

INTERNATIONAL ISOTOPES INC  
Form 10-Q  
November 07, 2008

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D. C. 20549**

**FORM 10-Q**

(Mark One)

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:

0-22923

**INTERNATIONAL ISOTOPES INC.**

(Exact name of registrant as specified in its charter)

**Texas**  
(State of incorporation)

**74-2763837**  
(IRS Employer Identification Number)

**4137 Commerce Circle**  
**Idaho Falls, Idaho, 83401**  
(Address of principal executive offices)

**(208) 524-5300**  
(Registrant's telephone number, including area code)

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  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 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 smaller reporting company)

Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

“ Yes ý No

As of November 7, 2008 the number of shares of Common Stock, \$.01 par value, outstanding was 280,403,608.

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## Part I. Financial Statements

## Item 1. Financial Statements

**INTERNATIONAL ISOTOPES INC. AND SUBSIDIARIES****Unaudited Condensed Consolidated Balance Sheets**

| Assets                                 | September 30,<br>2008 | December 31,<br>2007 |
|--|-----------------------|----------------------|
| Current assets                         |                       |                      |
| Cash and cash equivalents              | \$ 660,361            | \$ 121,887           |
| Accounts receivable                    | 627,528               | 518,464              |
| Inventories                            | 2,551,292             | 2,502,266            |
| Prepays and other current assets       | 151,247               | 94,936               |
| Total current assets                   | 3,990,428             | 3,237,553            |
| Long-term assets                       |                       |                      |
| Restricted certificate of deposit      | 258,767               | 184,937              |
| Property, plant and equipment, net     | 2,947,225             | 2,095,610            |
| Capitalized lease disposal costs, net  | 90,682                | 83,271               |
| Investment                             | 1,290,000             | 330,000              |
| Patents, net                           | 111,300               | 91,857               |
| Total long-term assets                 | 4,697,974             | 2,785,675            |
| Total assets                           | \$ 8,688,402          | \$ 6,023,228         |
| Liabilities and Stockholders' Equity   |                       |                      |
| Current liabilities                    |                       |                      |
| Accounts payable                       | \$ 385,626            | \$ 441,910           |
| Accrued liabilities                    | 563,119               | 402,950              |
| Current installments of capital leases | 32,236                | 29,648               |
| Current installments of notes payable  | 1,435,328             | 937,969              |
| Total current liabilities              | 2,416,309             | 1,812,477            |

|  |              |              |
|--|--------------|--------------|
| Long-term liabilities  |              |              |
| Obligation for lease disposal costs  | 258,461      | 221,742      |
| Capital leases, excluding current installments   | 55,627       | 80,138       |
| Notes payable, excluding current installments  | 100,776      | 669,859      |
| Mandatorily redeemable convertible preferred stock   | 850,000      | 850,000      |
| Total long-term liabilities  | 1,264,864    | 1,821,739    |
| Total liabilities  | 3,681,173    | 3,634,216    |
| Stockholders' Equity   |              |              |
| Common stock, \$0.01 par value; 500,000,000 shares authorized;<br>280,403,608 and 250,481,324 shares issued and outstanding respectively | 2,804,036    | 2,504,811    |
| Additional paid-in capital   | 96,207,714   | 92,436,907   |
| Accumulated deficit  | (94,004,521) | (92,552,706) |
| Total stockholders' equity   | 5,007,229    | 2,389,012    |
| Total liabilities and stockholders' equity   | \$ 8,688,402 | \$ 6,023,228 |

*See accompanying notes to condensed consolidated financial statements.*

**INTERNATIONAL ISOTOPES INC. AND SUBSIDIARIES****Unaudited Condensed Consolidated Statements of Operations**

|   | <b>Three Months ended</b> |              | <b>Nine Months ended</b> |                |
|---|---------------------------|--------------|--------------------------|----------------|
|   | <b>September 30,</b>      |              | <b>September 30,</b>     |                |
|   | <b>2008</b>               | <b>2007</b>  | <b>2008</b>              | <b>2007</b>    |
| Sale of product   | \$ 1,245,164              | \$ 1,486,112 | \$ 4,429,144             | \$ 3,592,049   |
| Cost of product   | 647,882                   | 796,263      | 2,182,789                | 1,973,170      |
| Gross profit  | 597,282                   | 689,849      | 2,246,355                | 1,618,879      |
| Operating costs and expenses:                                 |                           |              |                          |                |
| Salaries and contract labor                                   | 510,908                   | 406,783      | 1,531,385                | 1,101,605      |
| General, administrative and consulting                        | 806,888                   | 536,502      | 2,087,470                | 1,608,698      |
| Research and development                                      | 6,470                     | 26,830       | 28,588                   | 45,749         |
| Total operating expenses                                      | 1,324,266                 | 970,115      | 3,647,443                | 2,756,052      |
| Operating loss  | (726,984)                 | (280,266)    | (1,401,088)              | (1,137,173)    |
| Other income (expense):                                       |                           |              |                          |                |
| Other income  | 16,951                    | 39,661       | 37,353                   | 108,531        |
| Interest income   | 6,578                     | 1,967        | 19,934                   | 5,985          |
| Interest expense  | (35,706)                  | (37,649)     | (108,014)                | (123,624)      |
| Total other income (expense)                                  | (12,177)                  | 3,979        | (50,727)                 | (9,108)        |
| Net loss  | \$ (739,161)              | \$ (276,287) | \$ (1,451,815)           | \$ (1,146,281) |
| Net loss per common share basic and diluted                   | \$ (0.00)                 | \$ (0.00)    | \$ (0.01)                | \$ (0.00)      |
| Weighted average common shares outstanding -basic and diluted | 280,402,224               | 247,646,540  | 273,051,820              | 235,378,328    |

*See accompanying notes to condensed consolidated financial statements.*





**INTERNATIONAL ISOTOPES INC. AND SUBSIDIARIES****Unaudited Condensed Consolidated Statements of Cash Flows**

|  | <b>Nine Months ended</b> |                |
|--|--------------------------|----------------|
|  | <b>September 30,</b>     |                |
|  | <b>2008</b>              | <b>2007</b>    |
| Cash flows from operating activities:                                      |                          |                |
| Net loss   | \$ (1,451,815)           | \$ (1,146,281) |
| Adjustments to reconcile net loss to net cash used in operating activities |                          |                |
| Depreciation and amortization  | 294,631                  | 250,481        |
| Accretion of obligation for lease disposal costs                           | 18,184                   | 11,468         |
| Compensation expense related to issuance of options                        | 267,925                  | 229,852        |
| Changes in operating assets and liabilities:                               |                          |                |
| Accounts receivable  | (109,064)                | (646,661)      |
| Prepays and other assets   | (56,311)                 | (20,027)       |
| Inventories  | (49,026)                 | 44,275         |
| Accounts payable and accrued liabilities                                   | 103,885                  | 337,236        |
| Net cash used in operating activities                                      | (981,591)                | (939,657)      |
| Cash flows from investing activities:                                      |                          |                |
| Restricted certificate of deposit  | (73,830)                 | (5,929)        |
| Purchase of patents  | (30,466)                 | (23,510)       |
| Purchase of RadQual interest   | -                        | (275,000)      |
| Purchase of property, plant and equipment                                  | (1,124,099)              | (251,341)      |
| Net cash used in investing activities                                      | (1,228,395)              | (555,780)      |
| Cash flows from financing activities:                                      |                          |                |
| Proceeds from exercise of warrants   | 2,799,997                | 468,048        |
| Proceeds from sale of stock  | 42,110                   | 1,205,369      |
| Principal payments on notes payable and capital leases                     | (93,647)                 | (173,931)      |
| Net cash provided by financing activities                                  | 2,748,460                | 1,499,486      |
| Net increase in cash and cash equivalents                                  | 538,474                  | 4,049          |

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|   |    |         |    |         |
|---|----|---------|----|---------|
| Cash and cash equivalents at beginning of period  |    | 121,887 |    | 169,702 |
| Cash and cash equivalents at end of period  | \$ | 660,361 | \$ | 173,751 |
| Supplemental disclosure of cash flow activities:  |    |         |    |         |
| Cash paid for interest  | \$ | 124,818 | \$ | 140,947 |
| Supplemental disclosure of noncash transactions:  |    |         |    |         |
| Conversion of note payable and accrued interest into common stock                             | \$ | -       | \$ | 673,614 |
| Issuance of note payable for property and equipment   | \$ | -       | \$ | 42,499  |
| Issuance of 392,620 shares of common stock at \$0.14 per share to acquire investment          | \$ | -       | \$ | 55,000  |
| Increase in lease disposal costs  | \$ | 18,535  | \$ | -       |
| Acquisition of interest in RadQual LLC in exchange for issuance of 1,370,753 shares of stock. | \$ | 960,000 | \$ | -       |

*See accompanying notes to condensed consolidated financial statements.*

## **INTERNATIONAL ISOTOPES INC. AND SUBSIDIARIES**

### **Notes to Unaudited Condensed Consolidated Financial Statements**

(1)

#### **The Company and Basis of Presentation**

International Isotopes Inc. (the Company) was incorporated in Texas in November 1995. The consolidated financial statements include all the accounts of the Company and its wholly owned subsidiaries, International Isotopes Idaho Inc., International Isotopes Fluorine Products Inc., and International Isotopes Transportation Services Inc., all of which are Idaho corporations. The Company's headquarters and all operations are located in Idaho Falls, Idaho.

*Nature of Operations* The Company's business consists of six major business segments which include: Nuclear Medicine Standards, Cobalt Products, Radiochemical Products, Fluorine Products, Radiological Services, and Transportation.

With the exception of certain unique products, the Company's normal operating cycle is considered to be one year. Due to the time required to produce some cobalt products, the Company's operating cycle for those products is considered to be three years. All assets expected to be realized in cash or sold during the normal operating cycle of business are classified as current assets.

*Principles of Consolidation* The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries International Isotopes Idaho Inc., International Isotopes Fluorine Products Inc., and International Isotopes Transportation Services Inc. All significant intercompany accounts and transactions have been eliminated in consolidation.

*Interim Financial Information* The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, they do not include all of the information and notes required by accounting principles generally

accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments and reclassifications considered necessary in order to make the financial statements not misleading and for a fair and comparable presentation have been included and are of a normal recurring nature. Operating results for the three and nine-month periods ending September 30, 2008, are not necessarily indicative of the results that may be expected for the year ending December 31, 2008. The accompanying financial statements should be read in conjunction with the Company's most recent audited financial statements.

*Recent Accounting Standards* - In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 157, *Fair Value Measurements*, which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. In February 2008, the FASB issued FASB Staff Position (FSP FIN) No. 157-2 which extended the effective date for certain nonfinancial assets and nonfinancial liabilities to fiscal years beginning after November 15, 2008. The adoption of the portions of SFAS No. 157 that were not postponed by (FSP FIN) No. 157-2 did not have a material impact on our consolidated financial statements. The Company does not expect the adoption of the postponed portions of SFAS No. 157 to have a material impact on our consolidated financial statements.

(2)

#### Current Developments and Liquidity

*Business Condition* Since inception, the Company has suffered substantial losses. During the nine-month period ended September 30, 2008, the Company had a loss of \$1,451,815 and operations used cash of \$981,591. During the same period in 2007, the Company had a loss of \$1,146,281 and operations used cash of \$939,657. During the three-month period ended September 30, 2008, the Company had a loss of \$739,161 as compared to a loss of \$276,287 for the similar period in 2007. The Company believes that continued growth in its current business segments will continue to improve revenue and cash flow for the Company. However, the Company will continue to invest in development of the fluorine extraction process (FEP) technology as well as design and licensing of a larger scale uranium de-conversion and fluorine extraction facility. Management expects to generate sufficient cash flows from the existing business segments to meet operational needs during 2008; however, there is no assurance that these cash flows will occur. In addition, the Company will likely require additional capital to support ongoing efforts to expand the Company business to include the envisioned large scale uranium de-conversion processing and fluorine extraction plant. Site studies as well as initial design and licensing activities for that new facility will continue through the remainder of 2008 and a significant portion of 2009.

(3)

## Net Loss Per Common Share - Basic and Diluted

At September 30, 2008, and 2007, the Company had the following common stock equivalents outstanding that were not included in the computation of diluted net loss per common share as their effect would have been anti-dilutive, thereby decreasing the net loss per common share:

|   | <b>September 30,</b> |                   |
|---|----------------------|-------------------|
|   | <b>2008</b>          | <b>2007</b>       |
| Stock options   | 18,780,000           | 22,150,000        |
| Class C warrants  | -                    | 13,333,331        |
| Class D warrants  | -                    | 13,333,331        |
| Class E warrants  | 13,333,331           | -                 |
| 850 shares of Series B redeemable convertible preferred stock | 425,000              | 425,000           |
|   | <b>32,538,331</b>    | <b>49,241,662</b> |

(4)

## Inventories

Inventories consist of the following at September 30, 2008, and December 31, 2007:

|                  | <b>September 30, 2008</b> |                  | <b>December 31, 2007</b> |                  |
|------------------|---------------------------|------------------|--------------------------|------------------|
| Raw materials    | \$                        | 254,343          | \$                       | 260,611          |
| Work in progress |                           | 2,296,949        |                          | 2,241,655        |
|                  | \$                        | <b>2,551,292</b> | \$                       | <b>2,502,266</b> |

(5)

#### Asset Acquisition

In May 2008, the Company entered into an Asset Purchase Agreement with Sequoyah Fuels Corporation pursuant to which the Company purchased certain tangible and intangible assets related to Sequoyah's depleted uranium hexafluoride to depleted uranium tetrafluoride conversion facility located in Gore, Oklahoma. On May 30, 2008, the Company and Sequoyah entered into a Technical Support Services Agreement pursuant to which Sequoyah will perform up to 500 hours of certain technical services to support the Acquired Assets. As consideration for the acquired assets and the service agreement, the Company paid Sequoyah \$900,000 cash. The Company is currently considering how to allocate the purchase price among tangible assets, intangible assets and the service agreement and currently has the entire \$900,000 recorded as production equipment. These assets are not being depreciated until such time as the assets are placed into service.

(6)

#### Stockholders' Equity and Warrants

##### Options

During the nine months ended September 30, 2008, certain option holders exercised 470,000 options under cashless exercises and the Company issued 366,568 shares of common stock. Certain option holders also exercised 1,500,000 options at \$0.20 per share for \$30,000 and the Company issued 1,500,000 shares of common stock.

##### Warrants

During January 2008, 13,333,331 Series D warrants were exercised for cash totaling \$1,466,666. In April 2008, the holders of all Class C warrants agreed to amend the terms of the Class C warrant to allow for the Company's call of those warrants. Subsequent to completing this modification, all 13,333,331 Class C warrants were exercised for cash totaling \$1,333,333 and the Company issued 13,333,331 exchange (Class E) warrants in accordance with the terms of the Class C warrant. Class E warrants entitle the holder to purchase shares of common stock, \$0.01 par value per share, at an exercise price equal to \$0.869 per share. Class E warrants expire March 20, 2011.



### Employee Stock Purchase

During the nine months ended September 30, 2008, the Company issued 18,302 shares of common stock to employees for proceeds of \$12,110. All of these shares were issued in accordance with the Company's employee stock purchase plan.

### Stock-based Compensation Plans

The Company accounts for issuances of stock-based compensation to employees under the provisions of Statement of Financial Accounting Standards (SFAS) No. 123(R). SFAS 123R requires the recognition of the cost of employee services received in exchange for an award of equity instruments in the financial statements and is measured based on the grant date fair value of the award. SFAS 123R also requires the stock option compensation expense to be recognized over the period during which an employee is required to provide service in exchange for the award (the vesting period).

The Company accounts for its issuances of stock-based compensation to non-employees for services using the measurement date guidelines enumerated in SFAS 123(R) and EITF 96-18. Accordingly, the value of any awards that were vested and non-forfeitable at their date of issuance were measured based on the fair value of the equity instruments at the date of issuance. The non-vested portion of awards that are subject to the future performance of the counterparty are adjusted at each reporting date to their fair values based upon the then current market value of the Company's stock and other assumptions that management believes are reasonable. The fair value of the stock options granted was calculated using the Black-Scholes option pricing model.

In January 2008, the Company granted stock options to a consultant to purchase 400,000 shares of common stock, with an exercise price of \$0.77 per share. The options vest at the rate of 25% each year over four years beginning one year from the date granted. The options had a grant date fair value of \$258,012 or \$0.65 per share as calculated using the Black-Scholes option pricing model.

The weighted average assumptions for options granted during the nine months ended September 30, 2008 used an expected dividend yield of zero and a risk-free interest rate of 3.33%. The expected volatility factor used was 110.92% with an expected life of 6.26 years. Weighted average fair value per share was assumed to be \$0.56.



In accordance with EITF 96-18, as of September 30, 2008, the options awarded to consultants were re-valued using the Black-Scholes option pricing model and had a fair value of \$225,181 or \$0.56 per share with the following assumptions: volatility of 90.68%, remaining expected life of six years, risk free interest rate of 3.18% and no dividends.

The expected life of stock options represents the period of time that the stock options granted are expected to be outstanding based on historical exercise trends. The expected volatility is based on the historical price volatility of the Company's common stock. The risk-free interest rate represents the U.S. Treasury bill rate for the expected life of the related stock options. The dividend yield represents the anticipated cash dividend over the expected life of the stock options.

Compensation expense charged against income for stock based awards during the nine months ended September 30, 2008 was \$267,925, as compared to \$229,852 for the nine months ended September 30, 2008 and 2007, respectively, and is included in general and administrative expense in the accompanying financial statements.

A summary of the status of the stock options as of September 30, 2008, and changes during the nine months ended September 30, 2008, is as follows:

| <b>Fixed Options</b>              | <b>Shares</b> | <b>Weighted<br/>Average<br/>Exercise Price</b> | <b>Weighted<br/>Average<br/>Remaining<br/>Term</b> | <b>Aggregate<br/>Intrinsic<br/>Value</b> |
|-----------------------------------|---------------|--|--|--|
| Outstanding at December 31, 2007  | 21,350,000    | \$ 0.05  |  |  |
| Granted                           | 400,000       | 0.77   |  |  |
| Exercised                         | (1,970,000)   | 0.07   |  | \$ 1,521,500                             |
| Forfeited                         | (1,000,000)   | 0.17   |  |  |
| Outstanding at September 30, 2008 | 18,780,000    | 0.09   | 4.9  | \$ 7,829,800                             |
| Exercisable at September 30, 2008 | 16,580,000    | 0.04   | 4.5  | \$ 7,419,800                             |

The intrinsic value of outstanding and exercisable shares is based on a September 30, 2008, closing price of the Company's common stock of \$0.50 per share.

As of September 30, 2008, there was approximately \$348,198 of unrecognized compensation cost related to stock options that will be recognized over a weighted average period of 2.1 years.

(7)

#### Acquisition of Interest in RadQual, LLC

During April 2007, the Company acquired 6% of the equity interests of RadQual, LLC for a cash payment of \$330,000. In May 2008, the Company acquired an additional 18.5% interest by issuing 1,370,753 shares of common stock valued at \$960,000 or \$0.70 per share. The remaining 75.5% ownership of RadQual is concentrated among a very small group of investors and due to this concentration the Company is unable to exert significant control or influence over the operations and policies of RadQual, LLC. Accordingly, the investment in RadQual will continue to be recorded at the lower of cost or fair value in accordance with FAB Interpretation 35 *Criteria for Applying the Equity Method of Accounting for Investments in Common Stock*. The 24.5% ownership of RadQual has been recorded at cost of \$1,290,000.

(8)

Commitments and Contingencies

Dependence on Third Parties

The production of HSA Cobalt is dependent upon the U.S. Department of Energy, and its prime operating contractor, which controls the reactor operations and, therefore, controls the continued production of cobalt in the government funded reactor. The revenue associated with the sale of HSA Cobalt is largely dependent on General Electric, the Company's sole customer for this product. Nuclear Medicine Reference and Calibration Standard manufacturing is conducted under an exclusive contract with another of our customers, RadQual, LLC, which in turn has an agreement in place with several companies for distributing the product. A loss of either of these customers could adversely affect operating results by causing a delay in production or a possible loss of sales.

Contingencies

Because all of the Company's business segments involve radioactive materials the Company is required to have an operating license from the Nuclear Regulatory Commission ( NRC ) and specially trained staff to handle these materials. The Company has an NRC operating license and has amended this license several times to increase the amount of material permitted within the facility. Additional processing capabilities and license amendments could be implemented that would permit processing of other reactor produced radioisotopes by the Company but this license does not currently restrict the volume of business operation performed or projected to be performed in the coming year. An irrevocable, automatic renewable letter of credit against a Certificate of Deposit at Wells Fargo Bank has been used to provide the financial assurance required by the NRC for the Idaho facility license.

(9)

## Segment Information

Segment information has been prepared in accordance with SFAS No. 131, Disclosure About Segments of an Enterprise and Related Information.

The Company has six reportable segments which include; Nuclear Medicine Standards, Cobalt Products, Radiochemical Products, Fluorine Products, Radiological Services, and Transportation. Information regarding the operations and assets of these reportable business segments is contained in the following table:

| Sale of Product            | Three Months ended September 30, |              | Nine Months ended September 30, |              |
|----------------------------|----------------------------------|--------------|---------------------------------|--------------|
|                            | 2008                             | 2007         | 2008                            | 2007         |
| Radiochemical Products     | \$ 348,968                       | \$ 248,228   | \$ 1,017,366                    | \$ 758,235   |
| Cobalt Products            | 240,494                          | 608,374      | 1,390,538                       | 822,414      |
| Nuclear Medicine Standards | 487,640                          | 466,435      | 1,399,338                       | 1,386,213    |
| Radiological Services      | 115,262                          | 136,978      | 527,532                         | 503,877      |
| Fluorine Products          | -                                | -            | -                               | -            |
| Transportation             | 52,800                           | 26,097       | 94,370                          | 121,310      |
| Total Segments             | 1,245,164                        | 1,486,112    | 4,429,144                       | 3,592,049    |
| Corporate revenue          | -                                | -            | -                               | -            |
| Total Consolidated         | \$ 1,245,164                     | \$ 1,486,112 | \$ 4,429,144                    | \$ 3,592,049 |

| Depreciation and Amortization | Three Months ended September 30, |           | Nine Months ended September 30, |           |
|-------------------------------|----------------------------------|-----------|---------------------------------|-----------|
|                               | 2008                             | 2007      | 2008                            | 2007      |
| Radiochemical Products        | \$ 11,013                        | \$ 11,326 | \$ 33,665                       | \$ 34,047 |
| Cobalt Products               | 26,181                           | 16,217    | 74,681                          | 48,029    |
| Nuclear Medicine Standards    | 637                              | 968       | 2,329                           | 3,873     |
| Radiological Services         | 2,600                            | -         | 5,404                           | 458       |
| Fluorine Products             | 48,565                           | 43,546    | 140,328                         | 121,335   |

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|   |            |           |            |            |
|---|------------|-----------|------------|------------|
| Transportation                          | 4,984      | 4,600     | 14,241     | 10,447     |
| Total Segments                          | 93,980     | 76,657    | 270,648    | 218,189    |
| Corporate depreciation and amortization | 7,261      | 8,057     | 23,983     | 32,292     |
| Total Consolidated                      | \$ 101,241 | \$ 84,714 | \$ 294,631 | \$ 250,481 |

| Segment Income (Loss)      | Three Months ended September 30, |              | Nine Months ended September 30, |                |
|----------------------------|----------------------------------|--------------|---------------------------------|----------------|
|                            | 2008                             | 2007         | 2008                            | 2007           |
| Radiochemical Products     | \$ 24,092                        | \$ (4,989)   | \$ 82,642                       | \$ 53,319      |
| Cobalt Products            | 153,331                          | 380,444      | 788,845                         | 410,855        |
| Nuclear Medicine Standards | 175,490                          | 142,053      | 569,357                         | 479,274        |
| Radiological Services      | 75,024                           | 79,075       | 350,718                         | 295,596        |
| Fluorine Products          | (438,830)                        | (228,537)    | (1,037,188)                     | (720,451)      |
| Transportation             | (20,309)                         | (38,962)     | (103,596)                       | (60,818)       |
| Total Segments             | (31,202)                         | 329,084      | 650,778                         | 457,775        |
| Corporate Loss             | (707,959)                        | (605,371)    | (2,102,593)                     | (1,604,056)    |
| Net Loss                   | \$ (739,161)                     | \$ (276,287) | \$ (1,451,815)                  | \$ (1,146,281) |

| Expenditures for Segment Assets | Three Months ended September<br>30, |           | Nine Months ended September 30, |            |
|---------------------------------|-------------------------------------|-----------|---------------------------------|------------|
|                                 | 2008                                | 2007      | 2008                            | 2007       |
| Radiochemical Products          | \$ -                                | \$ -      | \$ -                            | \$ -       |
| Cobalt Products                 | -                                   | 7,320     | 141,771                         | 91,278     |
| Nuclear Medicine Standards      | -                                   | -         | -                               | -          |
| Radiological Services           | -                                   | -         | 51,995                          | -          |
| Fluorine Products               | 14,705                              | 37,813    | 914,706                         | 143,214    |
| Transportation                  | 5,736                               | -         | 12,369                          | 52,439     |
| Total Segments                  | 20,441                              | 45,133    | 1,120,841                       | 286,931    |
| Corporate purchases             | -                                   | 1,184     | 3,258                           | 6,909      |
| Total Consolidated              | \$ 20,441                           | \$ 46,317 | \$ 1,124,099                    | \$ 293,840 |

| Segment Assets             | September 30,<br>2008 | December 31,<br>2007 |
|----------------------------|-----------------------|----------------------|
| Radiochemical Products     | \$ 327,862            | \$ 311,278           |
| Cobalt Products            | 3,261,366             | 2,915,698            |
| Nuclear Medicine Standards | 454,906               | 439,875              |
| Radiological Services      | 51,256                | 28,374               |
| Fluorine Products          | 2,059,972             | 1,255,049            |
| Transportation             | 57,895                | 59,766               |
| Total Segments             | 6,213,257             | 5,010,040            |
| Corporate assets           | 2,475,145             | 1,013,188            |
| Total Consolidated         | \$ 8,688,402          | \$ 6,023,228         |

## **ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

*This Quarterly Report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and within the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. All statements, other than statements of historical fact, including statements regarding industry prospects and future results of operations or financial position, made in this Quarterly Report are forward looking. In particular, statements regarding growth in our business segments; increased cash flow to meet operational needs; improvement in our financial strength, debt ratio and attractiveness to investors and lenders; future liquidity requirements; NRC licensing requirements; and the consequences of the loss of any of our major customers are forward looking. Forward-looking statements reflect management's current expectations, plans or projections. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this report. Certain risks and uncertainties that could cause our actual results to differ significantly from management's expectations are described in the risk factors set forth in our annual report on Form 10-KSB for the fiscal year ended December 31, 2007 filed with the securities and Exchange Commission on March 28, 2008. These factors, describe some but not all of the factors that could cause actual results to differ significantly from management's expectations. The Company will not publicly release any revisions to these forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events. Readers are urged, however, to review the factors set forth in reports that we file from time to time with the Securities and Exchange Commission.*

### **RESULTS OF OPERATIONS**

*Three-month and nine-month periods ended September 30, 2008, and 2007.*

Revenues for the three and nine-month period ended September 30, 2008, were \$1,245,164 and \$4,429,144 as compared to \$1,486,112 and \$3,592,049 for the same periods in 2007, a decrease of \$240,948, or 16%, for the three-month period and an increase of \$837,095, or 23%, for the nine-month period. The increase in total revenues for the nine-month period was attributable to strong performance in cobalt and radiochemical product business segments. The decline in revenue for the three-month period was attributable to normal variations in the sale of bulk cobalt for the period comparisons. Since the timing of large bulk cobalt product sales during the course of the calendar year has a significant impact upon period comparisons management believes that excluding sales of bulk cobalt product from the period comparisons of revenues provides useful information to investors.

Excluding bulk cobalt sales, revenues for the three-month period ended September 30, 2008, were \$1,245,164 as compared to \$1,038,835 for the same period in 2007, which represents an increase of 20%. Excluding bulk cobalt product sales, revenues for the nine-month period ended September 30, 2008, were \$3,940,888 as compared to \$3,144,773 for the same period in 2007, which represents an increase of 25%. Please refer to the following tables for a further analysis of this measure:

**Three-Month Financial Measure Reconciliation**

|   | <b>Period ended September 30,<br/>2008</b> | <b>Period ended September 30,<br/>2007</b> |
|---|--|--|
| Total Revenues                                    | \$1,245,164                                | \$1,486,112                                |
| Bulk Cobalt Products Revenues                     | \$0  | \$447,277                                  |
| Total Revenues Excluding Cobalt Products Revenues | \$1,245,164                                | \$1,038,835                                |

**Six-Month Financial Measure Reconciliation**

|   | <b>Period ended September 30,<br/>2008</b> | <b>Period ended September 30,<br/>2007</b> |
|---|--|--|
| Total Revenues                                    | \$4,429,144                                | \$3,592,049                                |
| Bulk Cobalt Products Revenues                     | \$488,256                                  | \$447,276                                  |
| Total Revenues Excluding Cobalt Products Revenues | \$3,940,888                                | \$3,144,773                                |



Revenues from the sale of radiochemical products for the three-month period ending September 30, 2008, were \$348,968 compared to \$248,228 for the same period in 2007. Revenues from the sale of radiochemical products for the nine-month period ending September 30, 2008, were \$1,017,366 compared to \$758,235 for the same period in 2007. These represent increases in revenue of \$100,740, or about 40%, and \$259,131, or about 34% for the three and nine-month periods respectively. Increases in the segment performance are attributable to increased sales of radiochemical iodine-131. Revenues from nuclear medicine products for the three-month period ending September 30, 2008 were \$487,640 compared to \$466,435 for the same period in 2007. Revenues from the sale of nuclear medicine products for the nine-month period ending September 30, 2008, were \$1,399,338 compared to \$1,386,213 for the same period in 2007. This represents an increase in income of \$21,205, or about 4% , and an increase in income of \$13,125, or 1%, respectively. Revenues from radiological services segment for the three-month period ending September 30, 2008, were \$115,262 compared to \$136,978 for the same period in 2007; a decrease of \$21,716 or 16%. Revenues from radiological services segment for the nine-month period ending September 30, 2008, were \$527,532 compared to \$503,877 for the same period in 2007. This represents an increase in revenue of \$23,655 or approximately a 5% increase. The fluctuations in revenue from this segment were attributable to typical variations in the volume of gemstone processing.

Gross profit for the three and nine-month periods ended September 30, 2008, was \$597,282 and \$2,246,355 compared to \$689,849 and \$1,618,879 for the same periods in 2007. This represents a decrease of \$92,567 or 13% and an increase of \$627,476 or 39%, for the three and nine month periods respectively. However, gross profit as a percentage of revenue grew from 46% to 48% for the three-month period and from 45% to 50% for the nine-month period comparisons. The improvement in gross profit percentage was the result of improvements in production costs and production efficiencies.

Operating expenses increased to \$1,324,266 and \$3,647,443 for the three and nine-month period ended September 30, 2008, compared to \$970,115 and \$2,756,052 for the same periods of 2007. This represents an increase of \$354,151 or 36%, and \$891,391 or 32%, for the three and nine-month periods respectively. Operating costs have increased in the period comparisons due to increased salaries, contract labor, and legal expense related to engineering design, licensing, addition of full time staff, subcontractors, and legal counsel necessary to support continued growth of the fluorine products division. This includes pilot plant demonstrations and efforts related to equipment acquisition, raising capital, and protecting newly developed intellectual property. The Company also realized a significant increase in stock based compensation expense. Salaries and contract labor expenses for the three and nine-month periods ended September 30, 2008 were \$510,908 and \$1,531,385 as compared to \$406,783 and \$1,101,605 for the same periods of 2007. General administrative expenses totaled \$806,888 and \$2,087,470 for the three and nine-month periods ended September 30, 2008 as compared to \$536,502 and \$1,608,698 for the same periods of 2007.

Our net loss for the three and nine-month periods ended September 30, 2008 was \$739,161 and \$1,451,815 compared to a loss of \$276,287 and \$1,146,281 for the same periods in 2007. This is an increase in loss of \$462,874 and \$305,534, or 167% and 26% respectively, and was attributable to increases in operating costs related to the support and continued growth of the fluorine products division including the pilot plant demonstration facility and efforts

related to equipment acquisition, raising capital, and protecting newly developed intellectual property.

Interest expense for the three and nine-month period ended September 30, 2008, was \$35,706 and \$108,014 as compared to \$37,649 and \$123,624 for the same periods in 2007. The reduction in interest expense was attributable to a reduction in the principal balance owed.

#### LIQUIDITY AND CAPITAL RESOURCES

On September 30, 2008, we had cash and cash equivalents of \$660,361. For the nine-months ended September 30, 2008, net cash used in operating activities was \$981,591. We used \$1,228,395 for investing activities. Financing activities provided \$2,748,460 from exercise of warrants and issuance and sale of Company stock.

At September 30, 2008, the Company had two outstanding loans with Compass Bank, formerly known as Texas State Bank. One loan carries an outstanding balance of \$117,597 with an interest rate of 9.25% and matures September 15, 2011. The second loan has an outstanding balance of \$553,037 with an interest rate of 10.25%, matures March 31, 2009, and is, therefore, reported as a current liability.

Our future liquidity and capital funding requirements will depend on numerous factors, including, contract manufacturing agreements, commercial relationships, technological developments, market factors, available credit, and voluntary warrant redemption by shareholders. We have 13,333,331 Class E warrants still outstanding.

During January 2008, 13,333,331 Series D warrants were exercised for cash totaling \$1,466,666. In April 2008, the holders of all Class C warrants agreed to amend the terms of the Class C warrant to allow for the Company's call of those warrants. Subsequent to completing this modification, all Class C warrants were exercised for cash totaling \$1,333,331 and the Company issued 13,333,331 exchange (Class E) warrants in accordance with the terms of the Class C warrant. Class E warrants entitle the holder to purchase shares of common stock, \$0.01 par value per share, at an exercise price equal to \$0.869 per share. Class E warrants expire March 20, 2011.

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

We are a smaller reporting company as defined by Rule 12b-2 of the Securities Exchange Act of 1934 and are not required to provide the information under this item.

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

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

The Company has established disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the Exchange Act)) to ensure that material information relating to the Company is made known to the officers who certify the Company's financial reports and to other members of senior management and the Board of Directors. These disclosure controls and procedures are designed to ensure that information required to be disclosed in the reports that are filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's (SEC) rules and forms. Under the supervision and with the participation of management, including the principal executive officer and principal financial officer an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as of September 30, 2008 was completed based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this evaluation, the principal executive officer and principal financial officer concluded that the Company's disclosure controls and procedures are functioning effectively.

Although our disclosure controls and internal controls were designed to provide reasonable assurance of achieving their objectives, and our principal executive officer and principal financial officer have determined that our disclosure controls and procedures are effective at doing so, a control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected.

These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any system of controls also is based partly on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

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

There was no change in the Company's internal control over financial reporting during the Company's most recently completed fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## **PART II. OTHER INFORMATION**

### **Item 6. Exhibits**

3(i)

Second Amended and Restated Articles of Incorporation (incorporated by reference to Appendix C to the Company's definitive proxy statement on Schedule 14A filed on April 28, 2005).

3(ii)

Bylaws (incorporated by reference to Exhibit 3.2 to the Company's Registration Statement on Form SB-2 filed on May 1, 1997 (Registration No. 333-26269)).

4.1

Form of Class E Warrant (incorporated by reference to Exhibit 4.1 of the Company's Current Report of Form 8-K filed on April 21, 2008).

10.1

Form of Indemnification Agreement (incorporated by reference to Exhibit 99.1 of the Company's current Report of Form 8-K filed on September 17, 2008).

31.1

Certification under Section 302 of the Sarbanes-Oxley Act of 2002 for Chief Executive Officer.

31.2

Certification under Section 302 of the Sarbanes-Oxley Act of 2002 for Chief Financial Officer.

32.1

Certification by the Chief Executive Officer furnished pursuant to 18 U.S.C. Section 1350 adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2

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

### SIGNATURES

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

International Isotopes Inc.  
(Registrant)

By: /s/ Steve T. Laflin  
Steve T. Laflin  
President and Chief Executive  
Officer

By: /s/ Laurie McKenzie-Carter  
Laurie McKenzie-Carter  
Chief Financial Officer

Date: November 7, 2008



**EXHIBIT INDEX**

**Exhibit**

**Number**

**Description of Document**

|       |  |
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