

INTERNATIONAL ISOTOPES INC  
Form 10QSB  
November 14, 2006

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

FORM 10-QSB

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

For the quarterly period ended  
September 30, 2006

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

(Issuer's telephone number, including area code)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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 shell company (as defined in Rule 12b-2 of the Exchange Act).

YES  NO

As of November 8, 2006 the number of shares of Common Stock, \$.01 par value, outstanding was 216,705,145.

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INTERNATIONAL ISOTOPES INC.

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**Part I. Financial Statements****Item 1. Financial Statements**

## INTERNATIONAL ISOTOPES INC. AND SUBSIDIARIES

## Unaudited Condensed Consolidated Balance Sheets

	<b>September 30, 2006</b>	<b>December 31, 2005</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 197,488	\$ 184,631
Accounts receivable	535,229	386,862
Inventories	2,383,603	2,668,911
Prepays and other current assets	102,489	132,562
Total current assets	3,218,809	3,372,966
Long-term assets		
Restricted certificate of deposit	175,000	178,684
Property, plant and equipment, net	2,134,580	1,876,464
Capitalized lease disposal costs, net	101,811	112,935
Patents, net	76,125	84,000
Total long-term assets	2,487,516	2,252,083
Total assets	\$ 5,706,325	\$ 5,625,049
 <b>Liabilities and Stockholders' Equity</b>		
Current liabilities		
Accounts payable	\$ 195,809	\$ 238,393
Accrued liabilities	274,260	261,709
Current installments of notes payable	2,402,010	1,057,069
Current installments of capital leases	26,029	-
Total current liabilities	2,898,108	1,557,171
Long-term liabilities		
Obligation for lease disposal costs	202,628	191,160
Notes payable, excluding current installments	-	1,327,421

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Capital leases, excluding current installments	116,696	-
Mandatorily redeemable convertible preferred stock	850,000	850,000
Total long-term liabilities	1,169,324	2,368,581
Total liabilities	4,067,432	3,925,752
Stockholders' equity		
Common stock, \$0.01 par value; 500,000,000 shares authorized;		
213,605,079 and 206,582,688 shares issued and outstanding respectively	2,136,052	2,065,826
Additional paid-in capital	89,868,342	89,429,810
Accumulated deficit	(90,365,501)	(89,796,339)
Total stockholders' equity	1,638,893	1,699,297
Total liabilities and stockholders' equity	\$ 5,706,325	\$ 5,625,049

See accompanying notes to condensed consolidated financial statements.

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

	<b>Three Months ended September 30,</b>		<b>Nine Months ended September 30,</b>	
	<b>2006</b>		<b>2005</b>	
Sale of product	\$ 1,458,260	\$ 828,439	\$ 3,641,098	\$ 2,177,270
Cost of product	852,284	465,806	1,967,402	1,199,806
Gross profit	605,976	362,633	1,673,696	977,464
Operating costs and expenses:				
Salaries and contract labor	333,277	192,041	912,518	649,862
General, administrative and consulting	375,454	257,481	1,149,450	902,726
Research and development	13,732	13,500	44,990	52,372
Total operating expenses	722,463	463,022	2,106,958	1,604,960
Operating loss	(116,487)	(100,389)	(433,262)	(627,496)
Other income (expense):				
Other income	-	61	3,785	635
Interest income	1,556	1,103	3,779	2,574



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Interest expense	(50,810)	(45,690)	(143,464)	(124,250)
Total other expense	(49,254)	(44,526)	(135,900)	(121,041)
Net Loss	\$ (165,741)	\$ (144,915)	\$ (569,162)	\$ (748,537)
Net loss per common share - basic and diluted	\$ (0.00)	\$ (0.00)	\$ (0.00)	\$ (0.00)
Weighted common shares outstanding - basic and diluted	213,184,707	188,035,592	211,078,457	182,227,488

See accompanying notes to condensed consolidated financial statements.

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

	<b>Nine Months ended September 30,</b>	
	<b>2006</b>	<b>2005</b>
<b>Cash flows from operating activities:</b>		
Net loss	\$ (569,162)	\$ (748,537)
Adjustments to reconcile net loss to net cash used in operating activities		
Depreciation and amortization	125,519	165,664
Loss on disposal of property, plant and equipment	27,268	-
Accretion of obligation for lease disposal costs	11,468	-
Compensation expense related to issuance of options	155,329	-
Changes in operating assets and liabilities:		
Accounts receivable	(148,367)	67,530
Prepays and other assets	30,073	(265,499)
Inventories	285,308	4,222
Accounts payable and accrued liabilities	(30,034)	(3,666)
Net cash used in operating activities	(112,598)	(780,286)
<b>Cash flows from investing activities:</b>		
Restricted certificate of deposit	3,684	(24,846)
Purchase of patents	-	(10,287)
Purchase of property, plant and equipment	(228,971)	(569,684)
Net cash used in investing activities	(225,287)	(604,817)
<b>Cash flows from financing activities:</b>		
Proceeds from exercise of warrants	346,577	1,459,778

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Proceeds from sale of stock	6,853	3,436
Redemption of debt	-	(1,193)
Proceeds from issuance of debt	100,000	150,000
Principal payments on notes payable	(102,688)	(36,353)
Net cash provided by financing activities	350,742	1,575,668
Net change in cash and cash equivalents	12,857	190,565
Cash and cash equivalents at beginning of period	184,631	150,051
Cash and cash equivalents at end of period	\$ 197,488	\$ 340,616
Supplemental disclosure of cash flow activities:		
Cash paid for interest, net of amounts capitalized	\$ 177,990	\$ 111,597
Supplemental disclosure of noncash transactions:		
Assets acquired through capital lease	\$ 202,910	\$ -
Capitalization of lease disposal costs	-	25,413

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 formed as a Texas corporation in 1995. Its wholly owned subsidiaries, are 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 five reportable segments: Nuclear Medicine Standards, Cobalt Products, Radiochemical Products, Fluorine Products, and Radiological Services.

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 for a fair and comparable presentation have been included and are of a normal recurring nature. Operating results for the nine-month period ended September 30, 2006 are not necessarily indicative of the results that may be expected for the year ending December 31, 2006. The accompanying financial statements should be read in conjunction with the Company's most recent audited financial statements.

*Stock-based Compensation Plans* - Effective January 1, 2006, the Company adopted SFAS 123R, using the modified prospective method. 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). Prior to our adopting SFAS 123R, we accounted for our stock-based compensation plans under Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees" ("APB 25"). The Company adopted the disclosure-only provision of SFAS No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123").

For the nine months ended September 30, 2006, the Company calculated compensation expense of \$155,329 related to stock options.

For options granted subsequent to the adoption date of SFAS 123R on January 1, 2006, the fair value of each stock option grant will be estimated on the date of grant using the Black-Scholes option pricing model. The Company made stock option grants totaling 4,000,000 shares during the quarter ended September 30, 2006, in accordance with the Company's 2006 Equity Incentive Plan. Of those options granted 1,000,000 shares were vested at the date of grant. The Company has made no other stock option grants during the nine months ended September 30, 2006.

The following are the weighted-average assumptions used for options granted during the nine months ended September 30, 2006 and 2005:

	<b>September 30,</b>	
	<b>2006</b>	<b>2005</b>
Risk free interest rate	4.93%	4.17%
Expected life	10 Years	10 Years
Dividend yield	-	-
Volatility	137%	144%

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 our 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 our anticipated cash dividend over the expected life of the stock options.

A summary of stock option activity for the nine months ended September 30, 2006 is presented below:

	<b>Shares Under Option</b>	<b>Weighted Average Exercise Price</b>	<b>Weighted Average Remaining Contractual Life</b>	<b>Aggregate Intrinsic Value</b>
Outstanding at January 1, 2006	18,650,000	\$ .04		
Granted	4,000,000	.08		
Outstanding at September 30, 2006	22,650,000	\$ .05	6.6 years	\$ 1,753,500

Exercisable at September 30, 2006	18,700,000	\$	.04	6.0 years	\$	1,923,500
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As of September 30, 2006, there was approximately \$251,811 of unrecognized compensation cost related to stock options that will be recognized over a weighted average period of approximately 1.78 years.

Prior to January 1, 2006, the Company determined the value of stock-based compensation arrangements under the provisions of APB Opinion No. 25 "Accounting for Stock Issued to Employees" and made pro forma disclosures required under SFAS No. 123, "Accounting for Stock-Based Compensation. . Had compensation expense for stock option grants been determined based on the fair value at the grant dates consistent with the method prescribed in FASB 123, the Company's net loss and net loss per share would have been adjusted to the proforma amounts below for the three- month and nine-months ended September 30, 2005, as indicated below:

	<b>For the Three Months Ended September 30, 2005</b>	<b>For the Nine Months Ended September 30, 2005</b>
Net loss as reported	\$ (144,915)	\$ (748,537)
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(28,317)	(113,011)
Pro forma net loss	\$ (173,232)	\$ (861,548)
Loss per share, basic and diluted:		
As reported	\$ -	\$ -
Pro forma	\$ -	\$ -

(2)

#### Current Developments and Liquidity

*Business Condition* Since inception, the Company has suffered substantial losses. During the three and nine-month periods ended September 30, 2006 the Company had a loss of \$165,741 and \$569,162 respectively compared to a loss of \$144,915 and \$748,537 during the same periods ended September 30, 2005. During the nine-month period ended September 30, 2006, the Company's operations used cash of \$112,598 in operating activities compared to \$780,286 for the same period in 2005. The Company believes that continued growth in our major business segments, and the start of the fluorine product sales will lead to increased revenue and improved cash flow. Based upon these improvements to business conditions, management expects to generate sufficient cash flows to meet operational needs during 2006; however, there is no assurance that these cash flows will occur.

(3)

#### Net Loss Per Common Share - Basic and Diluted



At September 30, 2006, and 2005, 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>2006</b>	<b>2005</b>
Options/warrants	35,187,770	50,955,861
850 Shares of Series B redeemable convertible		
Preferred stock	425,000	425,000
\$650,000 of convertible notes payable	8,125,000	8,125,000
	43,737,770	60,005,861

(4)

Inventories

Inventories consist of the following at September 30, 2006, and December 31, 2005.

	<b>September 30, 2006</b>	<b>December 31, 2005</b>
Raw materials	\$ 263,867	\$ 264,137
Work in progress	2,119,736	2,404,774
Finished goods	-	-
	<b>\$ 2,383,603</b>	<b>\$ 2,668,911</b>

(5)

Notes Payable

During May 2006, the Company drew an additional \$100,000 against the line of credit with a bank. As of September 30, 2006 the Company had drawn the maximum amount available of \$250,000 against this line of credit. Effective August 18, 2006 the Company renegotiated the terms of its line of credit. The line is due August 18, 2007 and accrues interest at the bank prime rate plus 1.5%.

(6)

Obligation Under Capital Leases

In March 2006, the Company entered into a new five year capital lease with a financing company for the purchase of production equipment. The lease requires monthly payments of \$3,341, bears interest at 10% and is due in March 2011. The future minimum lease payments are as follows:

**Years Ending December 31,**

2006	\$ 10,023
2007	40,092
2008	40,092
2009	40,092
2010	40,092
Thereafter	10,023
<b>Total Minimum Lease Payments</b>	<b>180,414</b>
Less Amount Representing Interest	37,689
<b>Present Value of Net Minimum Lease Payments</b>	<b>142,725</b>
Less Current Portion	26,029
<b>Capital Lease Obligation-Long Term</b>	<b>\$ 116,696</b>

(7)

Stockholders Equity and Warrants

Warrants

During the nine months ended September 30, 2006, 6,931,591 Series B warrants were exercised for cash proceeds of \$346,577. At September 30, 2006 the Company had 12,537,770 Series B warrants outstanding which, if exercised, would generate \$626,888 in cash.

### Employee Stock Purchase Plan

During the three months ended September 30, 2006, the Company issued 50,105 shares of common stock to employees for proceeds of \$3,833 in accordance with the employee stock purchase plan. During the nine months ended September 30, 2006, the Company has issued 90,800 shares of common stock to employees for proceeds of \$6,853 in accordance with this plan.

### 2006 Equity Incentive Plan

In April 2006, the Company adopted the International Isotopes 2006 Equity Incentive Plan (the 2006 Plan ). The 2006 Plan obtained shareholder approval in July 2006. The 2006 Plan replaced the Company s 2002 Long-Term Incentive Plan (the Prior Plan ).

The 2006 Plan permits the granting of any or all of the following types of awards: (1) incentive and nonqualified stock options, (2) stock appreciation rights, (3) stock awards restricted stock and stock units, (4) performance shares and performance units conditioned upon meeting performance criteria and (5) other stock or cash based awards.

The 2006 Plan authorizes the issuance of up to 20,000,000 shares of Common Stock, plus 1,350,000 shares previously reserved under the Prior Plan and up to 18,650,000 additional shares that are subject to outstanding options granted under the Prior Plan, that may become available for issuance under the 2006 Plan to the extent that such outstanding options are forfeited or otherwise expire or terminate without the issuance of shares.

Unless earlier terminated the 2006 Plan will terminate on July 12, 2016.

(8)

Commitments and Contingencies

During April 2005, the Company was named as a defendant in a lawsuit filed in the District Court of Texas for Denton County, by a former employee. The plaintiff has alleged that the Company breached his employment contract, by failing to provide six months continuation pay upon his termination. The plaintiff seeks damages of approximately \$57,500, plus attorneys' fees and court costs. This suit is still in the discovery stage and the Company intends to vigorously defend against this lawsuit.

Dependence on Third Parties

The production of HSA Cobalt is dependent upon the U.S. Department of Energy, and its prime operating contractor, who controls the reactor operations. The revenue associated with the sale of HSA Cobalt is largely dependent on the Company's sole customer for this product. Nuclear Medicine Standard's manufacturing is conducted under an exclusive contract with another of our customers, RadQual, LLC, who 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 amended the NRC license numerous times to address changes in the quantities of material being handled, and to describe the types of activities being conducted in the facility, and has obtained an additional license for the Fluorine Products subsidiary operations. Additional processing capabilities and license amendments could be implemented that would permit processing of other reactor-produced radioisotopes by the Company, but our current licenses do not restrict the volume of business operations currently performed or projected to be performed in the coming year. An irrevocable, automatic renewable letter of credit against a Certificate of Deposit at Texas State Bank has been used to provide the financial assurance required by the NRC for these licenses.

## (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 five reportable segments which include; Nuclear Medicine Standards, Cobalt Products, Radiochemical Products, Fluorine Products, and Radiological Services. All interest expense is attributable to corporate administration. Information regarding the operations and assets of these reportable business segments follows:

Sale of Product	Three Months ended September 30,		Nine Months ended September 30,	
	2006	2005	2006	2005
Nuclear Medicine Standards	\$ 379,991	\$ 386,639	\$ 1,319,698	\$ 1,105,717
Cobalt Products	662,444	164,567	1,144,074	296,192
Radiochemical Products	214,904	180,096	617,782	518,160
Fluorine Extraction Process	-	-	-	-
Radiological Services	200,921	97,137	559,544	257,201
Total Segments	1,458,260	828,439	3,641,098	2,177,270

Corporate revenue		-		-		-		-
Total Consolidated	\$	1,458,260	\$	828,439	\$	3,641,098	\$	2,177,270

<b>Depreciation and Amortization</b>	<b>Three Months ended September 30,</b>		<b>Nine Months ended September 30,</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
Nuclear Medicine Standards	\$ 2,307	\$ 9,100	\$ 7,876	\$ 27,362
Cobalt Products	10,881	10,994	32,646	32,612
Radiochemical Products	11,393	13,198	36,587	39,102
Fluorine Extraction Process	10,575	5,126	15,977	14,143
Radiological Services	1,634	7,099	4,818	21,647
Total Segments	36,790	45,517	97,904	134,866
Corporate depreciation and amortization	12,605	6,388	27,615	30,798
Total Consolidated	\$ 49,395	\$ 51,905	\$ 125,519	\$ 165,664

Segment Income (Loss)	Three Months ended September 30,		Nine Months ended September 30,	
	2006	2005	2006	2005
Nuclear Medicine Standards	\$ 136,201	\$ 147,409	\$ 558,342	\$ 462,422
Cobalt Products	279,102	122,426	470,163	172,012
Radiochemical Products	14,665	(20,048)	29,011	(39,646)
Fluorine Extraction Process	(158,694)	(112,217)	(482,297)	(378,405)
Radiological Services	58,990	18,989	216,200	84,274
Total Segments	330,264	156,559	791,419	300,757
Corporate Loss	(496,005)	(301,474)	(1,360,581)	(1,049,294)
Net Loss	\$ (165,741)	\$ (144,915)	\$ (569,162)	\$ (748,537)

Expenditures for Segment Assets	Three Months ended September 30,		Nine Months ended September 30,	
	2006	2005	2006	2005
Nuclear Medicine Standards	\$ -	\$ -	\$ -	\$ -
Cobalt Products	-	-	-	10,287
Radiochemical Products	-	-	-	1,800
Fluorine Extraction Process	25,549	338,802	403,023	548,589
Radiological Services	6,290	-	25,659	-
Total Segments	31,839	338,802	428,682	560,676
Corporate purchases	2,169	12,375	3,199	19,295
Total Consolidated	\$ 34,008	\$ 351,177	\$ 431,881	\$ 579,971

Segment Assets	September 30, 2006	December 31, 2005
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Nuclear Medicine Standards	\$	477,112	\$	582,341
Cobalt Products		2,781,063		2,633,211
Radiochemical Products		367,239		557,608
Fluorine Extraction Process		1,370,975		1,161,687
Radiological Services		86,462		217,949
Total Segments		5,082,851		5,152,796
Corporate assets		623,474		472,253
Total Consolidated	\$	5,706,325	\$	5,625,049

(10)

Subsequent Events

In November 2006, 3,053,566 shares of the Company's common stock were issued in connection with the redemption of Series B Warrants. The associated value was \$152,678.30.

Also, in November 2006, the Company issued 33,166 shares of common stock to employees in accordance with the Employee 2006 stock purchase plan.

## **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 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 our future liquidity requirements 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, 2005 filed with the Securities and Exchange Commission on April 12, 2006. These factors describe some but not all of the factors that could cause actual results to differ significantly from management's expectations. The Company does not intend to 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 and nine-month periods ended September 30, 2006, and 2005.* The Company's losses from operations for the three and nine-month periods ended September 30, 2006, were \$165,741 and \$569,162 respectively, as compared to losses from operations of \$144,915 and \$748,537 respectively for the comparable periods of 2005. The figures represent a 14% increase and 24% reduction in loss for the three and nine-month periods respectively. The increase in loss for the three month period comparison was primarily attributable to recognition in 2006 of compensation expense in the amount of \$110,801 as a result of implementing FAS 123(R).

Revenue for the three and nine-month periods ended September 30, 2006, was \$1,458,260 and \$3,641,098 respectively, as compared to \$828,439 and \$2,177,270 for the same periods in 2005. These numbers represent an increase of \$629,821 (or 76%) for the three-month period and \$1,463,828 (or 67%) for the nine-month period comparisons. The increase in total revenues was attributable to excellent performance in some of the Company's business segments. The Radiological Services segment is up over 106% and 117% respectively for the three and nine-month periods of 2006 compared to 2005. Cobalt Products have also increased by about 302% and 286% respectively for the three and nine-month periods of 2006 compared to 2005. Radiochemical products segment revenues have also increased by about 19% for both the three and nine-month periods of 2006 compared to 2005.

The Nuclear medicine segment underwent a 2% decline in revenues for the three month period ended September 30, 2006 compared to the same period in 2005, however, this segment revenues for the nine-month period ended September 30, 2006 are still up 19% above the same period in 2005.



It should be noted that the Company typically sees large variations in the revenue produced by the cobalt product segment because a large percentage of that revenue results from the sale of bulk cobalt and those sales are cyclic in nature. Therefore, the timing of those bulk sales will have a significant impact upon revenue period comparisons. Excluding cobalt product sales, revenues for the three-month period ended September 30, 2006, were \$795,816 as compared to \$663,872 for the same period in 2005, which represents an increase of \$131,944 or 20%. Excluding cobalt product sales revenues for the nine-month period ended September 30, 2006, were \$2,497,024 as compared to \$1,881,078 for the same period in 2005, which represents an increase of \$615,946 or 33%. Because of the significant impact of the timing of cobalt product sales, management believes that excluding sales of cobalt products from the period comparisons of revenues provides useful information to investors and may provide a more accurate projection of the actual revenue growth trends of the Company. Please refer to the tables below for a further analysis of this measure.

#### Three-Month Financial Measure Reconciliation

	Period ended Sept 30, 2005	Period ended Sept 30, 2006
Total Revenues	\$828,439	\$1,458,260
Cobalt Products Revenues	\$164,567	\$662,444
Total Revenues Excluding Cobalt Products Revenues	\$663,872	\$795,816

#### Nine-Month Financial Measure Reconciliation

	Period ended Sept 30, 2005	Period ended Sept 30, 2006
Total Revenues	\$2,177,270	\$3,641,098
Cobalt Products Revenues	\$296,192	\$1,144,074
Total Revenues Excluding Cobalt Products Revenues	\$1,881,078	\$2,497,024

Gross profit for the three-month periods ended September 30, 2006, and 2005, was \$605,976 and \$362,633 respectively, which represents an increase of \$243,343 or 67%. Gross profit for the nine-month periods ended September 30, 2006, and 2005 was \$1,673,696 and \$977,464 respectively, which represents an increase of \$696,232 or 71%. The increases in gross profit were consistent with the overall increase in revenues for the periods. Gross profit as a percentage of revenue declined slightly, from 43.7% to 41.5%, for the three month periods ended September 30, 2005 and 2006, and increased slightly, from 44.8% to 45.9%, for the nine-month periods ended September 30, 2005 and 2006 respectively.



Operating expenses for the three month periods ended September 30, 2006, and 2005, were \$722,463 and \$463,022 respectively which represents an increase of \$259,441 or 56%. Operating expenses for the nine- month periods ended September 30, 2006, and 2005, were \$2,106,958 and \$1,604,960 respectively which represents an increase of \$501,998 or 31%. Salaries and contract labor expenses for the three and nine-month periods ended September 30, 2006, were \$333,277 and \$912,518 respectively, as compared to \$192,041 and \$649,862 for the same periods of 2005.

General, administrative and consulting expenses totaled \$375,454 and \$1,149,450 respectively for the three and nine-month periods ended September 30, 2006, as compared to \$257,481 and \$902,726 for the same periods of 2005.

The overall increase in operating expenses were attributable to four roughly equal factors. First, the additional operating expenses related to the Company's newly established transportation services subsidiary (International Isotopes Transportation Services). This was the company's first year of operation of this new transportation subsidiary and, therefore, the Company did not previously recognize any operational expense with this operation. Second, the increase in operating expense related to ongoing support of the Company's Fluorine Products subsidiary. These increased costs were attributed to equipment operational expenses and additional staff required to prepare for the start of routine production operations. Third the company has slightly increased staff required to support industrial and radiological safety coverage of our operations. This increase in staff was necessary to keep pace with increased regulations combined with an expanding scope and volume of licensed operations activity. And, fourth the third quarter saw an increase in salary and contract labor expense as a result of the Company implementing FAS 123(R) which added expense for certain stock options granted during the period.

Interest expense for the three and nine-month period ended September 30, 2006, was \$50,810 and \$143,464 as compared to \$45,690 and \$124,250 for the comparable periods in 2005, an increase of \$5,120 and \$19,214 respectively. The increase in interest expense was due to an escalation in interest rates and an increase in the principal balance of the Company's line of credit account.

#### LIQUIDITY AND CAPITAL RESOURCES

On September 30, 2006 the Company had cash and cash equivalents of \$197,488 compared to \$184,631 at December 31, 2005. For the nine months ended September 30, 2006, operating activities used cash of \$112,598, investing activities used cash of \$225,287 and financing activities provided cash of \$350,742 from exercise of series B warrants and issuance of debt on the Company's line of credit. As of September 30, 2006, we had drawn the maximum amount available of \$250,000 against this line of credit.

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 Series B Warrant redemption by shareholders. As of September 30, 2006 the Company has 12,537,770

Series B Warrants still outstanding from the Company's Rights Offering conducted in 2003. Shareholder exercise of those Series B Warrants would generate \$626,888 in cash.

### **ITEM 3. CONTROLS AND PROCEDURES**

As of the end of the period covered by this report, the Company conducted an evaluation, under the supervision and with the participation of our principal executive officer and principal financial officer, of our 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")). Based on this evaluation, the principal executive officer and principal financial officer concluded that our disclosure controls and procedures were effective as of September 30, 2006.

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

Our principal executive officer and principal financial officer do not expect that our disclosure controls or our internal controls will prevent all error and all fraud. 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.



**PART II. OTHER INFORMATION**

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

The Annual Meeting of Shareholders was held on July 12, 2006.

*1) Election of Directors*

All three incumbent directors were reelected without opposition to serve one-year terms in office. The results of this election were as follows:

Name of Director

For

Withheld

Steve T. Laflin

155,991,630

646,495

Christopher Grosso

156,590,405

47,720

Ralph M. Richart

156,571,815

66,310

*2) Ratification of Independent Auditors*

The appointment of Hansen, Barnett & Maxwell as the independent auditors for fiscal year ending December 31, 2006 was ratified. The results of the shareholder vote were as follows:

For

Against

Abstain

Appointment of Hansen, Barnett  
& Maxwell as independent auditor

156,538,168

90,077

6,030

*3) Adoption of the 2006 Equity Incentive Plan*

The Company's 2006 Equity Incentive Plan was approved. The results of the shareholder vote were as follows:

For

Against

Abstain

Not Voted

Approval of the 2006 Equity

Incentive Plan

109,616,460

707,832

56,245

46,257,588

**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 May 1, 2006).

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)).

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.

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Certification by the Chief Executive and Chief Financial Officer 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

Date: November 14, 2006

