

ITRONICS INC  
Form 10QSB/A  
January 06, 2006

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-QSB/A  
AMENDMENT NO. 2

(Mark One)

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

**For the quarterly period ended June 30, 2005**

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 33-18582

ITRONICS INC.

(Exact name of small business issuer as specified in its charter)

TEXAS

75-2198369

(State or other jurisdiction of (IRS Employer Identification Number)  
incorporation or organization)

6490 S. McCarran Blvd., Bldg C-23, Reno, Nevada 89509

(Address of principal executive offices)

Issuer's telephone number, including area code: (775)689-7696

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 during the past 90 days. Yes (x) No ( ).

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APPLICABLE ONLY TO CORPORATE ISSUERS

As of July 31, 2005, 194,344,788 shares of common stock were outstanding.

Transitional Small Business Disclosure Format (Check one): Yes ( ) No (X)

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ITRONICS INC. AND SUBSIDIARIES

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

ITRONICS INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS  
JUNE 30, 2005 AND DECEMBER 31, 2004  
(UNAUDITED)

|                | June 30,    | December 31, |
|----------------|-------------|--------------|
|                | <u>2005</u> | <u>2004</u>  |
| ASSETS         |             |              |
| CURRENT ASSETS |             |              |
| Cash           | \$ -        | \$ 5,180     |

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|                                                                                         |             |             |
|-----------------------------------------------------------------------------------------|-------------|-------------|
| Accounts receivable, less allowance for doubtful accounts, 2005, \$5,700; 2004, \$5,700 | 152,035     | 188,805     |
| Marketable securities, available for sale                                               | 112,004     | 26,180      |
| Inventories                                                                             | 583,488     | 571,704     |
| Prepaid expenses                                                                        | 120,135     | 142,509     |
| Total Current Assets                                                                    | 967,662     | 934,378     |
| PROPERTY AND EQUIPMENT                                                                  |             |             |
| Land                                                                                    | 215,000     | 215,000     |
| Building and improvements                                                               | 1,167,315   | 1,167,315   |
| Design and construction in progress, manufacturing facility                             | 136,921     | 121,171     |
| Equipment and furniture                                                                 | 2,077,587   | 2,071,998   |
| Vehicles                                                                                | 133,028     | 133,028     |
| Equipment under capital lease-equipment and furniture                                   | 1,008,432   | 1,008,432   |
| Equipment under capital lease-vehicles                                                  | 87,672      | 87,672      |
|                                                                                         | 4,825,955   | 4,804,616   |
| Less: Accumulated depreciation and amortization                                         | 1,794,154   | 1,670,668   |
|                                                                                         | 3,031,801   | 3,133,948   |
| OTHER ASSETS                                                                            |             |             |
| Intangibles, net of amortization                                                        | 79,911      | 8,435       |
| Deferred loan fees, net of amortization                                                 | 46,280      | 48,654      |
| Deposits                                                                                | 22,525      | 22,525      |
|                                                                                         | 148,716     | 79,614      |
|                                                                                         | \$4,148,179 | \$4,147,940 |

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 LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)

|                                                              | June 30,    | December 31, |
|--------------------------------------------------------------|-------------|--------------|
|                                                              | <u>2005</u> | <u>2004</u>  |
| CURRENT LIABILITIES                                          |             |              |
| Bank overdraft                                               | \$ 30,208   | \$ -         |
| Accounts payable                                             | 590,709     | 558,566      |
| Account receivable and inventory factoring                   | 144,310     | 51,229       |
| Accrued management salaries                                  | 528,799     | 389,127      |
| Accrued expenses                                             | 322,083     | 398,731      |
| Insurance contracts payable                                  | 34,327      | 15,048       |
| Interest payable on stockholder advances                     | 14,421      | 6,307        |
| Interest payable                                             | 262,659     | 204,909      |
| Current maturities of long-term debt                         | 179,222     | 522,845      |
| Current maturities of capital lease obligations              | 768,723     | 807,746      |
| Current maturities of advances from an officer/stockholder   | 246,525     | 161,525      |
| Current maturities of capital lease due stockholder          | 5,600       | 5,420        |
| Current maturities of convertible notes and accrued interest | 2,760,504   | 1,020,946    |
| Other                                                        | 30,679      | 21,429       |
| Total Current Liabilities                                    | 5,918,769   | 4,163,828    |
| LONG-TERM LIABILITIES                                        |             |              |
| Long-term debt, less current maturities                      | 549,735     | 97,022       |
| Convertible promissory notes, less current maturities        | -           | 1,517,000    |
|                                                              | -           | 925,216      |

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|                                                                                                                                                                           |              |              |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------|--------------|
| Accrued interest, convertible notes, less current maturities                                                                                                              |              |              |
| Capital lease obligation, shareholder, less current maturities                                                                                                            | 6,326        | 9,144        |
| Total Long-Term Liabilities                                                                                                                                               | 556,061      | 2,548,382    |
|                                                                                                                                                                           | 6,474,830    | 6,712,210    |
| STOCKHOLDERS' EQUITY (DEFICIT)                                                                                                                                            |              |              |
| Preferred stock, par value \$0.001 per share;<br>authorized 999,500 shares, issued and outstanding<br>2005, 0 shares; 2004, 0 shares                                      | -            | -            |
| Common stock, par value \$0.001 per share;<br>authorized 250,000,000 shares, issued and outstanding,<br>194,339,788 at June 30, 2005; 164,863,938 at<br>December 31, 2004 | 194,340      | 164,864      |
| Additional paid-in capital                                                                                                                                                | 21,475,837   | 19,438,213   |
| Accumulated deficit                                                                                                                                                       | (24,677,953) | (22,944,959) |
| Common stock to be issued                                                                                                                                                 | 663,242      | 786,426      |
| Accumulated other comprehensive income (loss)                                                                                                                             | (19,642)     | (9,568)      |
| Common stock options outstanding, net                                                                                                                                     | 37,525       | 754          |
|                                                                                                                                                                           | (2,326,651)  | (2,564,270)  |
|                                                                                                                                                                           | \$4,148,179  | \$4,147,940  |

See Notes to Condensed Consolidated Financial Statements

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FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2005 AND 2004

(UNAUDITED)

|                                                                                                  | Three Months Ended June 30, |             | Six Months Ended June 30, |             |
|--------------------------------------------------------------------------------------------------|-----------------------------|-------------|---------------------------|-------------|
|                                                                                                  | <u>2005</u>                 | <u>2004</u> | <u>2005</u>               | <u>2004</u> |
| REVENUES                                                                                         |                             |             |                           |             |
| Photochemical fertilizer                                                                         | \$ 523,667                  | \$ 573,511  | \$ 783,841                | \$ 900,507  |
| Mining technical services                                                                        | 33,661                      | 52,659      | 83,460                    | 132,503     |
| Total Revenues                                                                                   | 557,328                     | 626,170     | 867,301                   | 1,033,010   |
| COST OF REVENUES (exclusive of<br>depreciation and amortization<br>shown separately below)       |                             |             |                           |             |
| Photochemical fertilizer                                                                         | 502,949                     | 531,139     | 805,287                   | 893,774     |
| Mining technical services                                                                        | 43,709                      | 57,459      | 92,479                    | 135,397     |
| Total Cost of Revenues                                                                           | 546,658                     | 588,598     | 897,766                   | 1,029,171   |
| Gross Profit (Loss) (exclusive<br>of<br>depreciation and amortization<br>shown separately below) |                             |             |                           |             |
|                                                                                                  | 10,670                      | 37,572      | (30,465)                  | 3,839       |
| OPERATING EXPENSES                                                                               |                             |             |                           |             |
| Depreciation and amortization                                                                    | 65,442                      | 79,338      | 130,884                   | 157,449     |
| Research and development                                                                         | 52,920                      | 27,808      | 133,656                   | 48,911      |
| Sales and marketing                                                                              | 244,434                     | 269,122     | 525,271                   | 483,407     |
| Delivery and warehousing                                                                         | 34,908                      | 34,275      | 52,991                    | 51,881      |
| General and administrative                                                                       | 225,934                     | 249,425     | 485,569                   | 462,200     |

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|                                |             |             |               |               |
|--------------------------------|-------------|-------------|---------------|---------------|
| Total Operating Expenses       | 623,638     | 659,968     | 1,328,371     | 1,203,848     |
| Operating (Loss)               | (612,968)   | (622,396)   | (1,358,836)   | (1,200,009)   |
| OTHER INCOME (EXPENSE)         |             |             |               |               |
| Interest expense               | (201,722)   | (202,325)   | (365,774)     | (411,095)     |
| Gain (loss) on sale of         |             |             |               |               |
| <b>investments</b>             | (6,431)     | 22,044      | (10,116)      | 97,802        |
| Other                          | 1,732       | 5           | 1,732         | 13            |
| Total Other Income (Expense)   | (206,421)   | (180,276)   | (374,158)     | (313,280)     |
| Income (Loss) before provision |             |             |               |               |
| <b>for income tax</b>          | (819,389)   | (802,672)   | (1,732,994)   | (1,513,289)   |
| Provision for income tax       | -           | -           | -             | -             |
| Net Income(Loss)               | (819,389)   | (802,672)   | (1,732,994)   | (1,513,289)   |
| Other comprehensive income     |             |             |               |               |
| (loss)                         |             |             |               |               |
| Unrealized gains (losses) on   |             |             |               |               |
| <b>securities</b>              | (1,192)     | (105,099)   | (10,074)      | (289,853)     |
| Comprehensive Income (Loss)    | \$(820,581) | \$(907,771) | \$(1,743,068) | \$(1,803,142) |
| Weighted average number of     |             |             |               |               |
| shares                         |             |             |               |               |
| Outstanding (1,000 s)          | 192,661     | 137,761     | 183,628       | 132,651       |
| Earnings (Loss) per share,     |             |             |               |               |
| basic                          |             |             |               |               |
| and diluted                    | \$(0.004)   | \$(0.006)   | \$(0.009)     | \$(0.011)     |

See Notes to Condensed Consolidated Financial Statements



## ITRONICS INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE SIX MONTHS ENDED JUNE 30, 2005 AND 2004

(UNAUDITED)

|                                                 | Six Months Ended June 30, |               |
|-------------------------------------------------|---------------------------|---------------|
|                                                 | <u>2005</u>               | <u>2004</u>   |
| Cash flows from operating activities            |                           |               |
| Net income (loss)                               | \$(1,732,994)             | \$(1,513,289) |
| Adjustments to reconcile net loss to            |                           |               |
| <b>cash used by operating activities:</b>       |                           |               |
| Depreciation and amortization                   | 130,884                   | 157,449       |
| Interest on convertible notes                   | 180,038                   | 261,411       |
| Marketable securities received for services     | (116,193)                 | (15,256)      |
| (Gain) Loss on investments                      | 10,116                    | (97,802)      |
| Addition of silver in solution inventory by     |                           |               |
| <b>offsetting photochemical processing fees</b> | (11,144)                  | (51,212)      |
| Stock option compensation                       | 37,112                    | 123           |
| Other                                           | (1,725)                   | -             |
| Expenses paid with issuance of common stock     | 429,453                   | 310,925       |
| (Increase) decrease in:                         |                           |               |
| Trade accounts receivable                       | 36,770                    | (71,142)      |
| Inventories                                     | (640)                     | (53,159)      |
| Prepaid expenses and deposits                   | (15,295)                  | 1,805         |
| Increase (decrease) in:                         |                           |               |
| Accounts payable                                | 43,990                    | 77,479        |

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|                                                   |             |           |
|---------------------------------------------------|-------------|-----------|
| Accrued management salaries                       | 139,672     | 52,431    |
| Accrued expenses and contracts payable            | (48,119)    | 58,077    |
| Accrued interest                                  | 65,864      | 16,358    |
| Net cash used by operating activities             | (852,211)   | (865,802) |
| Cash flows from investing activities:             |             |           |
| Acquisition of property and equipment             | (5,589)     | (8,922)   |
| Acquisition of intangibles                        | (5,000)     | -         |
| Proceeds from sale of investments                 | 10,177      | 223,139   |
| Net cash provided (used) by investing activities  | (412)       | 214,217   |
| Cash flows from financing activities:             |             |           |
| Proceeds from sale of stock                       | 570,000     | 712,000   |
| Proceeds from debt, stockholder                   | 90,000      | -         |
| Proceeds from short term debt, unrelated          | 125,000     | -         |
| Proceeds from receivable/inventory factoring, net | 93,081      | 38,641    |
| Payments on debt                                  | (60,846)    | (112,080) |
| Net cash provided by financing activities         | 817,235     | 638,561   |
| Net increase (decrease) in cash                   | (35,388)    | (13,024)  |
| Cash, beginning of period                         | 5,180       | 34,499    |
| Cash, end of period                               | \$ (30,208) | \$ 21,475 |

See Notes to Condensed Consolidated Financial Statements

JUNE 30, 2005

(UNAUDITED)

1. The unaudited condensed consolidated financial statements presented herein have been prepared in accordance with the instructions to Form 10-QSB and do not include all of the information and disclosures required by U.S. Generally Accepted Accounting Principles. Therefore, these financial statements should be read in conjunction with the consolidated financial statements and related footnotes included in the Company's Form 10-KSB for the year ended December 31, 2004. These financial statements reflect all adjustments that are, in the opinion of management, necessary to fairly state the results for the interim periods reported. Certain amounts from the prior period have been reclassified to be consistent with the current period presentation.

2. The Company's consolidated financial statements have been presented on the basis that it is a going concern, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. The Company and its subsidiaries have reported recurring losses from operations, including a net loss of \$1,732,994 during the six months ended June 30, 2005, a working capital deficit of \$4,936,355, and a stockholders' deficit balance of \$2,326,651 as of June 30, 2005. These factors indicate the Company and its subsidiaries' ability to continue in existence is dependent upon their ability to obtain additional long-term debt and/or equity financing and achieve profitable operations. The consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts and classification of liabilities that might be necessary should the Company and its subsidiaries be unable to continue in existence. The results of operations for the six months ended June 30, 2005 were affected by rainy weather in California and are not necessarily indicative of the results to be expected for the full year.

3. A Private Placement of restricted stock with attached three year warrants was closed in June 2005. Terms of the Placement included an offering price of \$0.05 per share, plus an attached three year warrant for one half the number of shares with an exercise price of \$0.075 for the first year, double that amount for the second year, and triple that amount for the third year. During the six months ended June 30, 2005 \$570,000 was received from this private placement.

4. In June 2005 the Company obtained short term financing totaling \$125,000. Subsequent to June 30, 2005, the Company arranged convertible debt financing from four unrelated Investors totaling up to \$3,250,000. The first funding of the loan was for \$1,250,000 and the Company received net proceeds after financing costs of \$866,200 plus payment of the above mentioned short term loan and accrued interest. The second funding, for gross proceeds of \$1,000,000, will be received once a registration statement is filed with the U.S. Securities and Exchange Commission, and the third funding, for gross proceeds of \$1,000,000, will be received once the registration statement becomes effective. The loans are for three years and they accrue interest at 8% per annum. The Investors will receive five year warrants to acquire 3,000,000 Company common shares at an exercise price of \$0.15 per share. The warrants will be issued proportionally as each of the fundings is completed. The loans are convertible into common shares at the lesser of \$0.10 or 55% of the average of the lowest 3 trading prices during the 20 trading day period ending one trading day before the conversion date. The loans are secured by a

(UNAUDITED)

security interest in substantially all of the Company's assets, including the assets of its wholly owned subsidiaries, and intellectual property. The loans are further secured by 14,550,558 Company common shares owned by an officer/stockholder.

During the second quarter of 2005, the Company renegotiated its account receivable factoring arrangement. The Company now factors specified raw material inventory items, the related finished GOLD n GRO fertilizer products, and the related accounts receivable from the sale of the specified GOLD n GRO fertilizers. The Company also factored the sale of two Photochemical Concentrators during the quarter. The balance due under these arrangements was \$144,310 at June 30, 2005. These loans are secured by a security interest in the related inventory and account receivable items.

5.

The Company may become involved in a lawsuit or legal proceeding at any time in the ordinary course of business. Litigation is subject to inherent uncertainties, and an unexpected adverse result may arise that may adversely affect our business. Certain lawsuits have been filed against us for collection of funds due that are delinquent, as described below. The Company is currently not aware of any litigation pending or threatened for any reason other than collection of funds due and already recorded. The Company is not aware of any additional legal proceeding or claims that the Company believes will have, individually or in the aggregate, a material adverse affect on our business, financial condition or operating results.

As of June 30, 2005 total recorded liabilities of \$802,166 including accrued interest to June 30, 2005, were subject to a total of 15 separate lawsuits for the collection of the funds due. These include 12 leases totaling \$604,896 (reflected in Current Maturities of Capital Lease Obligations) plus \$56,960 in additional interest (reflected in Accrued Interest) and three trade payables totaling \$129,191 (reflected in Accounts Payable) plus \$11,119 in additional interest (reflected in Accrued Interest). The leases are individually secured by specified equipment.

The accrued interest noted above was recorded based on our assessment of additional amounts the Company believes is probable and is related to four cases originally seeking \$423,375; the creditors have received judgments in three of these cases and the fourth is in litigation. The Company will continue to accrue interest until these cases are settled or paid in full.

The Company estimates an additional \$48,600 interest may be reasonably possible on other cases; however, the Company has not accrued this amount because it does not believe it is probable to be incurred. This estimate is related to four cases, three of which, originally seeking a total of \$181,672, are presently in settlement negotiations with creditors' counsel. An offer to settle the three cases for less than our recorded liability has been received; if we accept the offer, the Company will incur a small gain. The fourth case, seeking \$35,210, was filed in March 2003, and no further contact has taken place since then. During the third quarter of 2005, we paid off one suit totaling \$36,626 including interest and costs of \$17,200 that had not been accrued; this loss will be recorded in the third quarter.

(UNAUDITED)

The Company has six other cases that it deems to have a remote possibility of incurring an additional unrecorded loss. As of June 30, 2005, the Company was delinquent on these six cases with a recorded liability of \$95,383. All six have since been brought current.

Successful settlement of the above claims is dependent on future financing.

As of December 31, 2004 certain subsidiaries were delinquent on approximately \$206,200 in federal payroll taxes. These amounts are included in Accrued expenses in the Balance Sheet. Subsequent to June 30, 2005, the taxes were paid in full.

6. As of June 30, 2005 lease payments totaling \$796,216 were in arrears. As required by U.S. Generally Accepted Accounting Principles, the principal balance of the leases that are in default have been classified as current liabilities. The Company is in ongoing communication with the lessors to avoid action that may be adverse to the Company.

In 2003 an offer was made to extend the Series 2000 Convertible Promissory Notes. The holders of \$80,000 of the Notes have not responded to the offer and that amount, plus \$55,452 in accrued interest, remains in default.

As of June 30, 2005, the Company was delinquent on real property taxes in the amount of \$14,630 plus interest and penalties and was delinquent two monthly payments totaling \$13,202 plus late charges on the promissory note. This is a default of the promissory note and deed of trust secured by the Stead manufacturing facility. The lender was aware of the situation and took no collection action. Subsequent to June 30, 2005 the taxes and payments were brought current. In accordance with U.S. Generally Accepted Accounting Principles, the long term portion of the principal balance of the note, in the amount of \$458,081, which would otherwise have been classified as a current liability, has been classified as a long term liability.

7. During the six months ended June 30, 2005 convertible promissory notes totaling \$626,100 principal and \$256,596 accrued interest were converted into common stock at \$0.10 per share.

8. Significant non-cash operating, investing, and financing activities for the six months ended June 30, 2005 include the conversion of \$882,696 in convertible promissory notes and accrued interest into restricted common stock and the acquisition of the product rights to GOLD n GRO Guardian fertilizer for \$71,500 in restricted common stock.

9. Warrants, options, and shares to be issued, totaling 62,553,670 and 66,217,576 shares as of June 30, 2005 and 2004, respectively, would dilute future Earnings Per Share (EPS). No diluted EPS is presented as the effect of including these shares is antidilutive.

10. Following is financial information for each of the Company's segments. No changes have occurred in the basis of segmentation since December 31, 2004.

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ITRONICS INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2005

(UNAUDITED)

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Reconciliation of segment revenues, gross profit (loss), operating income (loss), other income (expense), and net income (loss) before taxes to the respective consolidated amounts follows:

|                           | Three Months Ended June 30, |             | Six Months Ended June 30, |               |
|---------------------------|-----------------------------|-------------|---------------------------|---------------|
|                           | <u>2005</u>                 | <u>2004</u> | <u>2005</u>               | <u>2004</u>   |
| Revenues:                 |                             |             |                           |               |
| Photochemical Fertilizer  | \$ 523,667                  | \$ 573,511  | \$783,841                 | \$ 900,507    |
| Mining Technical Services | 33,661                      | 52,659      | 83,460                    | 132,503       |
| Consolidated Revenues     | \$ 557,328                  | \$ 626,170  | \$867,301                 | \$ 1,033,010  |
| Gross Profit (Loss):      |                             |             |                           |               |
| Photochemical Fertilizer  | \$ 20,718                   | \$ 42,372   | \$(21,446)                | \$ 6,733      |
| Mining Technical Services | (10,048)                    | (4,800)     | (9,019)                   | (2,894)       |
| Consolidated Gross Profit |                             |             |                           |               |
| (Loss)                    | \$ 10,670                   | \$ 37,572   | \$(30,465)                | \$ 3,839      |
| Operating Income (Loss):  |                             |             |                           |               |
| Photochemical Fertilizer  | \$(494,262)                 | \$(508,586) | \$(1,097,807)             | \$(992,089)   |
| Mining Technical Services | (118,706)                   | (113,810)   | (261,029)                 | (207,920)     |
| Consolidated Operating    |                             |             |                           |               |
| Income (Loss)             | \$(612,968)                 | \$(622,396) | \$(1,358,836)             | \$(1,200,009) |
| Other Income (Expense):   |                             |             |                           |               |
| Photochemical Fertilizer  | \$(201,722)                 | \$(202,325) | \$(365,774)               | \$(411,095)   |
| Mining Technical Services | (4,699)                     | 22,049      | (8,384)                   | 97,815        |

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Consolidated Other Income

|           |             |             |             |             |
|-----------|-------------|-------------|-------------|-------------|
| (Expense) | \$(206,421) | \$(180,276) | \$(374,158) | \$(313,280) |
|-----------|-------------|-------------|-------------|-------------|

Net Income (Loss) before taxes:

|                          |             |             |               |               |
|--------------------------|-------------|-------------|---------------|---------------|
| Photochemical Fertilizer | \$(695,984) | \$(710,911) | \$(1,463,581) | \$(1,403,184) |
|--------------------------|-------------|-------------|---------------|---------------|

|                           |           |          |           |           |
|---------------------------|-----------|----------|-----------|-----------|
| Mining Technical Services | (123,405) | (91,761) | (269,413) | (110,105) |
|---------------------------|-----------|----------|-----------|-----------|

Consolidated Net Income

|                     |             |             |               |               |
|---------------------|-------------|-------------|---------------|---------------|
| (Loss) before taxes | \$(819,389) | \$(802,672) | \$(1,732,994) | \$(1,513,289) |
|---------------------|-------------|-------------|---------------|---------------|

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ITRONICS INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2005

(UNAUDITED)

Identifiable assets by business segment for the major asset classifications and reconciliation to total consolidated assets are as follows:

|                              | June 30,<br><u>2005</u> | December 31,<br><u>2004</u> |
|------------------------------|-------------------------|-----------------------------|
| Current Assets:              |                         |                             |
| Photochemical Fertilizer     | \$753,788               | \$ 670,602                  |
| Mining Technical Services    | 129,433                 | 157,603                     |
|                              | 883,221                 | 828,205                     |
| Property and Equipment, net: |                         |                             |
| Photochemical Fertilizer     | 2,924,166               | 3,010,749                   |

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|                                 |              |              |
|---------------------------------|--------------|--------------|
| Mining Technical Services       | 107,210      | 122,342      |
|                                 | 3,031,376    | 3,133,091    |
| Other Assets, net:              |              |              |
| Photochemical Fertilizer        | 130,951      | 66,849       |
| Mining Technical Services       | 826,117      | 1,246,824    |
|                                 | 957,068      | 1,313,673    |
| Total Assets:                   |              |              |
| Photochemical Fertilizer        | 3,808,905    | 3,748,200    |
| Mining Technical Services       | 1,062,760    | 1,526,769    |
| Total Segment Assets            | 4,871,665    | 5,274,969    |
| Itronics Inc. assets            | 23,373,109   | 22,504,867   |
| Less: inter-company elimination | (24,096,595) | (23,631,896) |
| Consolidated Assets             | \$ 4,148,179 | \$ 4,147,940 |

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ITRONICS INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2005

(UNAUDITED)

11. The Company holds marketable securities that are available for sale, which consist solely of equity securities. The carrying amount on the balance sheets of these securities is adjusted to fair value at each balance sheet date. The adjustment to fair value is an unrealized holding gain or loss that is reported in Other Comprehensive Income. At present, these unrealized gains or losses are the only component of Accumulated and Other Comprehensive Income. The Company had Accumulated Unrealized Holding Losses of \$19,642 at June 30, 2005 and \$9,568 at December 31, 2004. No gains were reclassified out of accumulated other comprehensive income into earnings during 2005 and no



losses were reclassified out of accumulated other comprehensive income into earnings during 2004. The table below illustrates the amount of unrealized holding gains and losses included in other comprehensive income, net of tax effects of \$0. The reclassification adjustment listed in the below table represents unrealized holding gains and losses transferred into earnings as securities are sold.

Following are the components of Other Comprehensive Income:

|                                      | <u>Three Months Ended June 30,</u> |             | <u>Six Months Ended June 30,</u> |             |
|--------------------------------------|------------------------------------|-------------|----------------------------------|-------------|
|                                      | <u>2005</u>                        | <u>2004</u> | <u>2005</u>                      | <u>2004</u> |
| Unrealized holding gains<br>(losses) |                                    |             |                                  |             |
| arising during the period            | \$(13,031)                         | \$ (57,886) | \$(18,043)                       | \$(110,588) |
| Reclassification adjustment          | 11,839                             | (47,213)    | 7,969                            | (179,265)   |
| Other Comprehensive Income<br>(Loss) | \$ (1,192)                         | \$(105,099) | \$(10,074)                       | \$(289,853) |

Following is a summary of gross proceeds and gains and losses from sales of available for sale marketable securities:

|                                            | <u>Three Months Ended June 30,</u> |             | <u>Six Months Ended June 30,</u> |             |
|--------------------------------------------|------------------------------------|-------------|----------------------------------|-------------|
|                                            | <u>2005</u>                        | <u>2004</u> | <u>2005</u>                      | <u>2004</u> |
| Gross proceeds from sales of securities    | \$5,947                            | \$69,744    | \$10,177                         | \$223,139   |
| Gross gains from sale of securities        | \$ -                               | \$22,044    | \$ -                             | \$ 97,802   |
| Gross losses from sale of securities       | (6,431)                            | -           | (10,116)                         | -           |
| Net Gains (Losses) from sale of securities | \$(6,431)                          | \$22,044    | \$(10,116)                       | \$97,802    |

12. The Company applies APB Opinion 25 in accounting for stock options. The following table shows a comparison of option compensation expense between this method compared to the Fair Market Value method under FASB Statement No. 123. The table also indicates the impact on net loss and loss per share:

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|                              | <u>Three Months Ended June 30,</u> |             | <u>Six Months Ended June 30,</u> |             |
|------------------------------|------------------------------------|-------------|----------------------------------|-------------|
|                              | <u>2005</u>                        | <u>2004</u> | <u>2005</u>                      | <u>2004</u> |
| Option Compensation Expense: |                                    |             |                                  |             |
| As reported                  | \$ 4,178                           | \$ -        | \$ 37,112                        | \$ 123      |

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|                                   |             |              |               |               |
|-----------------------------------|-------------|--------------|---------------|---------------|
| Adjustment for additional expense |             |              |               |               |
| for fair value of options         | 623         | 38,296       | 3,755         | 39,418        |
| Pro forma                         | \$ 4,801    | \$ 38,296    | \$ 40,867     | \$ 39,541     |
| Net Income (Loss):                |             |              |               |               |
| As reported                       | \$(819,389) | \$( 802,672) | \$(1,732,994) | \$(1,513,289) |
| Adjustment for additional expense |             |              |               |               |
| for fair value of options         | (623)       | (38,296)     | (3,755)       | (39,418)      |
| Pro forma                         | \$(820,012) | \$( 840,968) | \$(1,736,749) | \$(1,552,707) |
| Earnings (Loss) per share,        |             |              |               |               |
| basic and diluted                 |             |              |               |               |
| As reported                       | \$(0.004)   | \$(0.006)    | \$(0.009)     | \$(0.011)     |
| Pro forma                         | \$(0.004)   | \$(0.006)    | \$(0.009)     | \$(0.012)     |

**Item 2. Management's Discussion and Analysis or Plan of Operations**

Some of the information in this report contains forward-looking statements that involve substantial risks and uncertainties. You can identify these statements by forward-looking words such as "may," "will," "expect," "anticipate," "believe," "estimate" and "continue," or similar words. You should read statements that contain these words carefully because they:

- discuss our future expectations;
- contain projections of our future results of operations or of our financial condition; and
- state other "forward-looking" information.

We believe it is important to communicate our expectations. However, there may be events in the future that we are not able to accurately predict or over which we have no control. Our actual results and the timing of certain events could differ materially from those anticipated in these forward-looking statements.

Results of Operations

We reported consolidated revenues of \$557,328 for the quarter ended June 30, 2005, compared to \$626,170 for the prior year quarter, a decrease of 11%. The decrease was due to a decrease in Photochemical Fertilizer segment revenue of \$49,800, or 9% and to a decrease of \$19,000 in Mining Technical Services segment revenues, a decrease of 36%. The consolidated net loss was \$819,389, or \$0.004 per share, for the quarter ended June 30, 2005, compared to a net loss of \$802,672 or \$0.006 per share for the comparable 2004 period, an increased loss of \$16,700, or 2%. Consolidated revenues for the first six months of 2005 were \$867,301 compared to \$1,033,010 for the prior year period, a decrease of 16%. The consolidated net loss was \$1,732,994 or \$0.009 per share, for the six months ended June 30, 2005, compared to a net loss of \$1,513,289

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or \$0.011 per share for the comparable 2003 period, an increased loss of 15%.

To provide a more complete understanding of the factors contributing to the changes in revenues, operating expenses, other income (expense) and the resultant operating income (loss) and net income (loss) before taxes, the discussion presented below is separated into our two operating segments.

## PHOTOCHEMICAL FERTILIZER

|                                | Three months Ended June 30, |             | Six Months Ended June 30, |               |
|--------------------------------|-----------------------------|-------------|---------------------------|---------------|
|                                | <u>2005</u>                 | <u>2004</u> | <u>2005</u>               | <u>2004</u>   |
| Revenues                       |                             |             |                           |               |
| Fertilizer                     | \$ 484,664                  | \$ 476,910  | \$ 695,898                | \$ 706,389    |
| Photochemical recycling        | \$ 19,888                   | \$ 75,084   | \$ 42,069                 | \$ 129,643    |
| Silver                         | \$ 19,115                   | \$ 21,517   | \$ 45,874                 | \$ 64,475     |
| Total Revenue                  | \$ 23,667                   | \$ 573,511  | \$ 783,841                | \$ 900,507    |
| Gross profit (loss)            | \$ 20,718                   | \$ 42,372   | \$ (21,446)               | \$ 6,733      |
| Operating income (loss)        | \$(494,262)                 | \$(508,586) | \$(1,097,807)             | \$ (992,089)  |
| Other income (loss)            | \$(201,722)                 | \$(202,325) | \$ (365,774)              | \$ (411,095)  |
| Net income (loss) before taxes | \$(695,984)                 | \$(710,911) | \$(1,463,581)             | \$(1,403,184) |

Total segment revenues for the second quarter of 2005 were approximately \$523,700, a decrease of 9% from the prior year second quarter. Fertilizer sales for the quarter were \$484,700 (766 tons), compared to \$476,900 (839 tons) for the 2004 second quarter, an increase of 2% in dollars and a decrease of 9% in tonnage. Sales of the Chelated Liquid Micro-nutrients were \$434,700 (625 tons) and \$408,000 (646 tons) for the second quarter of 2005 and 2004, respectively, an increase of 7% in dollars and a decrease of 3% in tonnage. Sales of the Chelated Liquid Multi-nutrients were \$44,000 (141 tons) and \$56,600 (193 tons) for the second quarter of 2005 and 2004, respectively, a decrease of 22% in dollars and 27% in tonnage. The expected fertilizer sales increase did not occur due to rainy weather in the Central Valley of California that continued into late May 2005. Total photochemical recycling revenue for the quarter decreased 74%, on decreased volume of 73%, compared to the second quarter of 2004. The decrease is

due to the December 2004 mutual termination of recycling services for Shutterfly, Inc., a significant photochemical recycling customer. To offset this loss of revenue, we are concentrating our efforts on sales of Photochemical Silver Concentrators. Silver sales decreased \$2,400 from the second quarter of 2004, a decrease of 11%. Cost of sales decreased \$28,200 due primarily to a decrease of \$20,700 in payroll and related costs. The segment recorded a gross profit of \$20,700 for the quarter, compared to a gross profit of \$42,400 for the second quarter of 2004, a decreased gross profit of \$21,700, or 51%.

Segment operating expenses decreased \$36,000 from the second quarter of 2004. This resulted from modest decreases in most all of the operating expense categories.

These factors resulted in a 2005 second quarter segment operating loss of \$494,300 compared to a loss of \$508,600 for the second quarter of 2004, a decreased operating loss of \$14,300, or 3%.

Other expense decreased nominally.

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The changes in operating loss and other expenses resulted in a segment net loss before taxes of \$696,000 for the quarter ended June 30, 2005, compared to a loss of \$710,900 for the prior year quarter, a decreased loss of \$14,900 or 2%.

For the first six months of 2005, revenues were \$783,800, compared to \$900,500 for the comparable 2004 period, a decrease of 13%. The decline is due primarily to the prior year mutual termination of a significant photochemical recycling customer. Gross loss for the first six months of 2005 was \$21,400, compared to a gross profit of \$6,700 for the comparable prior year period, a decline of \$28,200. Operating loss for the first six months of 2005 was approximately \$1,097,800 compared to \$992,100 for the first six months of 2004, an increased loss of \$105,700, or 11%.

Other expense decreased \$45,300 due to a decrease in interest expense resulting from prior and current year conversions of convertible promissory notes into common stock.

The changes in operating loss and other expenses resulted in a segment net loss before taxes of \$1,463,600 for the six months ended June 30, 2005, compared to a loss of \$1,403,200 for the prior year period, an increased loss of \$60,400 or 4%.

#### MINING TECHNICAL SERVICES

|                         | Three Months Ended<br>June 30, |             | Six Months Ended June 30, |             |
|-------------------------|--------------------------------|-------------|---------------------------|-------------|
|                         | <u>2005</u>                    | <u>2004</u> | <u>2005</u>               | <u>2004</u> |
| Revenues                | \$ 33,661                      | \$ 52,659   | \$ 83,460                 | \$ 132,503  |
| Gross profit (loss)     | \$ (10,048)                    | \$ (4,800)  | \$ (9,019)                | \$ (2,894)  |
| Operating income (loss) | \$(118,706)                    | \$(113,810) | \$(261,029)               | \$(207,920) |

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|                                |             |             |             |             |
|--------------------------------|-------------|-------------|-------------|-------------|
| Other income (expense)         | \$ (4,699)  | \$ 22,049   | (8,384)     | \$ 97,815   |
| Net income (loss) before taxes | \$(123,405) | \$ (91,761) | \$(269,413) | \$(110,105) |

Mining technical services revenue was \$33,700 for the quarter ended June 30, 2005, compared to \$52,700 for the comparable quarter of 2004, a decrease of 36%. The decrease is due to prior year short term projects that did not reoccur in the current period. Cost of sales decreased by \$13,800, due primarily to decreases in labor and consulting costs of \$10,600. These factors resulted in a second quarter gross loss for the segment of \$10,000 compared to a gross loss of \$4,800 for the prior year second quarter, an increased gross loss of \$5,200.

In early May 2005 the technical services satellite office was closed due to the winding down of most of the technical service contracts and completion of the majority of the data gathering for the insidemetals.com project, but certain key staff members have been retained. Programming is continuing for insidemetals.com and launch of the website Information Portal is planned for August 2005.

The redirection of Whitney & Whitney, Inc. to reduce emphasis on technical consulting services and to launch an internet information portal is brought about by the fact that Dr. Whitney, our President, has often been the lead person in generating new consulting contracts. Our President's increased responsibilities for managing the expanding photochemical recycling segment and overall corporate activities has reduced his time availability to actively participate in the consulting segment. Part of our objective in shifting the focus of the

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technical services segment is to retain our core professional staff that can provide assistance on possible future technical service contracts as well as perform administrative duties for the photochemical recycling segment, while at the same time adding a potential source of revenue that is not dependent upon labor sales and which can be managed by a professional staff. The information portal also better utilizes the Whitney & Whitney, Inc. library and information resources that are already in existence. For the six months ended June 30, 2005 we allocated costs of approximately \$99,000 to the development of the web site. The site was launched in mid-August 2005 and we are now fine-tuning the general presentation of the site, as well as improving the profiled mining company information. We expect this level of spending to continue well into the fourth quarter of 2005. As improvements to the site are completed and information maintenance becomes routine, we will reduce or redirect staff resources as needed.

Total segment operating expenses decreased nominally, but research and development costs increased \$36,100 due to costs related to developing the insidemetals.com project, which was offset by decreases in various other operating expenses.

The combination of these factors resulted in a 2005 second quarter segment operating loss of \$118,700, compared to a loss of \$113,800 for the second quarter of 2004, an increased operating loss of \$4,900, or 4%.

Other income (loss) for the second quarter of 2005 was a loss of \$4,700 compared to a gain of \$22,000 for the prior year second quarter. This decrease is due to reduced sales of common shares of Golden Phoenix Minerals, Inc. and other marketable securities.

The changes in operating loss and other income resulted in a segment net loss before taxes of \$123,400 for the quarter ended June 30, 2005, compared to a loss of \$91,800 for the prior year quarter, an increased loss of \$31,600, or 34%.

For the first six months of 2005, segment revenue totaled \$83,500 compared to \$132,500 for the first six months of 2004, a decrease of 37%. Gross loss for the first six months of 2005 was \$9,000, compared to a gross loss of \$2,900

for the comparable prior year period, an increased gross loss of \$6,100. Operating loss for the period was \$261,000 compared to an operating loss of \$207,900 for the comparable 2004 period, an increased operating loss of \$53,100, or 26%. The primary factor contributing to the decline was research and development costs related to the insidemetals.com project.

Other income (loss) for the first six months of 2005 was a loss of \$8,400 compared to a gain of \$97,800 for the prior year period. This decrease is due to reduced sales of common shares of Golden Phoenix Minerals, Inc. and other marketable securities.

The changes in operating loss and other income resulted in a segment net loss before taxes of \$269,400 for the six months ended June 30, 2005, compared to a net loss of \$110,100 for the prior year period, an increased loss of \$159,300.

## SUMMARY

On a consolidated basis, the various changes in revenues and operating expenses resulted in a second quarter 2005 operating loss of \$613,000, compared to \$622,400 for the second quarter of

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2004, a decreased operating loss of \$9,400, or 2%. Net loss before taxes for the second quarter 2005 was \$819,400 compared to \$802,700 for the prior year second quarter, an increased loss of \$16,700 or 2%. For the six month period ended June 30, 2005 the operating loss was \$1,358,800 compared to \$1,200,000 for the prior year comparable period, an increased operating loss of \$158,800, or 13%. Net loss before taxes for the six months ended June 30, 2005 was \$1,733,000 compared to \$1,513,300 for the prior year six month period, an increased loss of \$219,700, or 15%.

## Changes in Financial Condition; Capitalization

Cash amounted to \$(30,200) as of June 30, 2005, compared to \$21,500 as of June 30, 2004. Net cash used for operating activities was approximately \$852,200 for the first six months of 2005. The cash used for operating activities during the period was financed by a combination of sales of common stock of \$570,000 from a private placement of restricted common stock and attached warrants, short term loans from an officer/stockholder of \$90,000, short term financing of \$125,000, and \$93,100 in inventory and account receivable factoring.

Total assets increased nominally during the six months ended June 30, 2005 to \$4,148,200. Current assets increased \$33,300 due to an increase in marketable securities of \$85,800 due to receipt of the final billings for services to GPXM in their restricted common stock. At June 30, 2005 we owned 567,100 shares of GPXM with a current market value of \$112,000. Net property and equipment decreased \$102,100 due to depreciation and amortization. Other assets increased \$68,500 due to the acquisition of the product rights of the GOLD n GRO Guardian fertilizer for \$71,500 in restricted common stock.

Current liabilities increased during the six months ended June 30, 2005 by \$1,754,900 and total liabilities decreased by \$237,400. Total liabilities decreased due to the conversion into common stock of a total of \$882,700 in Convertible Promissory Notes and accrued interest. This decrease was partially offset by current period accrued interest on convertible promissory notes of \$180,000, net short term financing of \$210,000, and inventory and account receivable financing \$93,100. Changes in current liabilities include increases of \$30,200 in bank overdraft, \$32,100 in accounts payable, \$93,100 in account receivable and inventory factoring, \$139,700 in accrued management salaries, \$85,000 in advances from an officer/stockholder, and \$1,739,600 in current maturities of convertible notes and accrued interest. The increase in current maturities of convertible notes is due to the reclassification from long term debt of the 2000 Series Convertible Promissory Notes that were extended to 2006 and are now due within one year of the balance sheet date. These increases were partially offset by decreases of \$76,600 in accrued expenses, which reflect payment of a

portion of federal payroll tax obligations, and \$343,600 in current maturities of long term debt, which reflects the reclassification of the mortgage obligation on the Stead manufacturing facility to long term debt.

Addressing our financial condition, improvements have been made. The stockholders' deficit, \$4,587,900 at December 31, 2002, has been reduced to a deficit of \$2,326,700 at June 30, 2005, an improvement of \$2,261,200. This has been achieved by the conversion of approximately \$4.3 million in convertible notes and accrued interest into common stock. One significant area of difficulty for us has been meeting the payments on capital lease obligations. However, the capital lease obligation at December 31, 2002 of \$1,193,900 has been reduced to \$775,000 at June 30, 2005, a reduction of \$418,900. This includes the write off of five leases as debt

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forgiveness income in 2004 of \$187,800. We expect to make further meaningful progress expanding sales and restructuring debt in 2005.

### Liquidity and Capital Resources

During the six months ended June 30, 2005, working capital decreased by **\$1,721,700** to a deficit balance of \$4,951,100. The decrease is primarily due to the reclassification from long term debt of a net \$1,739,600 in convertible notes and accrued interest. We have had limited cash liquidity since the third quarter of 2000.

To meet short term cash needs, we factor certain inventory items and receivables. This process enables us to keep limited raw materials on hand for immediate production and to obtain cash immediately upon selling product. We generally receive payment from our customers within 30 days of sales; we then repay the factoring loan. The arrangement is with unrelated individuals, carries interest at 2% to 3% per month, and is generally limited to \$120,000 at any one time. The lenders are secured by a blanket UCC on specified inventory items, which is on file with the State of Nevada. A UCC form is also filed for individual invoices to further secure the lender.

We have sought and obtained the funding described above, which has not been sufficient to maintain all obligations on a current basis. Other factors limiting cash liquidity include fertilizer sales not expanding at the rate originally anticipated, so operating losses were not reduced as much as expected and the \$15 million equity line of credit agreement with Swartz Private Equities, LLC (Swartz) expired in February 2004. A private placement of stock with attached warrants was closed in June 2005, with \$570,000 received during the six months ended June 30, 2005. In July 2005 we obtained 8% convertible debt financing for up to \$3.25 million, with the final amount dependent upon the filing and effectiveness of a registration statement relating to common shares underlying the convertible debt and warrants issued in the recent financing. The funding will provide for working capital, manufacturing plant expansion, registration of GOLD n GRO Guardian fertilizer with the EPA, and debt reduction. It is anticipated that this funding will provide for our capital needs through March to June 2006, depending on fertilizer sales growth

There has been a long term commitment by officers and other members of management to support us by investing funds for our growth. One officer/shareholder has invested a total of \$1,403,900 in cash and deferred salary during the period 2001 through June 30, 2005. Two other members of management have deferred salary totaling \$550,500 during the period 2001 through June 30, 2005. Additional members of management invested \$62,000 cash in 2003. All cash and deferred salary that have been invested in our private placements were under the same terms and conditions as all other investors.

We believe that the business plan implementation needs to be accelerated to meet profitability goals and believe that can be accomplished upon obtaining sufficient capital.

The actual rate of growth in fertilizer and the related photochemical and silver sales necessary to achieve profitability is subject to a number of uncertainties, including the annual seasonal nature of fertilizer sales related to crop cycles,

short term weather patterns in specific markets, and the availability of funding to support sales growth.

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## Growth Plans and Implementation

Our Photochemical Fertilizer Division created the GOLD n GRO line of liquid fertilizers. The pioneering development work is complete, field trials have been completed on the first products and other field trials are under way.

The Mining Technical Services Division, originally provided typical consulting services which required high level technical personnel, including our President, devoted to each project. To reduce our dependence on our President to generate new consulting contracts, while better utilizing our core professional staff, the division is being reconfigured to focus most of its efforts on a global Internet Information Portal "insidemetals.com". The information portal operates 24 hours per day 7 days per week anywhere in the world where computers and the Internet are available. Anyone with access to the Internet anywhere in the world can subscribe to the service at any time using their credit card to pay the subscription fee.

With the successful completion of the initial pioneering development work by the Photochemical Fertilizer Division, and with the launch of the information portal by the Mining Technical Services Division, we are implementing growth plans for both divisions that are expected to drive expansion well into the future. The status of these plans and their implementation is described for each division.

### Photochemical Fertilizer Division (Itronics Metallurgical, Inc.)

Our manufacturing plant is presently configured to produce 1.2 million gallons (on a single shift basis) of GOLD n GRO fertilizer annually (about 5,700 tons) and can be expanded to produce 7.2 million gallons of GOLD'n GRO per year, or about 36,000 tons. GOLD'n GRO fertilizer production in 2004 utilized about 5 percent of planned capacity. Planned expansions to achieve the 36,000 ton volume include increasing both dry raw material and liquid storage, increasing tank truck loading capacity, and automation of certain manufacturing functions. Expansion can be achieved incrementally as fertilizer sales continue to grow.

We have developed the following eight-part approach to growth:

1. Increase sales in the established market segments.
2. Develop GOLD'n GRO fertilizer applications for more crops.
3. Expand sales to new territories.
4. Expand the GOLD'n GRO specialty fertilizer product line.
5. Complete development of and commercialize the new glass/tile products.
6. Develop and commercialize environmentally friendly metal leaching reagents for recovery of silver, gold, and other metals.
7. Continue facilities expansion and technology development.
8. Acquire established companies and/or their technologies.

Plans and status of implementing each of the growth categories is explained in more detail in the following sections.



1. Increase sales in established market segments.

We are selling into or developing applications for the three major segments. These are:

a. Specialty Agriculture which includes Avocados, Citrus, Grapes, Fruit and Nut Trees, and Vegetables.

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b. Bulk Field Crops which include alfalfa, cereal grains, corn, cotton, and soybeans.

c. The Urban Market, which includes Home Lawn and Garden, Landscape Construction and Maintenance, and Nursery and Greenhouse markets, and Golf Courses.

Our primary focus is to increase bulk GOLD 'n GRO liquid fertilizer sales as rapidly as possible. This is being achieved by expanding sales in the Specialty Agriculture segment and in the Bulk Field Crops segment. There are on-going small package sales in the Urban Market, but these are small relative to the other two segments.

2. Develop GOLD'n GRO fertilizer applications for more crops.

Based on our experience to date, it takes approximately two to five years to develop each fertilizer product, which includes regulatory approval. It typically takes another two to four years to achieve market acceptance of successful products, which includes field trials to demonstrate product effectiveness

New product applications are being developed for the dairy cow feed market including young oats, alfalfa, hay, and silage corn. Trials were conducted in 2004. The nutrient content of the alfalfa was improved, in some cases to the highest quality ratings. This benefits the dairy because less nutrient supplements are required for feeding the cows, thus reducing dairy operating expenses. The amount of hay produced per acre increased up to 25 percent. Results of the corn crops are still being evaluated. The dairy cow feed market is large with more than 23 million acres of alfalfa hay being grown in the United States. We anticipate it will take another one to three years to complete development and launch these product applications.

In 2004, we began field trials in Idaho, Oregon, and Washington for applications on onions, potatoes, and winter wheat. In the second quarter of 2005, we began field trials in Rhode Island for lawn and landscape application. Also in the second quarter, we started several new trials in California for silage corn applications.

A new GOLD'n GRO base liquid nutrition program is now being marketed. The program is called the "Gallon and a Quart" or "4 to 1" program. It calls for one gallon of GOLD 'n GRO base liquid for each quart of GOLD'n GRO chelated micro-nutrient used in soil applications. Field demonstrations have shown improved nutrition uptake and crop output under this cost effective program. Marketing of this program over the next two to three years is expected to produce a very substantial increase in the tonnage of GOLD'n GRO fertilizers sales.

3. Expand sales to new territories.

The GOLD'n GRO products are being sold in Arizona, California, Colorado, Idaho, Nevada, Oregon, Rhode Island, and Washington, with the majority of our sales in central California. We completed registration of select GOLD 'n GRO fertilizers in Idaho, Oregon and Washington during the first quarter of 2005; sales development is now underway. Two GOLD'n GRO products are registered in seven northeastern states and all of the products are

registered in New York and in New Jersey with a distributor agreement signed for New Jersey. Based on our experience, commercial sales can be generated approximately one year after introductory sales activities

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are initiated. We are in the process of identifying distributors for New York and the other seven northeastern states. Each new geographic area developed will require the same procedural approach.

Our plan to expand sales in Urban Markets requires the consumer to utilize fertilizer injection equipment. This equipment provides economical, easy use of liquid fertilizers for consumer lawns and gardens. We recently added two types of fertilizer injectors to our "e" store, which is the first step into this market. Additionally, other fertilizer injectors are already available to consumers through irrigation supply stores.

4. Expand the GOLD'n GRO specialty fertilizer product line.

We are developing two new specialty product lines, calcium plus magnesium fertilizer and a high magnesium content fertilizer, both targeting foliar and soil application. We expect to launch sales of the calcium plus magnesium product in the second half of 2005 and the magnesium in 2006 or 2007.

We are developing a new category of repellent fertilizers that are expected to be sold at higher profit margins than our other products. The GOLD n GRO Guardian animal repellent fertilizer is an example of this type of specialty fertilizer. The U.S. market for animal repellents is believed to exceed \$50 million in annual sales. Products currently in the market have limited effectiveness so there is a real opportunity for a line of systemic products that are effective for several weeks after each application. GOLD'n GRO Guardian small plot tests have shown effectiveness for 8 to 12 weeks as well as excellent wintertime effectiveness.

In the second quarter of 2005 we acquired ownership interest in the GOLD n GRO Guardian trademark, product rights, and the repelling product. We now own 100% of all rights related to GOLD n GRO Guardian. Results of the research of the GOLD n GRO Guardian animal repellent fertilizer has provided a basis for a bird (goose) repellent fertilizer that will be perfected for small plot field trials and registration after the registration of GOLD n GRO Guardian is underway. Currently, this product line is strictly for non-food plant applications.

We believe the users of the GOLD n GRO animal repellent/fertilizer will be upscale homeowners, commercial landscapers, and municipal facilities, and wholesale and retail nurseries. The initial sales center will be in Rhode Island.

5. Complete development of and commercialize glass/tile products.

In 2003, we developed and produced glass /tile products proving that the product concept is technically viable. When the development of the glass/ceramic tile product is completed, we will achieve the ability to recycle 100 percent of the photoliquid materials received from customers, including waste that is generated internally during fertilizer production. We have completed preliminary market research for the tile markets, but expect to do much more work to develop a plan to enter this market.

6. Develop and commercialize metal leaching reagents for recovery of silver, gold, and other metals.

In 2002 and 2003, we initiated efforts to apply our technology to extract silver from photoliquids to the mining sector. This work will be further expanded and a small pilot circuit will be established to chemically process certain categories of silver-bearing solid wastes.

The gold mining sector currently uses cyanide and other toxic chemicals in their leaching process. We believe it may be possible to create and adapt new non-toxic leaching reagents and leaching procedures for processing other secondary materials and certain types of mine generated products. The specific markets for leaching reagents in gold and silver mining is large and world wide, but has not yet been studied in detail for market development. Our Technical Services Division maintains an extensive library and database of mines and mining activities worldwide, which provides us ready access to market information as we need it. Much pilot plant work, including one or more field pilot operations, must be completed before this can be done.

7. Continue facilities expansion and technology development.

As fertilizer sales volume increases, we will need to increase tank truck loading capacity. With the introduction of additional bulk products and increased demand for our products, load out capacity for shipment of three more bulk products is needed. We developed a preliminary construction budget and are seeking financing so that construction can be scheduled. While we believe that we can handle expected growth in 2005 with the existing load-out module, we hope to complete construction on the new load out equipment during the first quarter of 2006.

8. Acquire established companies and/or their technologies.

To enhance our operations and market presence, we intend to acquire small established companies or their technologies. In 2005, we completed our acquisition of the GOLD n GRO Guardian technology. We have decided to delay any further acquisitions until additional financing is obtained.

Mining Technical Services Division (Whitney & Whitney, Inc.)

Historically, this division provided consulting services to the mining industry. In August 2005, we launched an Information Portal in the Internet. This division has a two-part approach to growth:

1. Continue to provide consulting services.
2. "e-commerce" Internet Information Portal-"insidemetals.com".

Plans and status of implementing each of the growth categories is explained in more detail in the following sections.

1. Continue to provide consulting services

During the third quarter of 2004, sales of the Mining Technical Services (Whitney & Whitney, Inc.) division declined due to winding down of on-going projects and delays related to client financing for new projects. Some of the issues related to new client project start up were resolved by the clients during the third quarter of 2004 and the remaining work was completed in early 2005. The technical services satellite consulting office was closed in early May, but certain key staff members have been retained. We intend to continue a low level effort to solicit and perform technical services for mining companies and other businesses or government agencies that have mineral interests or minerals related responsibilities.

2. "e-commerce" Internet Information Portal-"insidemetals.com".

In August 2005, we launched the website "insidemetals.com," an Information Portal targeting the companies and individuals interested in the mining and precious metals industry. The website will generate revenue by charging a

subscription fee for monthly access to the site. Currently, the site contains an array of information about gold and companies in the gold industry. We intend to add information on other mineral sectors gradually over time.

We anticipate that mining company professionals, all government agencies with minerals related responsibilities, financial industry investment professionals, and individual investors who have an interest in investing in mining companies but who have limited mineral industry knowledge will benefit from this Information Portal. The market scope for this service is global and is accessible with a "click of a mouse" in all countries of the world through the Internet. Whitney & Whitney, Inc. has contacts throughout the world and expects that the good will generated over a period of more than 25 years will provide market support for this service.

### Item 3. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures. As of the end of the period covered by this report, we conducted an evaluation, under the supervision and with the participation of our chief executive officer and chief financial officer of our disclosure controls and procedures (as defined in Rule 13a-15(e) and Rule 15d-15(e) of the Exchange Act). Based upon this evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures are effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms.

(b) Changes in internal controls. There was no change in our internal controls or in other factors that could affect these controls during our last fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting."

## PART II- OTHER INFORMATION

### Item 1. Legal Proceedings

We may become involved in a lawsuit or legal proceeding at any time in the ordinary course of business. Litigation is subject to inherent uncertainties, and an unexpected adverse result may arise that may adversely affect our business. Certain lawsuits have been filed against us for collection of funds due that are delinquent, as described below. We are currently not aware of any litigation pending or threatened for any reason other than collection of funds due and already recorded. We are not aware of any additional legal proceeding or claims that we believe will have, individually or in the aggregate, a material adverse affect on our business, financial condition or operating results.

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As of June 30, 2005 total recorded liabilities of \$802,166 including accrued interest to June 30, 2005, were subject to a total of 15 separate lawsuits for the collection of the funds due. These include 12 leases totaling \$604,896 (reflected in Current Maturities of Capital Lease Obligations) plus \$56,960 in additional interest (reflected in Accrued Interest) and three trade payables totaling \$129,191 (reflected in Accounts Payable) plus \$11,119 in additional interest (reflected in Accrued Interest). The leases are individually secured by specified equipment.

The accrued interest noted above was recorded based on our assessment of additional amounts we believe is probable and is related to four cases originally seeking \$423,375; the creditors have received judgments in three of these cases and the fourth is in litigation. We will continue to accrue interest until these cases are settled or paid in full.

We estimate an additional \$48,600 interest may be reasonably possible on other cases; however, we have not accrued this amount because we do not believe it is probable to be incurred. This estimate is related to four cases, three of which, originally seeking a total of \$181,672, are presently in settlement negotiations with creditors' counsel. An offer to settle the three cases for less than our recorded liability has been received; if we accept the offer, the Company will incur a small gain. The fourth case, seeking \$35,210, was filed in March 2003, and no further contact has taken place since then. During the third quarter of 2005, we paid off one suit totaling \$36,626 including interest and costs of \$17,200 that had not been accrued; this loss will be recorded in the third quarter.

We have six other cases that we deem to have a remote possibility of incurring an additional unrecorded loss. As of June 30, 2005, we were delinquent on these cases with a recorded liability of \$95,383. All six have since been brought current.

Successful settlement of the above claims is dependent on future financing.

As of December 31, 2004 certain subsidiaries were delinquent on approximately \$206,200 in federal payroll taxes. These amounts are included Accrued expenses in the Balance Sheet. Subsequent to June 30, 2005, the taxes were paid in full.

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## Item 2. Changes in Securities and Use of Proceeds

### (c) Recent Sales of Unregistered Securities:

In June 2005, we issued an aggregate of 200,000 shares of common stock to one accredited investor at \$0.05 per share for a total of \$10,000. In addition, we issued to this investor a three year warrant to purchase an aggregate of 100,000 shares of common stock at an exercise price \$0.075 per share during the first year, \$0.15 per share during the second year, and \$0.225 per share during the third year.

During the second quarter of 2005, we issued an aggregate of 474,660 shares of common stock to three accredited investors who converted \$47,466 in convertible promissory notes and accrued interest into common stock at a conversion price of \$0.10 per share.

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In May 2005, we issued an aggregate of 1,000,000 shares of common stock valued at \$71,500 to Howland S. Green, our Director, for the purchase of his product rights in the GOLD n GRO Guardian fertilizers. In addition, we issued to Mr. Green a warrant to purchase an aggregate of 1,000,000 shares of common stock at an exercise price of \$0.10 per share. The first 500,000 shares of the warrant will vest when the Federal EPA accepts the registration application for the GOLD n GRO Guardian and the second 500,000 shares of the warrant will vest when the Federal EPA issues the registration for the GOLD n GRO Guardian. The entire warrant is exercisable for two years after the EPA registration is received.

In May 2005, we issued an aggregate of 2,500 shares of common stock valued at \$250 to John W. Whitney, our President, as compensation for services performed on our behalf in his capacity as a director of our company for the first quarter of 2005.

In June 2005, we issued an aggregate of 62,500 shares of common stock valued at \$3,750 to Cervelle Group LLC as compensation for consulting services performed on our behalf.

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In August 2005, we issued an aggregate of 2,500 shares of common stock valued at \$150 to John W. Whitney, our President, as compensation for services performed on our behalf in his capacity as a director of our company for the second quarter of 2005.

In August 2005, we issued shares of common stock to the following management employees for accrued interest through June 30, 2005 on their unpaid salaries. Interest is paid at 12% per annum and the share price is calculated monthly using the weighted average of the closing bid prices.

John W. Whitney, President            371,232 shares valued at \$28,263

Michael C. Horsley, Controller       212,538 shares valued at \$15,890

In August 2005, we issued an aggregate of 21,444 shares of common stock, valued at \$1,664, to one employee for accrued interest through June 30, 2005 on his unpaid salary. Interest is paid at 12% per annum and the share price is calculated monthly using the weighted average of the closing bid prices.

Interest earned by Duane H. Rasmussen, our Vice President, on his unpaid salary during the period July 1, 2004 through June 30, 2005 amounted to \$37,430 and will be paid with 500,703 restricted common shares. The shares remain unissued due to income tax considerations.

We issued options to purchase an aggregate of 9,000 shares of common stock to Michael C. Horsley, our Controller on May 1, 2005. The options are exercisable at \$0.15 per share and expire three years after grant.

We issued options to purchase an aggregate of 21,000 shares of common stock to four of our employees on May 1, 2005. The options are exercisable at \$0.15 per share and expire three years after grant.

Unpaid salary due two management employees in the amount of \$10,800 is to be paid with an aggregate of 170,133 shares of common stock. These shares were earned as part of the employee savings plan during the second quarter of 2005 and will be issued when sufficient cash is available to pay the required payroll tax withholding. The number of shares are calculated each month for all employees participating in the plan by using the weighted average of the closing

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bid prices for the respective month. The amounts and related number of shares earned by quarter for each of the employees follows:

|                                       | <u>Amount</u> | <u>Shares</u> |
|---------------------------------------|---------------|---------------|
| Duane H. Rasmussen, Vice<br>President | \$ 6,000      | 94,518        |
| Michael C. Horsley, Controller        | 4,800         | 75,615        |
|                                       | \$10,800      | 170,133       |

During the three months ended June 30, 2005, the accrued interest on the 2000 through 2002 Series Convertible Promissory Notes resulted in the granting of additional options to purchase an aggregate of 892,282 shares of common stock. The options are exercisable at prices ranging from \$0.10 to \$1.18.

All of the above offerings and sales were deemed to be exempt under rule 506 of Regulation D and Section 4(2) of the Securities Act of 1933, as amended. No advertising or general solicitation was employed in offering the securities. The offerings and sales were made to a limited number of persons, all of whom were accredited investors, business associates of Itronics Inc. or executive officers of Itronics Inc., and transfer was restricted by Itronics Inc. in accordance with the requirements of the Securities Act of 1933. In addition to representations by the above-referenced persons, we have made independent determinations that all of the above-referenced persons were accredited or sophisticated investors, and that they were capable of analyzing the merits and risks of their investment, and that they understood the speculative nature of their investment. Furthermore, all of the above-referenced persons were provided with access to our Securities and Exchange Commission filings.

Except as expressly set forth above, the individuals and entities to whom we issued securities as indicated in this section of the registration statement are unaffiliated with us.

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Item 3. Defaults Upon Senior Securities

As of June 30, 2005 lease payments totaling \$796,216 were in arrears. As required by U.S. Generally Accepted Accounting Principles, the principal balance of the leases that are in default have been classified as current liabilities. The Company is in ongoing communication with the lessors to avoid action that may be adverse to the Company.

In 2003 an offer was made to extend the Series 2000 Convertible Promissory Notes. The holders of \$80,000 of the Notes have not responded to the offer and that amount, plus \$55,452 in accrued interest, remains in default.

As of June 30, 2005, the Company was delinquent on real property taxes in the amount of \$14,630 plus interest and penalties and was delinquent two monthly payments totaling \$13,202 plus late charges on the promissory note. This is a default of the promissory note and deed of trust secured by the Stead manufacturing facility. The lender was aware of the situation and took no collection action. Subsequent to June 30, 2005 the taxes and payments were brought current. In accordance with U.S. Generally Accepted Accounting Principles, the long term portion of the principal balance of the note, in the amount of \$458,081, which would otherwise have been classified as a current liability, has been classified as a long term liability.

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Item 6. Exhibits and Reports on Form 8-K

|                  |                                                 |    |
|------------------|-------------------------------------------------|----|
| (a) Exhibit 31.1 | CERTIFICATION OF PRESIDENT PURSUANT TO SECTION  |    |
|                  | 302 OF THE SARBANES-OXLEY ACT OF 2002           | 30 |
| Exhibit 31.2     | CERTIFICATION OF CONTROLLER PURSUANT TO SECTION |    |
|                  | 302 OF THE SARBANES-OXLEY ACT OF 2002           | 32 |
| Exhibit 32       | CERTIFICATIONS OF PRESIDENT AND CONTROLLER      |    |
|                  | PURSUANT TO 18 U.S.C. SECTION 1350 AS ADOPTED   |    |
|                  | PURSUANT SECTION 906 OF THE SARBANES-OXLEY ACT  |    |
|                  | OF 2002                                         | 34 |

(b) Reports on Form 8-K

Following is a list of Forms 8-K filed during the three months ended June 30, 2005:

|                |                                                                                                           |
|----------------|-----------------------------------------------------------------------------------------------------------|
| April 4, 2005  | Announced registration of nine GOLD n GRO fertilizer products was completed in Oregon.                    |
| April 20, 2005 | Announced Mr. Howland Green was appointed to the Board of Directors.                                      |
| May 17, 2005   | Announced completion of the acquisition of the product rights to GOLD n GRO Guardian fertilizer products. |
| June 2, 2005   | Announced sales and operating results for the year ended December 31, 2004.                               |

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SIGNATURES

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

ITRONICS INC.

DATED: January 6, 2006

By: /S/JOHN W. WHITNEY

John W. Whitney

President

(Principal Executive Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the Company and in the capacities and on the dates indicated

DATED: January 6, 2006

By: /S/JOHN W. WHITNEY

John W. Whitney



President

(Principal Executive Officer)

DATED: January 6, 2006

By: /S/MICHAEL C. HORSLEY

Michael C. Horsley

Controller

(Principal Accounting Officer)