for stock purchases	--	4,338

Deferred tax benefit	(2,600)	(1,268)
Changes in assets and liabilities:		
Trade accounts receivable	(956)	(1,750)
Inventories	(6,275)	2,933
Prepaid expenses and other current assets	(134)	(93)
Other assets	(64)	(10)
Accounts payable and accrued expenses	232	(1,570)
Cash provided (used) by operating activities	(1,822)	2,124
Cash flows from investing activities:		
Additions to patents	(21)	(13)
Additions to property, plant, and equipment	(477)	(335)
Cash used by investing activities	(498)	(348)
Cash flows from financing activities:		
Purchase of common stock - net	--	(5,332)
Issuance of common stock - net	344	--
Proceeds (repayment) from short-term debt - net	2,982	(2,935)
Repayment of long-term debt	(849)	(628)
Proceeds of long-term debt	300	7,000
Cash provided (used) by financing activities	2,777	(1,895)
Increase (decrease) in cash and cash equivalents	457	(119)
Cash and cash equivalents at beginning of period	283	593
Cash and cash equivalents at end of period	$740	$474
	======	======

Supplemental disclosure of cash flow information:		
Cash paid during period for interest	$916	$540
Cash paid for income taxes	$220	$ 24
Supplemental disclosure of non-cash investing and financing activities		
Deferred financing costs	$ 48	$ --

See accompanying Notes to the Consolidated Financial Statements.

Hudson Technologies, Inc. and subsidiaries

Notes to the Consolidated Financial Statements

Note 1 - Summary of significant accounting policies

Business

Hudson Technologies, Inc., incorporated under the laws of New York on January 11, 1991, is a refrigerant services company providing innovative solutions to recurring problems within the refrigeration industry. The Company's products and services are primarily used in commercial air conditioning, industrial processing and refrigeration systems, including (i) refrigerant sales, (ii) refrigerant management services consisting primarily of reclamation of refrigerants and (iii) RefrigerantSide® Services performed at a customer's site, consisting of system decontamination to remove moisture, oils and other contaminants. In addition, RefrigerantSide® Services includes predictive and diagnostic services for industrial and commercial refrigeration applications, which are designed to predict potential catastrophic problems and identify inefficiencies in an operating system. The Company's Chiller Chemistry®, Chill Smart®, Fluid Chemistry ™, and Performance Optimization are predictive and diagnostic service offerings. The Company operates through its wholly-owned subsidiary, Hudson Technologies Company unless the context requires otherwise, reference to the "Company", "Hudson", "We", "Us", "Our", or similar pronouns refer to Hudson Technologies, Inc. and subsidiaries.

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial statements and with the instructions of Regulation S-X. Accordingly, they do not include all the information and footnotes required by generally accepted accounting principles for complete financial statements. The financial information included in the quarterly report should be read in conjunction with the Company's audited financial statements and related notes thereto for the year ended December 31, 2007. Operating results for the nine month period ended September 30, 2008 are not necessarily indicative of the results that may be expected for the fiscal year ending December 31, 2008.

In the opinion of management, all estimates and adjustments considered necessary for a fair presentation have been included and all such adjustments were normal and recurring.

Consolidation

The consolidated financial statements represent all companies of which Hudson directly or indirectly has majority ownership or otherwise controls. Significant intercompany accounts and transactions have been eliminated. The Company's consolidated financial statements include the accounts of wholly-owned subsidiaries Hudson Holdings, Inc. and Hudson Technologies Company.

Fair value of financial instruments

The carrying values of financial instruments including trade accounts receivable and accounts payable approximate fair value at September 30, 2008, because of the relatively short maturity of these instruments. The carrying value of short-and long-term debt approximates fair value, based upon quoted market rates of similar debt issues, as of September 30, 2008 and December 31, 2007.

Credit risk

Financial instruments, which potentially subject the Company to concentrations of credit risk, consist principally of temporary cash investments and trade accounts receivable. The Company maintains its temporary cash investments in highly-rated financial institutions and, at times, the balances exceed FDIC insurance coverage. The Company's trade accounts receivables are primarily due from companies throughout the United States. The Company reviews each customer's credit history before extending credit.

The Company establishes an allowance for doubtful accounts based on factors associated with the credit risk of specific accounts, historical trends, and other information. The carrying value of the Company's accounts receivable is reduced by the established allowance for doubtful accounts. The allowance for doubtful accounts includes any accounts receivable balances that are determined to be uncollectible, along with a general reserve for the remaining accounts receivable balances. The Company adjusts its general or specific reserves based on factors that affect the collectability of the accounts receivable balances.

For the nine month period ended September 30, 2008, one customer accounted for approximately 10% of the Company's revenues. For the nine month period ended September 30, 2007, one customer accounted for approximately 13% of the Company's revenues.

The loss of a principal customer or a decline in the economic prospects of and/or a reduction in purchases of the Company's products or services by any such customer could have an adverse effect on the Company's future financial position and results of operations.

Cash and cash equivalents

Temporary investments with original maturities of ninety days or less are included in cash and cash equivalents.

Inventories

Inventories, consisting primarily of refrigerant products available for sale, are stated at the lower of cost, on a first-in first-out basis, or market.

Property, plant, and equipment

Property, plant, and equipment are stated at cost, including internally manufactured equipment. The cost to complete equipment that is under construction is not considered to be material to the Company's financial position. Provision for depreciation is recorded (for financial reporting purposes) using the straight-line method over the useful lives of the respective assets. Leasehold improvements are amortized on a straight-line basis over the shorter of economic life or terms of the respective leases. Costs of maintenance and repairs are charged to expense when incurred.

Due to the specialized nature of the Company's business, it is possible that the Company's estimates of equipment useful life periods may change in the future.

Revenues and cost of sales

Revenues are recorded upon completion of service or product shipment and passage of title to customers in accordance with contractual terms. The Company evaluates each sale to ensure collectability. In addition, each sale is based on an arrangement with the customer and the sales price to the buyer is fixed. License fees are recognized over the period of the license based on the respective performance measurements associated with the license. Royalty revenues are recognized when earned. Cost of sales is recorded based on the cost of products shipped or services performed and related direct operating costs of the Company's facilities. To the extent that the Company charges its customers shipping fees such amounts are included as a component of revenue and the corresponding costs are included as a component of cost of sales.

The Company's revenues are derived from refrigerant and reclamation sales and RefrigerantSide® Services, including license and royalty revenues. The revenues for each of these lines are as follows:

Nine Month Period Ended September 30,	2008	2007
(in thousands, unaudited)		
Refrigerant and reclamation sales	$27,509	$21,331
RefrigerantSide® Services	2,787	2,831
Total	$30,296	$24,162

Income taxes

The Company utilizes the asset and liability method for recording deferred income taxes, which provides for the establishment of deferred tax asset or liability accounts based on the difference between tax and financial reporting bases of certain assets and liabilities. The tax benefit associated with the Company's net operating loss carry forwards ("NOL's") is recognized to the extent that the Company is expected to recognize future taxable income. The Company has assessed the recoverability of its deferred tax assets based on its expectation that it will recognize future taxable income and accordingly has adjusted its valuation allowance for this asset. During the three months ended September 30, 2008, the Company recognized $2,600,000 of additional income tax benefit in connection with its deferred tax asset. As of September 30, 2008, the total deferred tax asset is $4,120,000.

Certain states either do not allow or limit NOL's and as such the Company will be liable for certain state taxes. To the extent that the Company utilizes its NOL's, it will not pay tax on such amount but will be subject to the federal alternative minimum tax. In addition, to the extent that the Company's net income, if any, exceeds the annual NOL limitation it will pay income taxes based on the existing statutory rates.

As a result of an Internal Revenue Service audit, the 2006 and prior tax years have been closed. The Company operates in many states throughout the United States and, as of September 30, 2008, the various states statute of limitations remain open for tax years subsequent to 2003.

On June 28, 2007, Fleming U.S. Discovery Fund III, L.P. and Fleming U.S. Offshore Discovery Fund III, L.P. (individually and collectively "Fleming Funds") sold a total of approximately 14,900,000 shares of Hudson's common stock in a series of transactions involving the Company and certain members of the Company's management (the "Transactions"). Prior to the Transactions, the Fleming Funds owned in the aggregate approximately 19,100,000 shares, or 74% of the Company's outstanding common stock. Under Section 382 of the Internal Revenue Code of 1986, ("Code") as amended, the sale by Fleming Funds of their shares resulted in a "change in control", which limits the Company's ability to utilize its existing NOL's to approximately $1,300,000 annually.

Income (loss) per common and equivalent shares

If dilutive, common equivalent shares (common shares assuming exercise of options and warrants) utilizing the treasury stock method are considered in the presentation of dilutive earnings per share. The reconciliation of earnings per share is as follows (amounts in 000's):

	Three month period ended September 30,		Nine month period ended September 30,	
	2008	2007	2008	2007
Net Income (loss) - basic and diluted	$2,739	$357	$7,490	($975)
	======	======	======	======
Weighted average number of shares - basic	19,409,761	20,234,664	19,262,425	24,021,864
Shares underlying warrants	83,919	21,502	66,987	--
Shares underlying options	1,486,033	144,538	1,193,842	--
Weighted average number of shares outstanding- diluted	20,979,713	20,400,704	20,523,254	24,021,864

Estimates and risks

The preparation of financial statements in conformity with generally accepted accounting principles in the United States requires management to make estimates and assumptions that affect reported amounts of certain assets and liabilities, the disclosure of contingent assets and liabilities, and the results of operations during the reporting period. Actual results could differ from these estimates.

The Company participates in an industry that is highly regulated, changes in which could affect operating results. Currently the Company purchases virgin, hydrochlorofluorocarbon ("HCFC") and hydroflourocarbon ("HFC") refrigerants and reclaimable, primarily, HCFC and chlorofluorocarbon ("CFC") refrigerants from suppliers and its customers. Effective January 1, 1996, the Clean Air Act (the "Act") prohibited the production of CFC refrigerants and limited the production of HCFC refrigerants. Additionally, effective January 2004, the Act further limited the production of HCFC refrigerants and federal regulations were enacted which impose limitations on the importation of certain virgin HCFC refrigerants. Under the Act, production of certain HCFC refrigerants are scheduled to be phased out during the period 2010 through 2020, and production of all HCFC refrigerants is scheduled to be phased out by 2030. Notwithstanding the limitations under the Act, the Company believes that sufficient quantities of new and used refrigerants will continue to be available to it at a reasonable cost for the foreseeable future. To the extent that the Company is unable to source sufficient quantities of refrigerants or is unable to obtain refrigerants on commercially reasonable terms or experiences a decline in demand for refrigerants, the Company could realize reductions in refrigerant processing and possible loss of revenues, which would have a material adverse affect on operating results.

The Company is subject to various legal proceedings. The Company assesses the merit and potential liability associated with each of these proceedings. In addition, the Company estimates potential liability, if any, related to these matters. To the extent that these estimates are not accurate, or circumstances change in the future, the Company could realize liabilities, which would have a material adverse effect on operating results and its financial position.

Impairment of long-lived assets and long-lived assets to be disposed of

The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of the assets to the future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less the cost to sell.

Recent accounting pronouncements

In September 2006, the Financial Accounting Standards Board ("FASB") issued FASB statement No. 157 ("SFAS No. 157"), "Fair Value Measurements," which establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. SFAS No. 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The FASB agreed to defer the effective date of SFAS No. 157 for one year for non-financial assets and non-financial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis. There is no deferral for financial assets and financial liabilities, nor for the rare non-financial assets and non-financial liabilities that are remeasured at fair value at least annually. The adoption of SFAS No. 157 did not have a material impact on the Company's results of operations or its financial position.

Note 2 - Share-based compensation

Share-based compensation represents the cost related to share-based awards, typically stock options, granted to employees, non-employees, officers and directors. Share-based compensation is measured at grant date, based on the estimated fair value of the award, and such amount is charged to compensation expense on a straight-line basis (net of estimated forfeitures) over the requisite service period. For the nine month period ended September 30, 2008 and 2007, the share-based compensation expense of $17,000 and $74,000, respectively, is reflected in general and administrative expenses in the consolidated statements of operations.

Share-based awards have historically been stock options issued pursuant to the terms of the Company's 1994 and 1997 stock option plans and the Company's 2004 and 2008 stock option incentive plans (the "Plans"), described below. The Plans may be administered by the Board of Directors or the Compensation and Stock Option Committee of the Board, or by another committee appointed by the Board from among its members as provided in the Plans. Presently, the Plans are administered by a committee consisting of non-employee directors. As of September 30, 2008, the Plans authorized the issuance of stock options to purchase an aggregate of 5,500,000 shares of the Company's common stock and, as of September 30, 2008 there were 3,360,000 shares of the Company's common stock available for issuance for future stock option grants.

Stock options are awards, which allow the recipient to purchase shares of the Company's common stock at a fixed price, are typically granted at an exercise price equal to the Company's stock price at the date of grant. Typically, the Company's stock option awards have vested from immediately to two years from the grant date and have had a contractual term ranging from five to ten years.

During the nine month period ended September 30, 2008 and 2007, the Company issued stock options of 220,000 and none, respectively, and the fair value of these awards was $133,000 and none, respectively. At September 30, 2008, there was $116,000 of unrecognized compensation cost related to non-vested previously granted option awards.

Effective October 31, 1994, the Company adopted an Employee Stock Option Plan ("1994 Plan") pursuant to which 725,000 shares of common stock were reserved for issuance upon the exercise of options designated as either (i) options intended to constitute incentive stock options ("ISOs") under the Internal Revenue Code of 1986, as amended, ("Code") or (ii) nonqualified options. ISOs could have been granted under the 1994 Plan to employees and officers of the Company. Non-qualified options could have been granted to consultants, directors (whether or not they are employees), employees or officers of the Company. Effective November 1, 2004, the Company's ability to grant options under the 1994 Plan expired.

Effective July 25, 1997, the Company adopted its 1997 Employee Stock Option Plan, which was amended on August 19, 1999, ("1997 Plan") pursuant to which 2,000,000 shares of common stock were reserved for issuance upon the exercise of options designated as either (i) ISOs under the Code, or (ii) nonqualified options. ISOs could have been granted under the 1997 Plan to employees and officers of the Company. Non-qualified options could have been granted to consultants, directors (whether or not they are employees), employees or officers of the Company. Effective September 11, 2007, the Company's ability to grant options under the 1997 Plan expired.

Effective September 10, 2004, the Company adopted its 2004 Stock Incentive Plan ("2004 Plan") pursuant to which 2,500,000 shares of common stock are currently reserved for issuance upon the exercise of options, designated as either (i) ISOs under the Code or (ii) nonqualified options, restricted stock, deferred stock or other stock-based awards. ISOs may be granted under the 2004 Plan to employees and officers of the Company. Non qualified options, restricted stock, deferred stock or other stock-based awards may be granted to consultants, directors (whether or not they are employees), employees or officers of the Company. Stock appreciation rights may also be issued in tandem with stock options. Unless the 2004 Plan is sooner terminated, the ability to grant options or other awards under the 2004 Plan will expire on September 10, 2014.

Options granted under the 2004 Plan may not be granted at a price less than the fair market value of the common stock on the date of grant (or 110% of fair market value in the case of persons holding 10% or more of the voting stock of the Company). Non-qualified options granted under the 2004 Plan may not be granted at a price less than the fair market value of the common stock. Options granted under the 2004 Plan expire not more than ten years from the date of grant (five years in the case of ISOs granted to persons holding 10% or more of the voting stock of the Company).

Effective August 27, 2008, the Company adopted its 2008 Stock Incentive Plan ("2008 Plan") pursuant to which 3,000,000 shares of common stock are currently reserved for issuance upon the exercise of options, designated as either (i) ISOs under the Code or (ii) nonqualified options, restricted stock, deferred stock or other stock-based awards. ISOs may be granted under the 2008 Plan to employees and officers of the Company. Non qualified options, restricted stock, deferred stock or other stock-based awards may be granted to consultants, directors (whether or not they are employees), employees or officers of the Company. Stock appreciation rights may also be issued in tandem with stock options. Unless the 2008 Plan is sooner terminated, the ability to grant options or other awards under the 2008 Plan will expire on August 27, 2018.

Options granted under the 2008 Plan may not be granted at a price less than the fair market value of the common stock on the date of grant (or 110% of fair market value in the case of persons holding 10% or more of the voting stock of the Company). Non-qualified options granted under the 2008 Plan may not be granted at a price less than the fair market value of the common stock. Options granted under the 2008 Plan expire not more than ten years from the date of grant (five years in the case of ISOs granted to persons holding 10% or more of the voting stock of the Company).

All stock options have been granted to employees and non-employees at exercise prices equal to or in excess of the market value on the date of the grant.

The Company determines the fair value of shared based awards at the grant date by using the Black-Scholes option-pricing model, and is incorporating the simplified method to compute expected lives of share based awards with the following weighted-average assumptions:

Nine Month Period ended September 30,	2008

Assumptions

Dividend Yield	0 %
Risk free interest rate	1.7% to 2.9%
Expected volatility	52% to 55%
Expected lives	2.5 to 5 years

A summary of the status of the Company's Plans as of December 31, 2007 and September 30, 2008 and changes for the periods ending on those dates is presented below:

Stock Option Plan Grants	Shares	Weighted Average Exercise Price
Outstanding at December 31, 2006	2,287,143	$1.47
• Granted	970,000	$0.85
• Forfeited	(242,500)	$3.07
• Exercised	(5,000)	$0.85
Outstanding at December 31, 2007	3,009,643	$1.15
• Granted	220,000	$1.44
• Forfeited	(60,000)	$1.09
• Exercised	(309,800)	$0.97
Outstanding at September 30, 2008	2,859,843	$1.19
	==========	

The following is the weighted average contractual life in years and the weighted average exercise price as of September 30, 2008 of:

	Number of Options	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price
Options outstanding	2,859,843	7.2 years	$1.19
Options vested	2,735,175	7.5 years	$1.19

The following is the intrinsic value as of September 30, 2008 of:

Options outstanding	$1,121,000
Options vested	$ 75,000
Options exercised	$ 496,000

The intrinsic value of options exercised during the year ended December 31, 2007 period was $2,000

The following is the weighted average fair value for the nine month period ended September 30, 2008 of:

Options granted	$ 1.45

Options vested $ 1.83

Note 3 - Stock repurchase

On June 28, 2007, the Company purchased and retired approximately 5,700,000 shares of its common stock from the Fleming Funds at a purchase price of $0.65 per share, for total consideration of approximately $3,700,000. Additionally, certain members of the Company's management, in separate private transactions, purchased approximately 9,200,000 shares of the Company's common stock from the Fleming Funds at a purchase price of $0.65 per share, for a total consideration of approximately $6,000,000. The shares purchased by management are unregistered shares and management did not receive registration rights in connection with their purchase of their shares.

On June 29, 2007, the Company commenced a tender offer to all of its common shareholders to purchase and retire up to approximately 1,200,000 shares of its common stock at a purchase price of $1.12 per share. Upon completion of the tender offer, a total of approximately 55,000 shares of the Company's common stock, at an aggregate purchase price of approximately $62,000, were tendered to and accepted for purchase by the Company, all of which were retired. On September 25, 2007 the Company utilized the unused tender offer funds to purchase and retire approximately 1,100,000 shares of its common stock from the Fleming Funds at a price of $1.12 per share, for a total consideration of approximately $1,200,000.

As a consequence of the shares purchased by the Company in the tender offer, and the shares purchased by the Company from the Fleming Funds, the Company retired an aggregate of approximately 6,900,000 shares of its common stock and increased its long-term debt by approximately $5,000,000. The retirement of those shares represents more than a 26% reduction in the number of outstanding shares of the Company's common stock when compared to the total outstanding shares prior to the tender offer and the purchases from the Fleming Funds.

The sale on June 28, 2007, by the Fleming Funds to certain members of the Company's management of approximately 9,200,000 shares at a purchase price of $0.65 per share required the Company to incur a non-cash, non-recurring compensation expense and a corresponding increase to additional paid-in capital of approximately $4,338,000, both of which were recognized in the quarter ended September 30, 2007,which represents the difference between the market value of the Company's common stock on June 28, 2007 and the purchase price of the common stock. The Company's net worth was unaffected by the $4,338,000 non-cash, non-recurring charge.

Note 4 - Long-Term debt

On April 17, 2008, Hudson amended its credit facility with Keltic Financial Partners, LLP ("Keltic") and secured participation from Bridge Healthcare Financial, LLC ("Bridge") to provide for borrowings up to $15,000,000. The facility consists of a revolving line of credit and term loans, which expires on June 20, 2011. Advances under the revolving line of credit may not exceed, except as permitted in the agreement governing the credit facility, $9,000,000 and are limited to (i) 85% of eligible trade accounts receivable and (ii) 55% of eligible inventory. Advances available to Hudson under the A and B term loans may not exceed $2,500,000 and $4,500,000, respectively. At September 30, 2008, the facility bore interest at 6.5%. Substantially all of Hudson's assets are pledged as collateral for its obligations to Keltic and Bridge under the credit facility. In addition, among other

things, the agreement restricts Hudson's ability to declare or pay any cash dividends on its capital stock. As of September 30, 2008, Hudson had in the aggregate $4,985,000 of borrowings outstanding and $3,029,000 available for borrowing under the revolving line of credit. In addition, the Company had $5,750,000 of borrowings outstanding under the A and B term loans with Keltic and Bridge.

In connection with the amendment to the credit facility, the Company issued 66,667 five-year common stock purchase warrants to Keltic exercisable at $1.88 per share, and issued 33,333 five-year common stock purchase warrants to Bridge exercisable at $1.88 per share. The Company utilizes the Black- Scholes pricing model to compute the fair value of the 100,000 stock purchase warrants. The $73,704, representing fair value of the warrants, is being amortized over the life of the credit facility and as of September 30, 2008 there was $61,420 unamortized debt cost, which is included in other assets on the balance sheet.

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

Safe Harbor Statement Under The Private Securities Litigation Reform Act of 1995

Certain statements contained in this section and elsewhere in this Form 10-Q constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements involve a number of known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such factors include, but are not limited to, changes in the demand and price for refrigerants (including unfavorable market conditions adversely affecting the demand for, and the price of refrigerants), the Company's ability to source CFC and non-CFC based refrigerants, regulatory and economic factors, seasonality, competition, litigation, the nature of supplier or customer arrangements that become available to the Company in the future, adverse weather conditions, possible technological obsolescence of existing products and services, possible reduction in the carrying value of long-lived assets, estimates of the useful life of its assets, potential environmental liability, customer concentration, the ability to obtain financing, and other risks detailed in this report and in the Company's other periodic reports filed with the Securities and Exchange Commission ("SEC"). The words "believe", "expect", "anticipate", "may", "plan", "should" and similar expressions identify forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date the statement was made.

Critical Accounting Policies

The Company's discussion and analysis of its financial condition and results of operations are based upon its consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these consolidated financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosure of contingent assets and liabilities. Several of the Company's accounting policies involve significant judgments, uncertainties and estimations. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities. Actual results may differ from these estimates under different assumptions or conditions. To the extent that actual results differ from management's judgments and estimates, there could be a material adverse effect on the Company. On a continuous basis, the Company evaluates its estimates, including, but not limited to, those estimates related to its allowance for doubtful accounts, inventory reserves, valuation allowance for the deferred tax assets relating to its NOL's and commitments and contingencies. With respect to accounts receivable, the Company estimates the necessary allowance for doubtful accounts based on both historical and anticipated trends of payment history and the ability of the customer to fulfill its obligations. For inventory, the Company evaluates both current and anticipated sales prices of its products to determine if a write down of inventory to net realizable value is necessary. In determining the Company's valuation allowance for its deferred tax assets, the Company assesses its ability to generate taxable income in the future. The Company utilizes both internal and external sources to evaluate potential current and future liabilities for various commitments and contingencies. In the event that the assumptions or conditions change in the future, the estimates could differ from the original estimates.

Overview

The Company has created and developed a service offering known as RefrigerantSide® Services. RefrigerantSide® Services are sold to contractors and end-users whose refrigeration systems are used in commercial air conditioning and industrial processing. These services are offered in addition to refrigerant sales and the Company's traditional refrigerant management services, which consist primarily of reclamation of refrigerants. The Company has created a network of service depots that provide a full range of the Company's RefrigerantSide® Services to facilitate the growth and development of its service offerings.

The Company focuses its sales and marketing efforts for its RefrigerantSide® Services on customers who the Company believes most readily appreciate and understand the value that is provided by its RefrigerantSide® Services offering. In pursuing its sales and marketing strategy, the Company offers its RefrigerantSide® Services to customers in the following industries; petrochemical, pharmaceutical, industrial power, manufacturing, commercial facility and property management and maritime. Moreover, to maintain its current ability to quickly respond to customer service requests throughout the United States, the Company seeks to pursue the creation of strategic alliances with companies that service larger customers in targeted industries, which, when consummated, would enable the Company to (i) co-locate its equipment with these strategic partners and (ii) utilize these partners' sales and marketing resources to offer their customers the Company's RefrigerantSide® Services. In addition, the Company has expanded its service offering outside of the United States through a strategic alliance with the Linde Group. The Company may incur additional expenses as it develops its RefrigerantSide® Services offering.

Sales of refrigerants continue to represent a significant portion of the Company revenues. Certain of the Company's refrigerant sales are CFC based refrigerants, which are no longer manufactured. The demand for CFC based refrigerants has and will continue to decrease as equipment that utilizes non-CFC based refrigerants displaces those units that utilize CFC based

refrigerants. The Company has increased its refrigerant sales from non-CFC based refrigerants, including HCFC and HFC refrigerants, which are the most widely used refrigerants. The Act limits the production of HCFC refrigerants, which production was further limited in January 2004. Federal regulations enacted in January 2004 also imposed limitations on the importation of certain HCFC refrigerants. Under the Act, production of certain HCFC refrigerants are scheduled to be phased out during the period 2010 through 2020, and production of all HCFC refrigerants is scheduled to be phased out by the year 2030. To the extent that the Company is unable to source CFC based or non-CFC based refrigerants on commercially reasonable terms or at all, or the demand for CFC based or non-CFC based refrigerants decreases, the Company's financial condition and results of operations could be materially adversely affected.

Results of Operations

Three month period ended September 30, 2008 as compared to the three month period ended September 30, 2007

Revenues for the three month period ended September 30, 2008 were $5,841,000 an increase of $1,103,000 or 23% from the $4,738,000 reported during the comparable 2007 period. The increase in revenues was primarily attributable to an increase in refrigerant revenues of $1,245,000 offset by a decrease in RefrigerantSide® Services revenues of $142,000. The increase in refrigerant revenues is related to both an increase in the sales price of refrigerants sold of $648,000 and an increased in this volume of refrigerants sold of $597,000. The decrease in RefrigerantSide® Services was primarily attributable to a decrease in the number of jobs completed when compared to the same period of 2007.

Cost of sales for the three month period ended September 30, 2008 was $3,917,000 an increase of $786,000 or 25% from the $3,131,000 reported during the comparable 2007 period. The increase in cost of sales was primarily due to an increase in pounds of refrigerant sold. As a percentage of sales, cost of sales was 67% of revenues for 2008, a slight increase from the 66% reported for the comparable 2007 period. The increase in cost of sales as a percentage of revenues was primarily attributable to an increase in the materials price of certain refrigerants sold when compared to the same period of 2007.

Operating expenses for the three month period ended September 30, 2008 were $1,282,000 an increase of $266,000 from the $1,016,000 reported during the comparable 2007 period. The increase in operating expenses was primarily related to an increase in compensation expense consisting primarily of selling salaries and commissions, and to a lesser extent for professional fees.

Other income (expense) for the three month period ended September 30, 2008 was ($298,000), compared to the ($231,000) reported during the comparable 2007 period. Other income (expense) includes interest expense of $299,000 and $235,000 for the comparable 2008 and 2007 periods, respectively. The increase in interest expense is primarily attributed to an increase in outstanding indebtedness.

Income tax expense (benefit) for the three month period ended September 30, 2008 and 2007 were $(2,395,000) and $3,000 respectively. For the three month period ended September 30, 2008, the income tax benefit consisted of the recognition of additional deferred tax asset of $2,600,000 offset by income tax expense of $205,000. For the three month period ended September 30, 2007, income tax of $3,000 was recognized for states that either don't allow or limit NOL's. The tax benefits associated with the Company's NOL's are recognized to the extent that the Company is expected to recognize taxable income. The Company's NOL's are subject to annual limitations and the Company expects to continue to incur certain state and federal alternative minimum taxes for the foreseeable future.

Net income for the three month period ended September 30, 2008 was $2,739,000 an increase of $2,382,000 from the $357,000 net income reported during the comparable 2007 period. The increase in net income in the 2008 period was primarily due to the income tax benefit of $2,395,000 recorded in the 2008 period.

Page 14

Nine month period ended September 30, 2008 as compared to the nine month period ended September 30, 2007

Revenues for the nine month period ended September 30, 2008 were $30,296,000 an increase of $6,134,000 or 25% from the $24,162,000 reported during the comparable 2007 period. The increase in revenues was primarily attributable to an increase in refrigerant revenues of $6,178,000 offset by a decrease in RefrigerantSide® Services revenues of $44,000. The increase in refrigerant revenues is primarily related to an increase in the sales price of certain refrigerants sold, in the 2008 period. During the first nine months of 2007, the Company completed refrigerant sales to a large customer at a lower margin than those made by the Company during the 2008 period. The Company subsequently chose to discontinue refrigerant sales to this customer and has substantially replaced most of this volume with various smaller transactions at higher margins. The decrease in RefrigerantSide® Services was primarily attributable to a decrease in the numbers of jobs completed when compared to the same period of 2007.

Cost of sales for the nine month period ended September 30, 2008 was $19,632,000, an increase of $1,584,000 or 9% from the $18,048,000 reported during the comparable 2007 period. The increase in cost of sales was primarily due to an increase in cost of certain refrigerants sold. As a percentage of sales, cost of sales was 65% of revenues for 2008, a decrease from the 75% reported for the comparable 2007 period. The decrease in cost of sales as a percentage of revenues was primarily attributable to an increase in the sales price of certain refrigerants sold when compared to the same period of 2007.

Operating expenses for the nine month period ended September 30, 2008 were $4,160,000 a decrease of $3,655,000 from the $7,815,000 reported during the comparable 2007 period. The decrease in operating expenses was primarily related to a reduction in compensation expense attributed to the non-cash, non-recurring charge of $4,338,000 in connection with the Transactions that occurred during the 2007 period partially offset by increased selling expenses and professional fees.

Other income (expense) for the nine month period ended September 30, 2008 was ($865,000), compared to the ($525,000) reported during the comparable 2007 period. Other income (expense) includes interest expense of $868,000 and $540,000 for the comparable 2008 and 2007 periods, respectively. The increase in interest expense is primarily attributed to an increase in outstanding indebtedness.

Income tax expense (benefit) for the nine month period ended September 30, 2008 and 2007 were ($1,851,000) and ($1,251,000) respectively. For the nine month period ended September 2008, the income tax expense of $749,000 was for federal and state income taxes and was offset by an increase in the tax benefit by 2,600,000. The tax benefits associated with the Company's NOL's are recognized to the extent that the Company is expected to recognize taxable income. The Company's NOL's are subject to annual limitations and the Company expects to continue to incur certain state and federal alternative minimum taxes for the foreseeable future.

Net income for the nine month period ended September 30, 2008 was $7,490,000 an increase of $8,465,000 from the ($975,000) net loss reported during the comparable 2007 period. The increase in net income in the 2008 period was primarily due to an increase in gross profit from an increase in refrigerant revenues and the absence of the $4,338,000 of compensation expense recorded in the 2007 period, as well as an increase in the income tax benefit recorded in 2008 compared to 2007.

Liquidity and Capital Resources

At September 30, 2008, the Company had working capital, which represents current assets less current liabilities, of $12,078,000 and an increase of $4,535,000 from the working capital of $7,543,000 at December 31, 2007. The increase in working capital is primarily attributable to net income during the period.

Inventory and trade receivables are principal components of current assets. At September 30, 2008, the Company had inventories of $18,877,000 an increase of $6,275,000 or 50% from the $12,602,000 at December 31, 2007. The increase in the inventory balance is due to the timing and availability of inventory purchases and the sale of refrigerants. The Company's ability to sell and replace its inventory on a timely basis and the prices at which it can be sold are subject, among other things, to current market conditions and the nature of supplier or customer arrangements and the Company's ability to source CFC based refrigerants, which are no longer being manufactured or non-CFC based refrigerants. At September 30, 2008, the Company had trade receivables, net of allowance for doubtful accounts of $2,641,000 an increase of $895,000 from the $1,746,000 at December 31, 2007. The Company's trade receivables are concentrated with various wholesalers, brokers, contractors and end-users within the refrigeration industry that are primarily located in the continental United States.

The Company has historically financed its working capital requirements through cash flows from operations, the issuance of debt and equity securities, and bank borrowings.

Net cash used by operating activities for the nine month period ended September 30, 2008, was $1,822,000 compared with net cash provided by operating activities of $2,124,000 for the comparable 2007 period. Net cash used by operating activities for the

2008 period was primarily attributable to increases in accounts receivable and inventory of $956,000 and $6,275,000, respectively, partially offset by net income.

Net cash used by investing activities for the nine month period ended September 30, 2008, was $498,000 compared with net cash used by investing activities of $348,000 for the prior comparable 2007 period. The net cash used by investing activities for the 2008 period was primarily related to investment in general purpose equipment and purchase of land in Champaign, Illinois.

Net cash provided by financing activities for the nine month period ended September 30, 2008, was $2,777,000 compared with net cash used by financing activities of $1,895,000 for the comparable 2007 period. The net cash provided by financing activities for the 2008 period was due to borrowings under the Company's revolving line of credit and proceeds of issuances of common stock offset by repayments of long term debt.

At September 30, 2008, the Company had cash and cash equivalents of $740,000. The Company continues to assess its capital expenditure needs. The Company may, to the extent necessary, continue to utilize its cash balances to purchase equipment primarily for its operations. The Company estimates that the total capital expenditures for 2008 will be approximately $800,000.

The following is a summary of the Company's significant contractual cash obligations for the periods indicated that existed as of September 30, 2008 (in 000's).

	Twelve Month Period ended September 30,					
	2009	2010	2011	2012	2013 And after	Total
Long and short term debt and capital lease obligations (1) & (2)	$6,889	$1,859	$4,328	$967	$ 0	$14,043
Operating leases	452	327	254	110	46	1,189
Total contractual cash obligations	$7,341	$2,186	$4,582	$1,077	$ 46	$15,232

(1) The contractual cash obligations included in the table includes both principal and estimated interest payments. The estimated interest payments on revolving debt are based primarily on the interest rates in effect and the outstanding revolving debt obligation as of September 30, 2008.

(2) Long and short term debt and capital lease obligations include payment of obligations of outstanding principal amounts of debt as of September 30, 2008 and estimated future interest payments on the outstanding principal amounts under the Company's credit facility with Keltic and Bridge, which expires on June 20, 2011.

On April 17, 2008, Hudson amended its credit facility with Keltic and secured participation from Bridge to provide for borrowings up to $15,000,000. The facility consists of a revolving line of credit and term loans, which expires on June 20, 2011. Advances under the revolving line of credit may not exceed, except as permitted in the agreement governing the credit facility, $9,000,000 and are limited to (i) 85% of eligible trade accounts receivable and (ii) 55% of eligible inventory. Advances available to Hudson under the A and B term loans may not exceed $2,500,000 and $4,500,000, respectively. At September 30, 2008, the facility bore interest at 6.5%. Substantially all of Hudson's assets are pledged as collateral for its obligations to Keltic and Bridge under the credit facility. In addition, among other things, the agreement restricts Hudson's ability to declare or pay any cash dividends on its capital stock. As of September 30, 2008, Hudson had in the aggregate $4,985,000 of borrowings outstanding and $3,029,000 available for borrowing under the revolving line of credit. In addition, the Company had $5,750,000 of borrowings outstanding under the A and B term loans with Keltic and Bridge.

In connection with the amendment to the credit facility, the Company issued 66,667 five-year common stock purchase warrants to Keltic exercisable at $1.88 per share, and issued 33,333 five-year common stock purchase warrants to Bridge exercisable at $1.88 per share.

On June 28, 2007, the Company purchased and retired approximately 5,700,000 shares of its common stock from the Fleming Funds at a purchase price of $0.65 per share, for total consideration of approximately $3,700,000. Additionally, certain members of the Company's management, in separate private transactions, purchased approximately 9,200,000 shares of the Company's common stock from the Fleming Funds at a purchase price of $0.65 per share, for a total consideration of approximately $6,000,000. The shares purchased by management are unregistered shares and management did not receive registration rights in connection with their purchase of their shares.

On June 29, 2007 the Company commenced a tender offer to all of its common shareholders to purchase and retire up to approximately 1,200,000 shares of its common stock at a purchase price of $1.12 per share. Upon completion of the tender offer, a

total of approximately 55,000 shares of the Company's common stock, at an aggregate purchase price of approximately $62,000, were tendered to and accepted for purchase by the Company, all of which were retired. On September 25, 2007 the Company utilized the unused tender offer funds to purchase and retire approximately 1,100,000 shares of its common stock from the Fleming Funds at a price of $1.12 per share, for a total consideration of approximately $1,200,000.

As a consequence of the shares purchased by the Company in the tender offer, and the shares purchased by the Company from the Fleming Funds, in 2007 the Company retired an aggregate of approximately 6,900,000 shares of its common stock and has increased its long-term debt by approximately $5,000,000. The retirement of those shares represents more than a 26% reduction in the number of outstanding shares of the Company when compared to the total outstanding shares prior to the tender offer and the purchases from the Fleming Funds.

In May 2005, the Company purchased its Champaign, Illinois facility for a total purchase price of $999,999. The Company financed the purchase with a 15 year amortizing loan in the amount of $945,000 with a balloon payment due on September 1, 2012. The note bears interest at 7% for the first five years and then adjusts annually based on prime plus 2%.

The Company believes that it will be able to satisfy its working capital requirements for the next twelve months from anticipated cash flows from operations and available funds under its existing credit facility. Any unanticipated expenses, including, but not limited to, an increase in the cost of refrigerants purchased by the Company, an increase in operating expenses or failure to achieve expected revenues from the Company's RefrigerantSide® Services and/or refrigerant sales or additional expansion or acquisition costs that may arise in the future would adversely affect the Company's future capital needs. There can be no assurances that the Company's proposed or future plans will be successful, and as such, the Company may require additional capital sooner than anticipated, which capital may not be available.

Inflation

Inflation has not historically had a material impact on the Company's operations.

Reliance on Suppliers and Customers

The Company's financial performance and its ability to sell refrigerants is in part dependent on its ability to obtain sufficient quantities of virgin, non-CFC based refrigerants, and of reclaimable, primarily CFC based, refrigerants from manufacturers, wholesalers, distributors, bulk gas brokers, and from other sources within the air conditioning, refrigeration and automotive aftermarket industries, and on corresponding demand for refrigerants. The Company's refrigerant sales include CFC based refrigerants, which are no longer manufactured. Additionally, the Company's refrigerant sales include non-CFC based refrigerants, including HCFC refrigerants, which are the most widely used refrigerants. Effective January 1, 1996, the Act limits the production of HCFC refrigerants, which production was further limited in January 2004. Federal regulations enacted in January 2004 also imposed limitations on the importation of certain HCFC refrigerants. Under the Act, production of certain HCFC refrigerants is scheduled to be phased out by the year 2020 and production of all HCFC refrigerants is scheduled to be phased out by the year 2030. The limitations imposed by and under the Act, may limit supplies of virgin refrigerants for the foreseeable future or cause a significant increase in the price of virgin HCFC refrigerants. To the extent the Company is unable to source sufficient quantities of virgin or reclaimable refrigerants in the future, or resell refrigerants at a profit, the Company's financial condition and results of operations would be materially adversely affected.

For the nine month period ended September 30, 2008 one customer accounted for approximately 10% of the Company's revenues. For the nine month period ended September 30, 2007 one customer accounted for approximately 13% of the Company's revenues.

The loss of a principal customer or a decline in the economic prospects of and/or a reduction in purchases of the Company's products or services by any such customer could have a material adverse effect on the Company's financial position and results of operations.

Seasonality and Fluctuations in Operating Results

The Company's operating results vary from period to period as a result of weather conditions, requirements of potential customers, non-recurring refrigerant and service sales, availability and price of refrigerant products (virgin or reclaimable), changes in reclamation technology and regulations, timing in introduction and/or retrofit or replacement of CFC and non CFC based refrigeration equipment, the rate of expansion of the Company's operations, and by other factors. The Company's business is seasonal in nature with peak sales of refrigerants occurring in the first half of each year. During past years, the seasonal decrease in sales of refrigerants has resulted in losses particularly in the fourth quarter of the year. Delays or inability in securing adequate supplies of refrigerants at peak demand periods, lack of refrigerant demand, increased expenses, declining refrigerant prices and a loss of a principal customer could result in significant losses. There can be no assurance that the foregoing factors will not occur and result in a material adverse effect on the Company's financial position and significant losses. The Company believes that there

is a similar seasonal element to RefrigerantSide® Service revenues as refrigerant sales. The Company is continuing to assess its RefrigerantSide® Service revenues seasonal trend.

Recent Accounting Pronouncements

In September 2006, the FASB issued FASB statement No. 157 ("SFAS No. 157,") "Fair Value Measurements," which establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. SFAS No. 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The FASB agreed to defer the effective date of SFAS No.157 for one year for non-financial assets and non-financial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis. There is no deferral for financial assets and financial liabilities, nor for the rare non-financial assets and non-financial liabilities that are remeasured at fair value at least annually. The adoption of SFAS No. 157 did not have a material impact on the Company's results of operations or its financial position.

Item 3 - Quantitative and Qualitative Disclosures about Market Risk

<u>Not Applicable</u>

Item 4T - Controls and Procedures

Disclosure Controls and Procedures

The Company, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures, as defined in Rule 13a-15(e) of the Securities Exchange Act or 1934, as amended ("Exchange Act"), as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed in reports filed under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission, and that such information is accumulated and communicated to the Company's management, including its principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure. Because of the inherent limitations in all control systems, any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Furthermore, the Company's controls and procedures can be circumvented by the individual acts of some persons, by collusion of two or more people or by management override of the control, and misstatements due to error or fraud may occur and not be detected on a timely basis.

Changes in Internal Control Over Financial Reporting

There were no changes in the Company's internal control over financial reporting (as defined in Rule 13a-15(f) of the Exchange Act) in the quarter ended September 30, 2008 that materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1 - Legal Proceedings

For information regarding pending legal matters, refer to the Legal Proceedings Section in Part I, Item 3 of the Company's Form 10-KSB for the year ended December 31, 2007.

Item 4 - Submission of Matters to a Vote of Security Holders

On August 27, 2008, the Company held an Annual Meeting of Shareholders at which the Company's shareholders voted for: (a) the election of two directors whose class was set to expire in 2008 (Messrs. Dominic J. Monetta and Kevin J. Zugibe) to serve until the Annual Meeting of Shareholders of the Company to be held in 2010 and (b) a proposal to approve the Company's 2008 Stock Incentive Plan. In addition to the foregoing individuals, Messrs. Vincent P. Abbatecola, Brian F. Coleman and Otto C. Morch, directors of the Company whose terms expire in 2010, continued to serve as directors of the Company after the Annual Meeting of Shareholders. The results of the vote were as follows:

1) Election of Directors

Director	Votes Cast "For"	Votes Withheld
Dominic J. Monetta	16,819,497	112,136
Kevin J. Zugibe	15,914,019	1,017,614

2) Approval of 2008 Stock Incentive Plan

Votes Cast "For	Votes Cast "Against"	"Votes "Abstaining"

11,260,810	1,692,114	5,418

In addition, there were 3,973,291 "broker non-votes" on this proposal.

Item 6 - Exhibits

The following exhibits are attached to this report:

10.1 2008 Stock Incentive Plan (1)
31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

---

(1) Incorporated by reference to Appendix I to the Company's Definitive Proxy Statement on Schedule 14A filed with the SEC on July 29, 2008.

SIGNATURES

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

HUDSON TECHNOLOGIES, INC.

By:	/s/ Kevin J. Zugibe Kevin J. Zugibe Chairman and Chief Executive Officer	November 4, 2008 Date
By:	/s/ James R. Buscemi James R. Buscemi Chief Financial Officer	November 4, 2008 Date

Exhibit Index

Number

Exhibit Title

10.1 2008 Stock Incentive Plan (1)

31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes Oxley Act of 2002

32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

____

(1) Incorporated by reference to Appendix I to the Company's Definitive Proxy Statement on Schedule 14A filed with the SEC on July 29, 2008

style="font-family:times;"> 322

Issuance of treasury shares

(832) 832

Issuance of common stock for acquisition

3,500 4 8,454 8,458

Stock based compensation

3,143 3,143

Balance December 31, 2011

36,675 37 204,076 (450) (2,247) (165,532) 35,884

Net income

603 603

Other comprehensive income

204 204

Equity securities repurchased

(1,513) (1,513)

Proceeds from issuance of ESPP

(29) 363 334

Issuance of treasury shares

(1,276) 1,276

Stock based compensation

2,797 2,797

Balance December 31, 2012

36,675 $37 $205,568 (324)(2,043)$(164,929)$38,309

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

Table of Contents

INFORMATION SERVICES GROUP, INC.

CONSOLIDATED STATEMENT OF CASH FLOWS

(in thousands)

	Years Ended December 31,		
	2012	**2011**	**2010**
Cash flows from operating activities			
Net income (loss)	$ 603	$ (55,937)	$ (53,165)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Depreciation expense	1,707	1,483	1,420
Goodwill impairment charge		34,314	46,591
Intangible assets impairment charge		27,380	5,900
Amortization of intangible assets	7,150	9,551	8,426
Amortization of deferred financing costs	350	360	359
Stock-based compensation	2,797	3,143	3,087
Change in fair value of contingent consideration	(2,000)		
Bad debt expense	297	588	(51)
Deferred tax benefit	(2,643)	(11,003)	(6,763)
Loss on disposal of fixed assets	22	3	11
Changes in operating assets and liabilities:			
Accounts receivable	931	(6,238)	(675)
Prepaid expense and other current assets	(1,071)	1,401	(31)
Accounts payable	1,953	(236)	(202)
Deferred revenue	(951)	593	(497)
Accrued expenses	1,585	(4,531)	1,337
Net cash provided by operating activities	10,730	871	5,747
Cash flows from investing activities			
Acquisitions, net of cash acquired	(24)	(13,684)	
Restricted cash	(1)	5,699	(5,750)
Proceeds from sale of furniture, fixtures and equipment		20	
Purchase of furniture, fixtures and equipment	(1,823)	(1,690)	(957)
Net cash used in investing activities	(1,848)	(9,655)	(6,707)
Cash flows from financing activities			
Principal payments on borrowings	(7,000)	(6,000)	(2,000)
Proceeds from issuance of ESPP shares	334	322	302
Payment of contingent consideration	(2,000)		
Equity securities repurchased	(1,513)	(1,225)	
Net cash used in financing activities	(10,179)	(6,903)	(1,698)
Effect of exchange rate changes on cash	327	(145)	173
Net decrease in cash and cash equivalents	(970)	(15,832)	(2,485)
Cash and cash equivalents, beginning of period	24,469	40,301	42,786
Cash and cash equivalents, end of period	$ 23,499	$ 24,469	$ 40,301
Supplemental disclosures of cash flow information:			
Cash paid for:			
Interest	$ 2,609	$ 2,914	$ 2,910
Taxes	$ 1,966	$ 3,904	$ 7,712

Noncash investing and financing activities:						
Issuance of common stock for acquisition	$		$	7,980	$	
Issuance of convertible debt for acquisition	$		$	6,250	$	
Issuance of treasury stock for vested restricted stock awards	$	1,276	$	832	$	

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

Table of Contents

INFORMATION SERVICES GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(tabular amounts in thousands, except per share data)

NOTE 1 DESCRIPTION OF ORGANIZATION AND BUSINESS OPERATIONS

Information Services Group, Inc. (the "Company") was incorporated in Delaware on July 20, 2006. The Company was formed to acquire, through a merger, capital stock exchange, asset or stock acquisition or other similar business combination one or more domestic or international operating businesses.

On November 16, 2007 (the "TPI Acquisition Date"), we consummated the acquisition of TPI Advisory Services Americas, Inc., a Texas corporation ("TPI"), pursuant to a Purchase Agreement dated April 24, 2007, as amended on September 30, 2007, by and between MCP-TPI Holdings, LLC, a Texas limited liability company ("MCP-TPI"), and the Company.

On January 4, 2011, the Company completed the acquisition of Compass. Compass is a premier independent global provider of business and information technology benchmarking, performance improvement, data and analytics services. It was founded in 1980 and headquartered in the United Kingdom and has 180 employees in 16 countries serving nearly 250 clients worldwide. The company pioneered the aggregation and application of sophisticated metrics to understand root causes of organizational performance issues. In addition, their Fact-Based Consulting unit generates tangible improvements in client businesses through sourcing advisory programs, recommendations in operational excellence and support in implementing transformational change in business operations. Compass uses benchmarking to support fact-based decision making, analysis to optimize cost reduction, and tools and techniques to manage business performance. For accounting purposes, the acquisition of Compass has been treated as a business combination.

On February 10, 2011 the Company completed the acquisition of STA Consulting (Salvaggio, Teal & Associates) a premier independent information technology advisor serving the public sector. STA Consulting advises clients on information technology strategic planning and the acquisition and implementation of new Enterprise Resource Planning (ERP) and other enterprise administration and management systems. STA Consulting was founded in 1997 and is based in Austin, Texas with approximately 40 professionals experienced in information systems consulting in public sector areas such as government operations, IT and project management, contract negotiations, financial management, procurement, human resources and payroll. STA Consulting works with such states as Alaska, Kansas, Kentucky, Louisiana, Mississippi and West Virginia. STA Consulting and TPI have worked together in the past on engagements for such states as Georgia and Texas. For accounting purposes, the acquisition of STA Consulting has been treated as a business combination.

During the fourth quarter of 2011, we merged our individual corporate brands into one globally integrated business under the ISG brand. TPI, the world's leading sourcing data and advisory firm; Compass, a premier independent provider of business and IT benchmarking; and STA Consulting, a premier independent technology advisory serving the North America public sector, and marketed together under the ISG brand. The merger is designed to offer clients one source to drive operational excellence in their organizations. We have retained our legacy brands to identify specific products and services we are known for including "The TPI Index", "TPI Sourcing" and "Compass Benchmarks".

Table of Contents

INFORMATION SERVICES GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(tabular amounts in thousands, except per share data)

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation and Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. These consolidated financial statements and footnotes are presented in accordance with accounting principles generally accepted in the United States of America ("US GAAP"). All intercompany accounts and transactions have been eliminated in consolidation. Unless the context requires otherwise, references to the Company include ISG and its consolidated subsidiaries.

Use of Estimates

The preparation of financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the periods reported. Actual results may differ from those estimates. The complexity of the estimation process and issues related to the assumptions, risks and uncertainties inherent in the application of the proportional performance method of accounting affect the amounts of revenues, expenses, unbilled receivables and deferred revenue. Numerous internal and external factors can affect estimates. Estimates are also used for but not limited to: allowance for doubtful accounts, useful lives of furniture, fixtures and equipment and definite-lived intangible assets, depreciation expense, fair value assumptions in analyzing goodwill and intangible asset impairments, income taxes and deferred tax asset valuation, and the valuation of stock based compensation.

Business Combinations

We have acquired businesses critical to the Company's long-term growth strategy. Results of operations for acquisitions are included in the accompanying consolidated statement of comprehensive income (loss) from the date of acquisition. Acquisitions are accounted for using the purchase method of accounting and the purchase price is allocated to the net assets acquired based upon their estimated fair values at the date of acquisition. The excess of the purchase price over the net assets was recorded as goodwill. Final valuations of assets and liabilities are obtained and recorded within one year from the date of the acquisition.

Reclassifications

Certain amounts from previously reported consolidated financial statements have been reclassified to conform to current year presentation. The reclassifications have no impact on the Company's financial position, results of operations or cash flows.

Cash and Cash Equivalents

The Company considers all highly liquid instruments with an original maturity of three months or less to be cash equivalents, including certain money market accounts. The Company principally

INFORMATION SERVICES GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(tabular amounts in thousands, except per share data)

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

maintains its cash in money market and bank deposit accounts in the United States of America which typically exceed applicable insurance limits. The Company believes it is not exposed to any significant credit risk on cash and cash equivalents.

Restricted Cash

Restricted cash consists of cash and cash equivalents which the Company has pledged to fulfill certain obligations and are not available for general corporate purposes.

Accounts and Unbilled Receivables and Allowance for Doubtful Accounts

Our trade receivables primarily consist of amounts due for services already performed via fixed fee or time and materials arrangements. The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of clients to pay fees or for disputes that affect its ability to fully collect billed accounts receivable. The allowance for these risks is prepared by reviewing the status of all accounts and recording reserves on a specific identification method based on previous experiences and historical bad debts. However, our actual experience may vary significantly from these estimates. If the financial condition of our clients were to deteriorate, resulting in their inability or unwillingness to pay their invoices, we may need to record additional allowances or write-offs in future periods. To the extent the provision relates to a client's inability or unwillingness to make required payments, the provision is recorded as bad debt expense, which is classified within selling, general and administrative expense in the accompanying consolidated statement of comprehensive income (loss).

The provision for unbilled services is recorded as a reduction to revenues to the extent the provision relates to fee adjustments and other discretionary pricing adjustments.

Prepaid Expenses and Other Assets

Prepaid expenses and other assets consist primarily of prepaid expenses for insurance, conferences and deposits for facilities, programs and promotion items.

Furniture, Fixtures and Equipment, net

Furniture, fixtures and equipment is recorded at cost. Depreciation is computed by applying the straight-line method over the estimated useful life of the assets, which ranges from three to five years. Leasehold improvements are depreciated over the lesser of the useful life of the underlying asset or the lease term, which generally range from three to five years. Expenditures for renewals and betterments are capitalized. Repairs and maintenance are charged to expense as incurred. The cost and accumulated depreciation of assets sold or otherwise disposed of are removed from the accounts and any associated gain or loss thereon is reflected in the accompanying consolidated statement of comprehensive income (loss).

Table of Contents

INFORMATION SERVICES GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(tabular amounts in thousands, except per share data)

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Internal-Use Software and Website Development Costs

The Company capitalizes internal-use software and website development costs and records these amounts within furniture, fixtures and equipment. Accounting standards require that certain costs related to the development or purchase of internal-use software and systems as well as the costs incurred in the application development stage related to its website be capitalized and amortized over the estimated useful life of the software or system. They also require that costs related to the preliminary project stage, data conversion and post implementation/operation stage of an internal-use software development project be expensed as incurred.

During the years ended December 31, 2012 and 2011, the Company capitalized $0.6 million and $0.5 million, respectively, of costs associated with the system conversion and website development.

Goodwill

Our goodwill represents the excess of the cost of businesses acquired over the fair value of the net assets acquired at the date of acquisition. Goodwill is not amortized but rather tested for impairment at least annually by applying a fair-value based test in accordance with accounting and disclosure requirements for goodwill and other indefinite-lived intangible assets. This test is performed by us during our fourth fiscal quarter or more frequently if we believe impairment indicators are present. At October 31, 2012, our annual impairment testing date, we maintain a single operating segment and reporting unit.

During the third quarter of 2012, management determined that a triggering event had occurred due to a revision in forecasted earnings as a result of macro-economic environment in Europe and continued unfavorable currency translation. Accordingly, the Company evaluated the carrying value of goodwill.

We performed a two-step impairment test on goodwill. Step one compares the fair value of the reporting unit to its carrying amount, including goodwill. If the carrying value of the reporting unit exceeds the fair value of the reporting unit, then we must perform the second step of the impairment test whereby the carrying value of the reporting unit's goodwill is compared to its implied fair value. If the carrying value of the goodwill exceeds the implied fair value, an impairment loss equal to the difference is recorded.

In performing the first step of the impairment test on goodwill, we determined the fair value of the reporting unit using both a market and income approach. The income approach utilizes a discounted cash flow model and is based on projections of future operations of the reporting unit as of the valuation date. The market approach is based on the guideline public company method which considers multiples of comparable companies. The Company selected an amount in the first quartile of such comparable companies. The discounted cash flow model assumed revenue growth rates of approximately 3% per year. We employed a discount rate of 13.5% based on the weighted average cost of capital of guideline public companies to discount future excess cash flows. As a result of the step

INFORMATION SERVICES GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(tabular amounts in thousands, except per share data)

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

one test performed, the fair value of our reporting unit exceeded the carrying value by 9%. Accordingly, step two was not performed or required.

The Company tested the fair value of goodwill during our scheduled annual impairment testing date in the fourth quarter of 2012 as of October 31, 2012 and passed step one of the impairment test by approximately 9%. In performing our fourth quarter impairment test we utilized the same assumptions as those in the third quarter impairment test. Management will continue to monitor changes in the business, as well as overall market conditions and economic factors that could require additional impairment tests.

Future downturns in our business, particularly changes in the discount rates or growth rates inherent in management's estimates of future cash flows, continued deterioration of economic conditions, or our stock trading below book value per share may result in an impairment charge in future periods, which could adversely affect our results of operations for those periods.

Long-Lived Assets

Long-lived assets, excluding goodwill and indefinite-lived intangibles, to be held and used by the Company are reviewed to determine whether any significant change in the long-lived asset's physical condition, a change in industry conditions or a reduction in cash flows associated with the use of the long-lived asset. If these or other factors indicate the carrying amount of the asset may not be recoverable, the Company determines whether impairment has occurred through the use of an undiscounted cash flow analysis of the asset at the lowest level for which identifiable cash flows exist. If impairment has occurred, the Company recognizes a loss for the difference between the carrying amount and the fair value of the asset. The fair value of the asset is measured using market prices or, in the absence of market prices, an estimate of discounted cash flows. Cash flows are generally discounted at an interest rate commensurate with our weighted average cost of capital for a similar asset. Assets are classified as held for sale when the Company has a plan for disposal of certain assets and those assets meet the held for sale criteria of accounting and disclosure requirement for the impairment or disposal of long-lived assets.

As a result of the triggering event which occurred during the third quarter of 2012, an impairment test was performed including definite-lived intangible assets based on the undiscounted cash flows method. The analysis determined there was no impairment.

Debt Issuance Costs

Costs directly incurred in obtaining long-term financing, typically bank and attorney fees, are deferred and are amortized over the life of the related loan using the effective interest method. Deferred issuance costs are classified as other assets in the accompanying consolidated balance sheet. Amortization of debt issuance costs is included in interest expense and totaled $0.4 million for each of the years ended December 31, 2012 and 2011.

Table of Contents

INFORMATION SERVICES GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(tabular amounts in thousands, except per share data)

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue Recognition

We recognize our revenues for the sale of services and products when persuasive evidence of an arrangement exists, services have been rendered or delivery has occurred, the fee is fixed or determinable and the collectability of the related revenue is reasonably assured.

We principally derive revenues from fees for services generated on a project-by-project basis. Prior to the commencement of a project, we reach agreement with the client on rates for services based upon the scope of the project, staffing requirements and the level of client involvement. It is our policy to obtain written agreements from new clients prior to performing services. In these agreements, the clients acknowledge that they will pay based upon the amount of time spent on the project or an agreed upon fee structure. Revenues for services rendered are recognized on a time and materials basis or on a fixed-fee or capped-fee basis in accordance with accounting and disclosure requirements for revenue recognition.

Fees for services that have been performed, but for which we have not invoiced the customers are recorded as unbilled receivables in the accompanying consolidated balance sheets. Invoices issued before the related services have been performed are recorded as deferred revenue in the accompanying consolidated balance sheets.

Revenues for time and materials contracts are recognized based on the number of hours worked by our advisors at an agreed upon rate per hour and are recognized in the period in which services are performed. Revenues for time and materials contracts are billed monthly, semimonthly or in accordance with the specific contractual terms of each project.

Revenues related to fixed-fee or capped-fee contracts are recognized into revenue as value is delivered to the customer. The pattern of revenue recognition for these contracts varies depending on the terms of the individual contracts, and may be recognized proportionally over the term of the contract or deferred until the end of the contract term and recognized when our obligations have been fulfilled with the customer. In instances where substantive acceptance provisions are specified in customer contracts, revenues are deferred until all acceptance criteria have been met. The pattern of revenue recognition for contracts where revenues are recognized proportionally over the term of the contact is based on the proportional performance method of accounting using the ratio of labor hours incurred to estimated total labor hours, which we consider to be the best available indicator of the pattern and timing in which contract obligations are fulfilled. This percentage is multiplied by the contracted dollar amount of the project to determine the amount of revenue to recognize in an accounting period. The contracted amount used in this calculation typically excludes the amount the client pays for reimbursable expenses. There are situations where the number of hours to complete projects may exceed our original estimate as a result of an increase in project scope or unforeseen events. On a regular basis, we review the hours incurred and estimated total labor hours to complete. The results of any revisions in these estimates are reflected in the period in which they become known.

Table of Contents

INFORMATION SERVICES GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(tabular amounts in thousands, except per share data)

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

We believe we have demonstrated a history of successfully estimating the total labor hours to complete a project.

The agreements entered into in connection with a project, whether on a time and materials basis or fixed-fee or capped-fee basis, typically allow our clients to terminate early due to breach or for convenience with 30 days' notice. In the event of termination, the client is contractually required to pay for all time, materials and expenses incurred by us through the effective date of the termination. In addition, from time to time, we enter into agreements with clients that limit our right to enter into business relationships with specific competitors of that client for a specific time period. These provisions typically prohibit us from performing a defined range of services that it might otherwise be willing to perform for potential clients. These provisions are generally limited to six to twelve months and usually apply only to specific employees or the specific project team.

Reimbursable Expenditures

Amounts billed to customers for reimbursable expenditures are included in revenues and the associated costs incurred by the Company are included in direct costs and expenses for advisors in the accompanying consolidated statement of comprehensive income (loss). Non-reimbursable amounts are expensed as incurred. Reimbursable expenditures totaled $9.7 million and $9.5 million for the years ended December 31, 2012 and 2011, respectively.

Direct Costs and Expenses for Advisors

Direct costs and expenses for advisors include payroll expenses and advisory fees directly associated with the generation of revenues and other program expenses. Direct costs and expenses for advisors are expensed as incurred.

Direct costs and expenses for advisors also include expense accruals for discretionary bonus payments. Bonus accrual levels are adjusted throughout the year based on actual and projected individual and Company performance.

Stock-Based Compensation

Stock Appreciation Rights ("SARs") for a fixed number of shares are granted to certain employees with an exercise price based on the closing trading price of our common stock on the grant date. We use the Black-Scholes option pricing model to determine the fair value of each option award on the date of grant. Prior to December 31, 2009, the volatility calculation was based on the most recent trading day average volatility of a representative sample of seven companies with market capitalizations of approximately $125 million to $4.6 billion that management believed to be engaged in the business of information services (the "Sample Companies"). We referred to the average volatility of the Sample Companies because management believes that the average volatility of such companies is a reasonable benchmark to use in estimating the expected volatility of our common stock as we had a limited history

Table of Contents

INFORMATION SERVICES GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(tabular amounts in thousands, except per share data)

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

as a public company. The risk-free interest rate is determined based upon the interest rate on a U.S. Treasury Bill with a term equal to the expected life of the option at the time the option was granted. An expected life of five years was taken into account for purposes of assigning a fair value to the option. The expected life represents the period of time the awards granted are expected to be outstanding. There were no grants of SARS during the years ended December 31, 2012 or 2011.

We also grant restricted stock with a fair value that is determined based on the closing price of our common stock on the date of grant. SARs and restricted stock generally vest over a four-year period. Stock-based compensation expense is recognized ratably over the applicable service period.

We follow the provisions of accounting and disclosures requirement for share-based payments, requiring the measurement and recognition of all share-based compensation under the fair value method.

Concentration of Credit Risk

Financial instruments that potentially subject the Company to significant concentrations of credit risk consist principally of cash and accounts receivable. The Company places its cash investments with high quality financial institutions. The Company extends credit to its customers based upon an evaluation of the customer's financial condition and credit history and generally does not require collateral.

Treasury Stock

The Company makes treasury stock purchases in the open market pursuant to the share repurchase program, which was approved by the Board of Directors on November 14, 2007.

Treasury stock is recorded on the consolidated balance sheet at cost as a reduction of stockholders' equity. Shares are released from Treasury at original cost on a first-in, first-out basis, with any gain on the sale reflected as an adjustment to additional paid-in capital. Losses are reflected as an adjustment to additional paid-in capital to the extent of gains previously recognized, otherwise as an adjustment to retained earnings.

Foreign Currency Translation

The assets and liabilities of the Company's foreign subsidiaries are translated into U.S. dollars at exchange rates in effect at the end of the reporting period. Revenue and expense items are translated at average exchange rates for the reporting period. Resulting translation adjustments are included in the accompanying statement of comprehensive income (loss) and accompanying statement of stockholders' equity as a component of *Accumulated Other Comprehensive Loss*.

The functional currency of the Company and its subsidiaries is the respective local currency. The Company has contracts denominated in foreign currencies and therefore, a portion of the Company's

Table of Contents

INFORMATION SERVICES GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(tabular amounts in thousands, except per share data)

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

revenues are subject to foreign currency risks. Transactional currency gains and losses that arise from transactions denominated in currencies other than the functional currencies of our operations are recorded in *Foreign Currency Transaction (Loss) Gain* in the accompanying consolidated statement of comprehensive income (loss).

Fair Value of Financial Instruments

The carrying value of the Company's cash and cash equivalents, receivables, accounts payable, other current liabilities, and accrued interest approximate fair value.

Fair value measurements were applied with respect to our nonfinancial assets and liabilities measured on a nonrecurring basis, which would consist of measurements primarily to goodwill, intangible assets and other long-lived assets, and assets acquired and liabilities assumed in a business combination.

Fair value is the price that would be received upon a sale of an asset or paid upon a transfer of a liability in an orderly transaction between market participants at the measurement date (exit price). Market participants can use market data or assumptions in pricing the asset or liability, including assumptions about risk and the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market-corroborated, or generally unobservable. The use of unobservable inputs is intended to allow for fair value determinations in situations where there is little, if any, market activity for the asset or liability at the measurement date. Under the fair-value hierarchy:

Level 1 measurements include unadjusted quoted market prices for identical assets or liabilities in an active market;

Level 2 measurements include quoted market prices for identical assets or liabilities in an active market that have been adjusted for items such as effects of restrictions for transferability and those that are not quoted but are observable through corroboration with observable market data, including quoted market prices for similar assets; and

Level 3 measurements include those that are unobservable and of a highly subjective measure.

During 2012, there were no transfers of our financial assets between Level 1 and Level 2 measures. Our financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

The Company held investments in cash equivalent money market funds of approximately $20 thousand and $1.1 million at December 31, 2012 and 2011, respectively. The Company considers the fair value of cash equivalent money market funds to be classified within Level 1 of the fair value hierarchy.

The Company's financial instruments include outstanding borrowings of $63.1 million and $70.1 million at December 31, 2012 and 2011, respectively, which are carried at amortized cost. The

INFORMATION SERVICES GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(tabular amounts in thousands, except per share data)

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

fair values of these instruments are classified within Level 3 of the fair value hierarchy. The fair value of the Company's outstanding borrowings is approximately $62.9 million and $67.1 million at December 31, 2012 and 2011, respectively. The fair values of these instruments have been estimated using a discounted cash flow analysis based on the Company's incremental borrowing rate for similar borrowing arrangements. The incremental borrowing rate used to discount future cash flows ranged from 3.63% to 4.00%. The Company also considered recent transactions of peer group companies for similar instruments with comparable terms and maturities as well as an analysis of current market conditions.

The fair value of the Company's contingent consideration liability related to the STA acquisition was $2.8 million and $6.8 million at December 31, 2012 and 2011, respectively. During the year ended December 31, 2012, the Company reduced the contingent consideration liability by $1.9 million based on the latest estimates of future profit levels due to increased competition in the public sector and increased pricing pressures. The Company paid $2.0 million related to the contingent consideration during the second quarter of 2012 related to 2011 performance. The fair value measurement of this contingent consideration is classified within Level 3 of the fair value hierarchy and reflects the Company's own assumptions in measuring fair values using the income approach. In developing these estimates, the Company considered certain performance projections, historical results, and industry trends. This amount was estimated through a valuation model that incorporated probability-weighted assumptions related to the achievement of these milestones and thus the likelihood of us making payments. These cash outflow projections have been discounted using a rate of 2.3%, which is the after-tax cost of debt financing for market participants.

Income Taxes

We use the asset and liability method to account for income taxes, including recognition of deferred tax assets and liabilities for the anticipated future tax consequences attributable to differences between financial statement amounts and their respective tax basis. We review our deferred tax assets for recovery. A valuation allowance is established when we believe that it is more likely than not that some portion of its deferred tax assets will not be realized. Changes in the valuation allowance from period to period are included in our tax provision in the period of change.

For uncertain tax positions, we use a prescribed model for assessing the financial recognition and measurement of all tax positions taken or expected to be taken in its tax returns. The guidance provides clarification on derecognition, classification, interest and penalties, accounting in interim periods, disclosures and transition. Our provision for income taxes also includes the impact of provisions established for uncertain income tax positions, as well as the related interest.

Table of Contents

INFORMATION SERVICES GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(tabular amounts in thousands, except per share data)

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Earnings (loss) Per Share

Basic earnings (loss) per share is computed by dividing net income (loss) available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that would share in the net income of the Company. As of December 31, 2012, 35.6 million warrants and 1.4 million Units (each Unit comprising one common share and one warrant) have expired. The 250,000 STA shares were excluded from basic and diluted earnings per share since the contingency has not been met as of the reporting period. For the year ended December 31, 2012, the effect of 0.3 million stock appreciation rights ("SARs") have not been considered in the diluted earnings per share, since the market price of the stock was less than the exercise price during the period in the computation. In addition, 1.2 million restricted shares have not been considered in the diluted earnings per share calculation for the year ended December 31, 2012, as the effect would be anti-dilutive. For the year ended December 31, 2011, the effect of 1.6 million shares related to the Company's convertible debt, 5.0 million warrants, 0.4 million SARs and 2.7 million restricted shares have not been considered in the diluted earnings per share calculation for the year ended December 31, 2011, as the effect would be anti-dilutive. For the year ended December 31, 2010, the effect of 35.6 million warrants, 0.4 million SARs and 1.4 million Units associated with the Company's IPO underwriters purchase option have not been considered in the diluted earnings per share calculation, since the market price of the Company's common stock was less than the exercise price during the period in the computation. Also, 2.0 million restricted shares have not been considered in the diluted earnings per share calculation for the year ended December 31, 2010, as the effect would be anti-dilutive.

The following tables set forth the computation of basic and diluted earnings per share:

	2012	2011	2010
Basic:			
Net income (loss)	$ 603	$ (55,937)	$ (53,165)
Weighted average common shares	36,205	36,258	32,050
Basic income (loss) per share	$ 0.02	$ (1.54)	$ (1.66)
Diluted:			
Net income (loss)	$ 603	$ (55,937)	$ (53,165)
Interest expense of convertible debt, net of tax	46		
Net income (loss), as adjusted	$ 649	$ (55,937)	$ (53,165)
Basic weighted average common shares	36,205	36,258	32,050
Potential common shares	1,421		
Diluted weighted average common shares	37,626	36,258	32,050
Diluted income (loss) per share	$ 0.02	$ (1.54)	$ (1.66)

Table of Contents

INFORMATION SERVICES GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(tabular amounts in thousands, except per share data)

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Recently Issued Accounting Pronouncements

In July 2012, the Financial Accounting Standards Board ("FASB') amended the Intangibles Goodwill and Other Topic of the ASC that allows us to make a qualitative assessment of whether it is more likely than not that the fair value of an indefinite-lived intangible asset is less than its carrying amount. If, after assessing the relevant information, we determine it is more likely than not that the fair value is more than the carrying amount, no additional analysis is necessary. If we determine it is more likely than not that the fair value is less than the carrying amount, then we are required to proceed to the quantitative approach. The amended guidance is effective for us in our annual test in the fourth quarter of 2012, and adoption did not have an impact our consolidated financial condition or results of operations.

In June 2011, the FASB issued accounting guidance related to the presentation of comprehensive income. This guidance presents an entity with the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both choices, an entity is required to present each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. This update eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders' equity. The amendments in this update do not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. This guidance relates only to the presentation of comprehensive income. The provisions of this new guidance are effective for fiscal years and interim periods beginning after December 15, 2011 and are applied retrospectively for all periods presented. The adoption of this standard did not have a material impact on the Company's consolidated financial statements.

In February 2013, the FASB issued new accounting guidance that improves the reporting of reclassifications out of accumulated other comprehensive income. This new guidance requires entities to report the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in net income when applicable or to cross-reference the reclassifications with other disclosures that provide additional detail about the reclassifications made when the reclassifications are not made to net income. The new standard is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2012. The Company does not expect this guidance to have a material impact on the Company's financial position, results of operations, or cash flows since it is an enhancement to current required disclosures.

NOTE 3 ACQUISITIONS

On April 1, 2012, the Company executed an agreement for the purchase of the entire business of Compass Consulting Oy, previously a franchise incorporated in Finland for approximately $0.1 million plus deferred consideration of $0.01 million plus 50% of the amount by which the relevant profit exceeds targeted profit for the twelve month period ended March 31, 2012. The targeted profit for the twelve month period ended March 31, 2012 was not achieved. This transaction has been accounted for

Table of Contents

INFORMATION SERVICES GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(tabular amounts in thousands, except per share data)

NOTE 3 ACQUISITIONS (Continued)

as a business combination and the purchase price has been allocated to the assets acquired and liabilities assumed based upon their estimated fair values as of the acquisition date. There was no goodwill recorded as a part of this business combination.

Compass Acquisition

On January 4, 2011 (the "Compass Acquisition Date"), the Company executed an Agreement for the Sale and Purchase of the Entire Issued Share Capital of CCGH Limited (the "Agreement") and consummated the acquisition of the entire issued share capital CCGH Limited, an English corporation ("Compass").

Under the terms of the Agreement, each of the holders of the issued share capital of Compass (the "Compass Sellers") agreed to sell and transfer, and the Company agreed to buy, the entire share capital of Compass (the "Share Purchase"). The Share Purchase was consummated on January 4, 2011.

The final allocable purchase price consists of the following:

Cash	$	5,750
Common Stock*		7,980
Convertible Notes**		6,250
Stamp Tax		98
Total allocable purchase price	$	20,078

* 3,500,000 shares issued at $2.28 per share as part of the acquisition.

** The Convertible Notes (the "Notes") mature on January 4, 2018 and interest is payable on the outstanding principal amount, computed daily, at the rate of 3.875% per annum on January 31 of each calendar year and on the seventh anniversary of the date of the Notes. The Notes are subject to transfer restrictions until January 31, 2013. If the price of the Company's common stock on the Nasdaq Global Market exceeds $4 per share for 60 consecutive trading days (the "Trigger Event"), the holder of the Notes may convert all (but not less than all) of the outstanding principal amount of the Notes into shares of the Company's common stock at the rate of 1 share for every $4 in principal amount outstanding. After the Trigger Event, the Company may prepay all or any portion of the outstanding principal amount of the Notes by giving the holder 30 days written notice.

The purchase price has been allocated to the assets acquired and liabilities assumed based upon their estimated fair values as of the Compass Acquisition Date. The purchase price allocation was based upon a valuation completed by third-party valuation specialists using an income approach and estimates and assumptions provided by management. The excess of the purchase price over the net tangible and identifiable intangible assets was recorded as goodwill. Goodwill of $16.3 million acquired in the acquisition is not deductible for tax purposes.

Table of Contents

INFORMATION SERVICES GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(tabular amounts in thousands, except per share data)

NOTE 3 ACQUISITIONS (Continued)

The following table summarizes the final allocation of the aggregate purchase price to the fair value of the assets acquired and liabilities assumed as of the Compass Acquisition Date:

Allocation of Purchase Price:		
Cash	$	1,091
Accounts receivable		9,449
Prepaid expenses and other assets		2,042
Furniture, fixtures and equipment		685
Goodwill		16,295
Intangible assets		5,045
Accounts payable		(1,603)
Accrued expenses and other(1)		(11,009)
Deferred income tax liability		(1,917)
Net assets acquired	$	20,078

(1) The fair value of contingent liabilities related to uncertain tax positions recognized at the acquisition date is $1.5 million.

The intangible assets acquired include database, trademark and trade name, customer relationships, covenant not-to-compete and goodwill. Some of these assets, such as goodwill and the trademark and trade name are not subject to amortization but rather an annual test for possible impairment; other intangible assets that are amortized over their useful lives are reviewed when events or changes or circumstances indicate the carrying amount of the asset may not be recoverable.

Under the purchase method of accounting, the total purchase price of approximately $20.1 million was allocated to Compass's net tangible and intangible assets based on their estimated fair values as of the Compass Acquisition Date. Intangible assets are amortized utilizing the estimated pattern of the consumption of the economic benefit over their estimated lives, ranging from one to ten weighted average years. Based on the valuation and other factors as described above, the purchase price assigned to intangible assets and the amortization period were as follows:

		Purchase Price Allocation	Asset Life
Amortizable intangible assets:			
Customer relationships	$	1,150	10 years
Covenants not-to-compete		15	2 years
Databases-Financial Data Repository		1,840	7 years
Non-amortizable intangible assets:			
Trademark and trade name		2,040	Indefinite
Total intangible assets	$	5,045	

INFORMATION SERVICES GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(tabular amounts in thousands, except per share data)

NOTE 3 ACQUISITIONS (Continued)

STA Acquisition

On February 10, 2011 (the "STA Acquisition Date"), the Company executed an Asset Purchase Agreement (the "STA Agreement") with Salvaggio & Teal Ltd. (d/b/a Salvaggio, Teal & Associates, "STA Consulting"), Salvaggio & Teal II, LLC, Mitt Salvaggio, Kirk Teal, Nathan Frey and International Consulting Acquisition Corp., a wholly-owned subsidiary of ISG, and consummated the acquisition of substantially all of the assets and assumption of certain specified liabilities of STA (collectively, the "Asset Purchase").

Under the terms of the STA Agreement, ISG acquired the specified assets for cash consideration of $9.0 million subject to certain adjustments. In addition, the sellers under the Agreement (the "STA Sellers") are eligible to receive a minimum of $0 and a maximum up to $7.75 million of earn-out payments for fiscal years 2011-2015 if certain revenue a