

ITRONICS INC  
Form 10KSB  
April 16, 2008

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, DC 20549  
FORM 10-KSB

(Mark One)

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

For the fiscal year ended **December 31, 2007**

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

For the Transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 33-18582

**ITRONICS INC.**

(Name of small business issuer in its charter)

Texas 75-2198369

(State or other jurisdiction of (I.R.S. Employer Identification Number)  
incorporation or organization)

6490 South McCarran Boulevard, Building C, Suite 23 Reno, Nevada

89509

(Address of Principal Executive Offices) Zip Code

Issuer's telephone number: (775) 689-7696

Securities registered under Section 12(b) of the Exchange Act:

Edgar Filing: ITRONICS INC - Form 10KSB

Title of each class Name of each exchange on

which registered

None None

Securities registered under Section 12(g) of the Exchange Act:

None

(Title of class)

Check whether the issuer is not required to file reports pursuant Section 13 or 15(d) of the Exchange Act. ( )

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 (x) No ( )

Check if disclosure of delinquent filers in response to Item 405 of Regulation S-B is not contained in this form, and no disclosure will be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB. (x)

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

State issuer's revenues for its most recent fiscal year: \$2,342,296.

The aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the average bid and asked price of such common equity, as of March 31, 2008, was \$6,439,679.

As of March 31, 2008 there were issued and outstanding 999,996,999 shares of the Registrant's Common Stock.

DOCUMENTS INCORPORATED BY REFERENCE

None

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



ITRONICS INC. AND SUBSIDIARIES

2007 FORM 10-KSB ANNUAL REPORT

TABLE OF CONTENTS

| <u>PART I</u>   |   | <u>PAGE</u> |
|-----------------|---|-------------|
| Item 1.         | Description of Business   | 4           |
| Item 2.         | Description of Property   | 19          |
| Item 3.         | Legal Proceedings   | 19          |
| Item 4.         | Submission of Matters to a Vote of Security Holders   | 20          |
| <u>PART II</u>  |   |             |
| Item 5.         | Market for Common Equity and Related Stockholder Matters and<br><b>Small Business Issuer Purchases of Equity Securities</b> | 20          |
| Item 6.         | Management's Discussion and Analysis or Plan of Operation   | 24          |
| Item 7.         | Financial Statements  | 35          |
| Item 8.         | Changes in and Disagreements with Accountants on<br><b>Accounting and Financial Disclosure</b>                              | 35          |
| Item 8A         | Controls and procedures   | 35          |
| <u>PART III</u> |   |             |

## Edgar Filing: ITRONICS INC - Form 10KSB

|          |  |    |
|----------|--|----|
| Item 9.  | Directors, Executive Officers, Control persons and Corporate<br><b>Governance; Compliance with Section 16(a) of the Exchange<br/>Act</b> | 37 |
| Item 10. | Executive Compensation   | 39 |
| Item 11. | Security Ownership of Certain Beneficial Owners and<br><b>Management and Related Stockholder Matters</b>                                 | 41 |
| Item 12. | Certain Relationships and Related Transactions, and Director<br><b>Independence</b>  | 43 |
| Item 13. | Financial Statements and Exhibits  | 44 |
| Item 14. | Principal Accountant Fees and Services   | 82 |

## ITEM 1.

### DESCRIPTION OF BUSINESS.

#### **INTRODUCTION**

We are the inventor and developer of the "Beneficial Use Photochemical, Silver, and Water Recycling" technology that produces environmentally beneficial GOLD'n GRO fertilizers and silver bullion.

We are an environmental process technology company that has developed what we believe is a unique technology for photochemical recycling. We, through our subsidiary, Itronics Metallurgical, Inc., extract more than 99% of the silver and virtually all of the other toxic heavy metals from used photoliquids and use this "Beneficial Use Photochemical, Silver and Water Recycling" technology to produce environmentally beneficial chelated liquid fertilizer sold under the trademark GOLD n GRO, deer repellent/fertilizer to be sold under the trademark GOLD n GRO Guardian, and silver bullion. We also provide development planning and technical services to the mining industry.

#### **OUR PRODUCTS AND SERVICES**

We currently operate the following two business segments under separate wholly owned subsidiaries:

**GOLD n GRO Fertilizer:** This segment, known as Itronics Metallurgical, Inc., operates a fertilizer manufacturing, photochemical recycling, and silver refining facility. Revenues are generated by photochemical management services, sales of photochemical silver concentrators, sales of silver, and sales of GOLD n GRO liquid fertilizers.

#### **Mining Technical Services**

: This segment, known as Whitney & Whitney, Inc. (WWI), provides mineral project planning and technical services to the mining industry. It has specialized knowledge in all aspects of mineral project development and has been deeply involved in gold mine development for more than 25 years. It employs technical specialists with expertise in the areas of mining, geology, mining engineering, mineral economics, material processing, and technology development. Technical services have been provided to many of the leading U.S. and foreign mining companies, several public utilities with mineral interests, to various state agencies, the U.S. and foreign governments, and the United Nations and the World Bank. WWI was under contract with the Country of Bolivia from 1986 through early 1992 to assist it in developing its mining industry. In 2005 WWI launched an internet website to provide gold mining company profiles to the interested public.

We have three wholly owned subsidiaries, Whitney & Whitney, Inc. ("WWI"), Itronics Metallurgical, Inc. ("IMI"), and Itronics California, Inc. (ICI), a 92.5% owned partnership, Nevada Hydrometallurgical Project ("NHP"), and an 82.53% owned joint venture, American Hydromet. A brief description of each organization follows:

Itronics Metallurgical, Inc.

:

IMI was established in 1981 to manage the metallurgical and materials processing operations being developed under WWI and American Hydromet research and development programs. IMI has been the main provider of management services to American Hydromet since 1986. IMI is now managing the photochemical/GOLD'n GRO fertilizer segment as discussed below.

Nevada Hydrometallurgical Project

:

Nevada Hydrometallurgical Project ("NHP") is a research and development partnership formed in 1981 to fund research into potential commercial applications for certain hydrometallurgical process techniques developed by the U.S. Bureau of Mines Research Center in Reno, Nevada between 1970 and 1979. A number of potential commercial applications were defined by NHP, one of which is the American Hydromet silver/gold refining technique. In late 1985, NHP assigned its interest in the silver/gold refining technique to American Hydromet. NHP retained its proprietary interest in the other potential commercial applications for future developments. NHP continues as a financing and technology owning partnership. We own 92.5% of NHP.

American Hydromet

:

American Hydromet is a Nevada joint venture that was formed in 1985 to develop certain silver and gold refining/recovery technology and to create business based upon such technology. The GOLD n GRO fertilizer segment now being managed by IMI is owned by American Hydromet. The ownership interests in American Hydromet are: NHP for 76.5%, IMI for 1%, and American Gold & Silver Limited Partnership ("AG&S") for 22.5%. AG&S is a Nevada limited partnership, for which WWI serves as the general partner and owns a general and limited partnership interest totaling 11%. We own a 37% limited partnership interest in AG&S. In total, we own approximately 83% of American Hydromet.

Itronics California, Inc.

:

Itronics California, Inc. (ICI) was acquired in March 1999 by Itronics Metallurgical, Inc. ICI, originally named PD West, Inc., was acquired for its phosphoric acid recycling technology. ICI has no business operations but plans are to utilize the phosphoric acid technology and to eventually operate IMI's photochemical services and GOLD'n GRO fertilizer business in California.

Whitney & Whitney, Inc.

:

WWI was incorporated in 1977. WWI was primarily a mineral consulting firm that provided planning and technical services to the mining industry. WWI is now further developing an internet website originally launched in 2005 to provide gold mining industry data to the investing public, while maintaining a presence in the technical consulting field.

SUMMARY HISTORY OF OPERATIONS

Whitney & Whitney, Inc. was established to provide a wide range of technical services to the mining industry. During the 1980's, WWI completed several multi-client fertilizer marketing studies. Also during this time period, WWI was contacted by state and local environmental officials concerning the problem of photographic wastes, laden with silver and other toxic heavy metals, being dumped in local sewer systems.

Over the years, the mining technical services business was highly cyclical, closely following the base and precious metals industries, and specifically, the price of copper, other base metals and gold. This condition pointed out the necessity of expanding our business into new industries. When considering the fertilizer marketing studies previously performed, along with the growing national issue of sewer system contamination from toxic photowastes and silver toxicity to fish, it seemed to be a natural extension of WWI's existing expertise to expand into the photowaste recycling business. In 1987 the decision was made to move forward with research and development of a process to extract silver from photographic liquid wastes. It took until 1997 to develop and demonstrate a satisfactory fertilizer and to complete university testing to demonstrate its agronomic viability.

In March 1998 IMI signed a five year definitive licensing, manufacturing, and distribution agreement with Western Farm Service, Inc. (WFS), one of the largest liquid fertilizer bulk retailers in the western United States. The agreement was renewed in March 2003 for another five years and again in March 2008, subject to annual cancellation provisions. The agreement grants WFS an exclusive license and right to manufacture and market IMI's GOLD'n GRO line of bulk liquid fertilizer products for the Turf & Ornamental and Specialty Agricultural markets in the states of Arizona, California, Hawaii, Idaho, Oregon, and Washington. WFS has approximately 100 agricultural retail outlets in these states. In the discussion below, and elsewhere in this report, we refer to this group of retail outlets as our licensed distributor network.

A 35,000 square foot manufacturing plant in Reno/Stead, Nevada was purchased in 1999. Construction of the liquid processing area was completed in early 2000, and a "shake-out" period was completed in which small batches of photochemicals were processed and small batches of fertilizer were manufactured. By late 2000 the new facility had demonstrated the ability to "demetallize" the received photo liquids to required EPA levels, thereby proving the technical viability of the new technology on a commercial scale. By the first quarter of 2001 we were positioned to develop sales for more than a dozen liquid fertilizer products.

By the end of 2003, we had developed 13 fertilizers covering two categories: chelated liquid multinutrient fertilizers and chelated liquid micronutrient fertilizers. The fertilizers are sold both to the general public and through licensed and non-licensed distributors.

We are developing a deer repellent/fertilizer that will be sold under the trademark GOLD'n GRO Guardian. This product will use one of the GOLD'n GRO multi-nutrient liquid fertilizers as a base liquid, which has the property of being taken into the plant as a fertilizer and imparting odor and taste characteristics that are offensive to deer and other animals, such as rabbits, that eat plants. The GOLD'n GRO Guardian product was field tested during 2003 and was subsequently approved for use by the North American Deer Management Network. GOLD'n GRO Guardian is a repellent fertilizer and must be registered under both the pesticide regulations and the fertilizer regulations for each state in which it will be sold. The product must also be registered with the U.S. Environmental Protection Agency (U.S EPA) as a biopesticide. Introduction of this product for commercial sales will be delayed until the registrations are completed. In 2005 we acquired the interest in the GOLD n GRO Guardian trademark, product rights, and the repelling product formula owned by Mr. Howland Green. We now own 100% of all rights related to GOLD n GRO Guardian. Mr. Green has become one of our directors and is Northeast Manager for GOLD n GRO Sales Development. Substantial funding over the next 24 months will be required to complete the U.S. EPA and California registration process and to begin manufacturing and sales.

During the period 1999 through 2003 we developed a "low temperature vacuum distillation" machine that operates at room temperature and is able to remove up to 80% of the water from photochemical solutions without damaging the chemicals, producing a high silver content concentrate that can be shipped as a commercial product in inter-state



commerce. The distilled water is clean enough for re-use on site and the reduction in volume of material needing to be shipped produces an 80 percent reduction in transportation cost making shipment possible anywhere in the United States. These machines are being sold under the trademark "Itronics Metallurgical Photochemical Silver Concentrators".

After we began producing fertilizer, we noted that the by products of the process were the main materials needed to manufacture glass and ceramic. Therefore we began research and development of glass and tile formulations. During 2003, the first pieces of glass/ceramic tile were produced. With the successful development of a glass/ceramic tile product, we achieve the ability to recycle 100 percent of the materials received from customers, including waste that is generated internally during processing. The silver refining technology and the glass/ceramic tile products development efforts are being expanded in parallel with expansion of GOLD'n GRO fertilizer sales.

A more detailed discussion of our business, based on our two business segments described above, follows.

## GOLD n GRO FERTILIZER

### Operations

We operate a commercial scale plant to receive used photochemical liquids, recover the silver and other metals, and convert the demetallized liquids to liquid GOLD'n GRO fertilizer products. A critical component of this integrated manufacturing system is to match, within a reasonable range, the incoming volume of photochemical liquids with the utilization of those liquids in fertilizer or other manufactured products.

Photochemical services operates as a regional business in northern Nevada, serving more than 200 customers in the northern Nevada market. A satellite service operation has been established in the San Francisco Bay Area which is a large market with at least three strong competitors. We believe we are able to compete effectively based upon pricing and service quality. In October 2006 we began servicing a large company in northern Nevada and in November 2006 we began servicing a large company in the San Francisco Bay Area.

Growth of silver bullion output is driven by photochemical processing to support GOLD'n GRO fertilizer sales. There are some opportunities to expand silver output separate from photochemical recycling, but profit margins for the refining services are very small when compared to the inventory requirements and the security risk. Because of these factors, gold and silver refining services are limited to categories of materials where our proprietary technology can be used and that offer better profit margins than conventional precious metal refining. We will be actively looking at opportunities to expand this segment in future years.

Spent photochemical liquids received from customers are logged and recorded, then tested for silver content and contaminants. We achieve high contaminant control standards by working proactively with our regular customers. Once testing is completed, the photographic solutions are available for processing.

-

-

-

### Growth Plans and Implementation

With the successful completion of the initial pioneering development work by the GOLD n GRO Fertilizer Division, we are implementing growth plans that are expected to drive expansion well into the future. The status of these plans and their implementation is described below.

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 2007 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 is being done 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.
- 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 a new 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.

We are performing field trials in Idaho, Oregon, and Washington for applications on onions, potatoes, and winter wheat. We also have begun field trials in Rhode Island for lawn, landscape, and nursery application and have started several new trials in California for silage corn applications.

A GOLD'n GRO base liquid nutrition program is 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 is expected to produce substantial increases in the tonnage of GOLD'n GRO fertilizer sales.

In 2006 we began contributing to an ongoing Zinc Nutrition Research Program at Utah State University in Logan, Utah. To date, the research has demonstrated the effectiveness of GOLD n GRO 9-0-1+7% Zinc as a chelated liquid zinc micronutrient fertilizer for zinc deficient corn. Results include preventing visual symptoms of zinc deficiency, significantly increased tissue concentration of zinc compared to untreated plants, and doubled dry mass.

### 3. Expand sales to new territories.

The GOLD'n GRO products are being sold in Arizona, California, Colorado, Idaho, Nevada, Oregon, Rhode Island, Washington, and Utah, with the majority of our sales in central California. We completed registration of select GOLD n GRO fertilizers in Idaho, Oregon and Washington in 2005 and in Utah in 2006; 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. Based on our experience, commercial sales can be generated approximately one to three years after introductory sales activities 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.

The expansion into the Northwest states of Idaho, Oregon, Washington, and Utah is being managed by one field agronomist. The cost of maintaining that position ranges from \$120,000 to \$150,000 per year. The expansion into the Northeast states is being managed by one part time person at an annual cost of approximately \$30,000. That person is also the lead person in seeking customers for our Photochemical Silver Concentrators. We may increase these spending levels in 2008, depending on sales support requirements.

In general, expansion to new regions of the country will require at least one field agronomist for each new region at a cost similar to that for the Northwest region. In addition, each state has varying registration requirements for product labels and costs of registration. Development of product labels is done internally using existing staff. Registration fees for each state vary widely, ranging from \$25 to \$600 per year, largely depending on how many products are registered in the particular state. For the near term, we anticipate utilizing present staff and management for corporate support of the sales efforts for both existing regions and for the new regions. For the longer term, as we expand we will need to add corporate support personnel. In 2006 we added a Ph.D. agronomist, to support GOLD n GRO sales efforts.

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 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 products, a calcium plus magnesium fertilizer named GOLD n GRO 11-0-0+5% Ca (Calcium) and a high magnesium content fertilizer named GOLD n GRO 8-0-0+3% Mg (Magnesium), both

targeting foliar and soil application. We have registered GOLD n GRO 11-0-0+5% Ca in Nevada and California. The registration of GOLD n GRO 8-0-0+3% Mg is planned for the second quarter of 2008 at which time sales development will be started.

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 deer repellent fertilizer is an example of this type of specialty fertilizer. The U.S. market for deer repellents is believed to exceed \$200 million in annual sales. Products currently in the market have limited effectiveness so we believe that 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.

We acquired ownership interest in the GOLD n GRO Guardian trademark, product rights, and the repelling product in 2005. We now own 100% of all rights related to GOLD n GRO Guardian. Results of the research of the GOLD n GRO Guardian deer repellent fertilizer has provided a basis for a bird (goose) repellent fertilizer that will be perfected for small plot field trials. Currently, this product line is strictly for non-food plant applications. We have engaged consultants experienced in the EPA registration process. We are presently working with them to plan the process and lab work needed to complete a series of registrations. One registration was issued in March 2008.

We believe the users of the GOLD n GRO deer repellent fertilizer will be upscale homeowners, commercial landscapers, and municipal facilities, and wholesale and retail nurseries. Initial sales development will be centered in Utah and seven northeastern states.

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.

We are developing applications of our technology to extract silver from photoliquids to the mining sector. This work is being expanded and a small pilot circuit is being 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 quantitative market studies can be completed.

7. Continue facilities expansion and technology development.

As fertilizer sales volume increases, we 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. The first phase, construction of a containment area, was substantially completed in late 2006. While we believe that we can handle expected growth in 2008 with the existing load-out module, we hope to complete construction on the new load out equipment during the second half of 2008, subject to the availability of financing.

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. Further acquisitions will depend on the potential benefits and suitable financing.

Competition

Our GOLD n GRO fertilizer products compete with well established fertilizer companies that have significantly more capital with which to market their products. Our competitors include large companies such as Scotts Miracle-GRO, Dow AgroSciences Company, Uniroyal Chemical Corporation, and smaller companies such as Pursell Technologies, Inc. We believe that our fertilizers compete primarily on the basis of product quality and performance.

Our photochemical recycling fees are generated primarily from processing used photochemicals from our customer s sites. We are now providing services to large national firms like Safety Kleen and Philips Environmental. We are also providing these services to smaller regional firms. Our primary competition is small regional firms.

We sell our silver bullion to a commercial refiner under standard industry terms. We are a very small producer of silver; consequently the refiner will purchase all the silver we can presently produce. For several years, there has been a global shortage in the supply side of the silver market. Our ability to sell our silver bullion could only be impacted if there were a dramatic contraction in the demand for silver, and only then if we grow to be a much larger silver producer than we are now.

- 
- 
- 

Markets

Fertilizer

The total fertilizer market consists of the "Agricultural Market" and the "Urban Market". The Urban Market accounts for at least \$9 billion in annual sales in the United States. The "Specialty Ag" segment of the Agricultural Market is a \$5 billion segment making the total a \$14 billion market. Substantially all of our present GOLD n GRO fertilizer sales are in the "Specialty Ag" segment.

More than 50 million tons of fertilizer products are sold annually in the United States. This includes almost 20 million tons of multi-nutrient fertilizers and almost 3.5 million tons of secondary nutrient and micro-nutrient products. About 38 percent of the total usage is as fluid fertilizers. Our 2007 sales represent less than 0.05 percent of the specialty ag segment of the fertilizer market.

Our GOLD'n GRO fertilizers are all liquid. There are major differences in manufacturing, distribution, and sale of liquid fertilizers as compared to dry fertilizers. Basic differences are described here so that the investor can better understand the technology, logistics, and application of liquid fertilizers and thereby gain a better understanding for the market niche that we operate in.

Liquid fertilizer technology is more complex than dry technology. Typically dry solids can be readily blended into dry mixtures that can then be bagged, or transported as dry bulk powders. In contrast, liquid fertilizers are reacted products and must be manufactured using precise recipes so that the final product will remain stable. Dry products can be stored for years without degradation, whereas liquid products typically have a limited storage life ranging from a few days for proprietary field blends, up to 4 years or longer for certain types. Liquid fertilizers can also freeze over a rather wide range of temperatures, a problem not encountered with dry fertilizers. Because of these technical factors, bringing a line of liquid fertilizers to market is much more complex than bringing a line of dry products to market.

Dry fertilizers are typically applied with dry spreaders. Liquids are sprayed on with tank sprayers or aircraft, injected into the soil using special applicators, or applied through irrigation systems using sprinklers, micro-sprinklers, or drip irrigation. Liquid fertilizers can also be applied with ditch irrigation by running the fertilizer into the water at controlled rates. The use of irrigation water to apply the liquid fertilizers is called fertigation.

Dry fertilizer packaging and transport is typically simpler and less costly than liquid fertilizer packaging and transport. Bulk liquids must be moved in tank trucks or tank rail cars and stored in large bulk tanks at distribution points. The distributors who sell the liquids to farmers must install and operate tank farms and maintain a fleet of specialized applicators. Distribution and application of liquid fertilizers typically requires specialized technical knowledge related to mixing and handling as compared to the use of dry fertilizers. Liquid fertilizers are typically easier and less costly to apply when irrigation is available, and availability of the fertilizer nutrients in the soil for uptake by crops is greater when liquid fertilizers are used. Use of fertigation to apply liquid fertilizers can reduce tractor trips through the fields, reducing cost and also reducing soil compaction. Because of less cost for application and improved availability of the liquid nutrients to the plants, liquid fertilizers in the United States are continuing to gain market share. Use of liquid starter mixes for dry land crops is also expanding, especially for planting field crops such as cotton, corn, soybeans, and wheat.

Only certain fertilizer distribution companies are specialized in marketing liquid fertilizers and have the facilities and equipment required to sell, deliver, and apply the liquid fertilizers. Our licensed distributor is one of those companies.

The GOLD'n GRO fertilizers are complex and represent a new category of liquid nutrition technology. The GOLD'n GRO fertilizers contain bulk chelating agents that conventional liquid fertilizers do not contain. The chelating agents, which are normally quite costly, are supplied as components of the starting photographic liquids. The chelating agents improve the availability of micronutrient metals such as zinc, iron, manganese, and the secondary nutrients calcium, and magnesium, and are an advanced nutrient delivery technology. The photoliquids also have a natural content of sulfur, the other important secondary nutrient. These chelate enriched multinutrient fertilizers distinguish the GOLD'n GRO liquids from other liquid fertilizers and are the main reason why the GOLD'n GRO liquid fertilizers represent a new type of nutrient delivery technology.

The deer repellent/fertilizer market is a new market for us. The users of this product will be upscale homeowners, commercial and municipal facilities, commercial nurseries, and landscape maintenance companies. The deer population is growing rapidly in the northeastern U.S. and so the center of gravity for this product is the northeastern seaboard states. The initial sales center will be in Rhode Island. The markets being served are the Commercial Landscape and wholesale and retail Nursery segments. The GOLD'n GRO Guardian line of products is strictly for non-food plant applications so the distribution channels are different from the channels being developed for GOLD'n GRO fertilizers.

The U.S. market for deer repellents is believed to be well in excess of \$200 million per year. Products currently in the market are believed to have limited effectiveness so we believe that an opportunity exists for a line of systemic products that are effective for several weeks after each application. The GOLD'n GRO Guardian is demonstrating effectiveness for periods of 8 to 12 weeks, and may be able to provide "year round" protection. We are pursuing development of this line of products as rapidly as possible.

### Photochemical Recycling

We estimate that there are more than 1,500 generators of photographic hazardous waste in the State of Nevada and more than 500,000 throughout the United States. This includes printed circuit board manufacturers, photo off-set printers, photographic developers, lithographers, photographers, micro-filming (banks, companies, etc.) and x-ray users (dentists, doctors, hospitals, podiatrists, orthopedic surgeons, veterinarians, radiologists and industrial x-ray users). We estimate the total annual market for recycling this category of waste to be in the range of \$200 to \$400 million.

We are aware of digital imaging and its impact on usage of conventional photography. The impact is different for each of the major segments; medical, color photography, and printing/microfiche. Digital imaging has made significant inroads into printing/microfiche processing with an almost 85% reduction in volume of photographic liquids over the past ten years. We are estimating that the volume of color photography waste liquids has been reduced by up to 50%. Digital photography is creating a new source of photowastes from Internet companies that combine digital imaging services with the ability to print high quality photographs for their customers. Digital methods are being adopted in the medical industry, and although the medical sector is relatively high growth with the aging U.S. population, digital imaging has had the effect of slowing the growth of waste photo liquids being generated and may lead to a decline in future years.

A larger impact on photo waste generation has been the pressure for companies to reduce the amount of waste generated at the operating sites. In photography, water was used in copious quantities for film rinsing and large quantities of low chemical content waste liquids were generated. With the tightening of regulation of discharge of contaminated waters the equipment manufacturers have focused on reducing water usage and the volume of photochemicals that are used. This attention to reduction of waste water has contributed to a reduction in the quantities of waste liquids being generated. It is expected that efficiency of use and associated waste reduction will continue, driven by increasing waste disposal costs. On-site photochemical recovery using a Photochemical Silver Concentrator and re-using the recovered water is expected to continue to become more and more attractive to large photochemical waste generators.

Environmental restrictions on disposal of chemicals are continuing to tighten throughout the United States with the result that now the rate of growth for our photochemical recycling business is dependent upon the rate and vigor of fertilizer sales growth.

The Company believes that the volume of photochemical liquids being generated in the United States continues to greatly exceed its needs for fertilizer manufacturing.

### Silver

Nationally, more than 40 million ounces of silver are consumed in photomaterials annually. Approximately 30% of this is lost through disposal. The Silver Institute indicates that silver usage in photography declined in 2006.

### Seasonality and Working Capital

In analyzing the market and industry competitors, it is apparent that two factors significantly impact our ability to penetrate these markets in a meaningful way. First, the seasonal aspect of fertilizer sales, which directly results in the second factor, the need for a much higher level of working capital when compared to other industries. Based on experience, we expect fertilizer sales to continue to have a strong seasonal component, with the primary sales season running from April through November each year, with an in-season low in July and August. In addition to the general seasonal nature of sales caused by normal weather patterns, unusual weather can further affect fertilizer sales, especially in winter and spring. For example, unusually cold or wet spring seasons may delay the growing cycle of various crops for which our fertilizers are utilized. To overcome weather related effects on fertilizer sales, we are

evaluating markets in the southern areas of the United States where growing seasons are longer and, in some cases, year round.

Due to the seasonal nature of GOLD'n GRO fertilizer sales, we must increase our net working capital to a level higher than that of non-seasonal industries. For example, some of our competitors have working capital equal to their annual sales. Consequently, ongoing debt and equity funding will be required for us to grow, even after a profitable level of operations is achieved.

#### Research, Development, and Technology

The majority of our research and technology is proprietary, which means it has not been patented, but is protected with strict confidentiality agreements and limited access to our research and production facilities. A U.S. patent on the silver separation process was issued in 1987 and is now expired. We made a corporate decision to not patent our research results as the cost of obtaining and defending patents is prohibitive.

We conduct field trials to gather agronomic data and to develop knowledge of how the GOLD'n GRO products work on different crops. This field testing will continue as it is the most effective method for developing the field data needed to support claims of product effectiveness for specific crops. On-going field trials of GOLD n GRO fertilizer products continue to show significant improvements in crop production and quality. The trials are providing agronomic data that is being used to develop GOLD n GRO nutrition programs for the crops being tested.

The field trials are demonstrating that the GOLD n GRO products provide both agronomic and economic benefits in the "specialty agricultural" markets. Specialty agriculture includes vegetables, cut flowers, herbs and spices, and fruits and nuts of all types. These crops are relatively high value compared to field grains such as corn, wheat, and soybeans. Field trials in 2002 on cotton and on silage corn produced positive results, opening two new large acreage crops for GOLD'n GRO application development. Alfalfa is typically considered as a "hay" or "forage" crop and is generally of low to intermediate value when compared to specialty agricultural crops, however, high nutrient content alfalfa for the dairy market often commands a significant price premium which puts it at the low end of specialty agricultural crop values.

A 3 year field trial on Valencia orange trees was carried out with oversight from a major university in southern California was completed in 2004. Three year cumulative results were analyzed and positive results were obtained. Fruit output per tree and fruit quality were both increased.

During 2003, we completed a key phase of the research project to produce formulated glass products. The research identified three product categories: (1) a glass ceramic mixture that can be used to produce tile and other shapes suitable for glazing and commercial use; (2) glass formulations that can be used as "lead free" low and intermediate temperature glazes for decorative tile and the craft pottery trade; and (3) specialty boro-silicate glass formulations. The next phase of the research will focus on production of small quantities of products for evaluation and market studies and is expected to be completed over the next two to three years.

We continue to be offered the opportunity to explore the feasibility of recycling other non-photographic materials into fertilizer. We have concluded that certain acid waste streams generated by aerospace and electronics manufacturers may be able to be converted to a form that will fit "Beneficial Use" recycling into fertilizer in association with the processed photochemical materials.

#### Environment and Regulation



All chemistry has a "cradle to grave" regulatory life span. This term means under Federal law, the prime generator has the ultimate liability for all generated waste as long as it exists. For example, conventional services, through storing and hauling, relocate the waste to a legal landfill or dispose it to sewer. Liability then remains for the cost of cleanup if the landfill has to be reclaimed or the contamination of groundwater develops.

However, once the spent chemistry reaches our facility and has been processed, the generator's hazardous waste liability is eliminated. Using our process, virtually all metals, including most of the iron, are removed. The end result leaves us with a non-hazardous "toxic-metal-free" liquid which is legal for use in high quality GOLD n GRO liquid fertilizers.

While in general our business has benefited substantially from increased governmental regulation of hazardous disposal by private industry, the waste management and recycling industry itself has become subject to extensive, costly and evolving regulation by federal, state and local authorities. We make a continuing effort to anticipate regulatory, political and legal developments that might affect our operations, but may not always be able to do so. We cannot predict the extent to which any legislation or regulation may affect future operations.

In particular, the regulatory process requires firms in our industry to obtain and retain numerous governmental permits to conduct various aspects of their operations, any of which permits may be subject to revocation, modification or denial. We are not in a position at the present time to assess the extent of the impact of such potential changes in governmental policies and attitudes on the permitting process.

For several years we have been studying the various regulatory requirements under RCRA and have been working with state and local environmental officials regarding the extent to which hazardous waste regulations apply to our operations. Through this process, we reached the conclusion that due to use of photochemicals as a beneficial ingredient in our fertilizer products, the photochemicals are not "hazardous waste" as defined in the regulations, and therefore, beneficial materials that are otherwise regulated as hazardous waste, are exempt from most of such regulations. In early 1996 we received concurrence from State of Nevada environmental officials that our photochemical fertilizer process meets the existing RCRA requirements for exemption from all environmental regulation with the exception that certain presently conducted lab analyses of the photochemicals will continue to be required. Certain of our large scale customers presently meet the exemption requirements. Present levels of fertilizer sales utilize all the photochemicals received.

Environmental regulation of photowaste generators has strengthened over the last several years, and that trend is expected to continue. In the past year, heavy metal contamination of fertilizers has become a significant issue in California and other parts of the country. Public concern over this issue is expected to intensify. We believe that the GOLD n GRO line of fertilizer products is uniquely suited to alleviating this environmental concern and that we are well positioned to meet future environmental needs.

#### Permits and Inspections

To the best of our knowledge, we have obtained permits from all governmental agencies having jurisdiction, such as the U.S. EPA, Nevada Department of Environmental Protection, Washoe County Health Department and the City of Reno, Nevada. We are not required to obtain federal permits, but are required to have, and have obtained, local permits for our photochemical recycling facility under the provisions of the U.S. EPA. Similar permits will be required of all facilities that we may construct. Our recycling facility is subject to frequent inspections and to regulations (including certain requirements pursuant to federal statutes) which may govern operating procedures for land, water and air pollution, among other matters. In particular, our operations are subject to the Safe Drinking Water Act, TSCA (Toxic Substances Control Act-pursuant to which the EPA has promulgated regulations concerning the disposal of PCBs), the Clean Water Act (which regulates the discharge of pollutants into surface waters and sewers by municipal, industrial and other sources) and the Clean Air Act (which regulates emissions into the air of certain potentially harmful substances). Employee safety and health standards under the Occupational Safety and Health Act

are also applicable to our employees.

## MINING TECHNICAL SERVICES

### Services offered

Our Mining Technical Services segment offers a wide range of technical services to the mining industry, including management support, mineral project development, ore reserve and material balance reviews, expert assistance in contract dispute or litigation, and mineral economics and cost studies

### Operations

The Mining Technical Services Division originally provided typical consulting services to the mining industry 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.

We launched the insidemetals.com website in 2005, targeting the companies and individuals interested in the mining and precious metals industry. The website is generating revenue by charging a subscription fee for monthly access to the site. Currently, the site contains an array of information about gold mining and gold mining stocks. We intend to add information on other mineral sectors gradually over time. A program to solicit advertising customers is being developed and is being offered to gold exploration companies. To assist with the sales development program of the website, we hired a manager of marketing and sales in October 2006. He was responsible for marketing efforts for both the insidemetals.com website and for technical consulting services to the mining industry. As no revenue was generated from this work, the position was eliminated in February 2008. We are presently evaluating the steps we need to take to improve the revenue growth from the website.

New technical consulting contracts are now being generated from this effort.

### Expansion Plans

In 1999 WWI initiated a long term R&D project to replace the use of cyanide in the extraction of metals from silver/gold and gold/copper ores. The new thiosulfate leaching technology being developed under this program utilizes the same technology as our proprietary photochemical recycling process. The project, called Itronics Thiomet, may seek to establish operating joint ventures at specific mine sites to apply the thiosulfate leaching technology. This project is on hold pending further commercial development of fertilizer sales.

In 2004 a project to establish a subscription based gold industry and gold company Internet publication was begun. The web publication, called "insidemetals.com", provides the customer with gold industry and producing gold company financial, production, and ore profiles. Initially, the companies to be profiled are in the Gold Company sector, which includes gold, silver, platinum, and palladium producers. The profiled companies are publicly traded on the New York and American Stock Exchanges and on NASDAQ. The publication was launched in August 2005 and the target market includes gold company employees, governmental agencies, both domestic and foreign, and individual investors interested in the gold markets. In addition to providing subscription revenue, it is anticipated that

the publication will enhance our opportunity to obtain new sources for technical consulting work. This subscription based Internet Information Portal provides an opportunity for relatively unrestricted growth by being available to a diverse global base of potential customers.

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. The site is now receiving visits from more than 170 countries world wide.

### Competition

Our consulting services are generally in the area of management support and mineral economics. Management support projects include advice on mineral development strategies, audits of ore reserves and appraisals on mineral properties primarily to mining companies. Our projects tend to be short term, generally less than one year, and are typically sole sourced to us based on the reputation of our president. Other companies that provide similar services include local and regional mineral consulting firms.

Our competition for the Internet Information Portal is other websites that provide gold and other precious metal information to the interested public.

## ITEM 2.

### DESCRIPTION OF PROPERTY.

#### I. FACILITIES.

Itronics leases approximately 3,000 square feet of office space at 6490 South McCarran Blvd., Building C-23, Reno, Nevada. IMI leases approximately 2,000 square feet of warehouse space in Reno, Nevada. This space is being used for supply storage and will be used for manufacturing GOLD n GRO Guardian.

IMI owns a 35,000 square foot manufacturing facility in Reno-Stead, Nevada. The building contains all the equipment used for treating the used photochemicals, preparing the recovered silver for sale, and manufacturing the GOLD n GRO fertilizer products.

#### II. EQUIPMENT.

The equipment being used in the recycling and fertilizer manufacturing process is proprietary information. However, the plant for recycling liquid photochemicals into fertilizer is a fairly typical chemical process facility consisting of appropriate arrangement of tanks and pumps. Solids produced by processing are recovered by filtration.

The refining operation consists of a material handling section, solids drying, and a melting section. The equipment arrangements are proprietary, but the main items are pumps, tanks, filtration equipment, drying ovens, and the melting furnaces.

-

ITEM 3.

LEGAL PROCEEDINGS.

As of December 31, 2007 we have accrued for liabilities, including interest, of \$544,965 which relate to various lawsuits and claims for the collection of the funds due. These include 8 leases totaling \$366,358 (reflected in Capital Lease Obligations) plus \$62,435 in additional interest (reflected in Accrued Interest) and one trade payable totaling \$85,801 (reflected in Accounts Payable) plus \$30,371 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 three cases that are seeking \$251,522, which we believe are probable. The creditors have received judgments in these cases, but have taken no further collection action. We will continue to accrue interest until these cases are settled or paid in full.

We have two cases, that originally sought \$171,853, that we deem to have a remote possibility of incurring an additional unrecorded loss. We have negotiated payment agreements on these cases and, as of December 31, 2007, the recorded liability was \$163,128. We are delinquent in our payments under the respective settlement agreements, but we are in contact with the lender's legal representative and no collection action has been taken.

In addition to the above leases that are subject to litigation, there are four leases, with a recorded liability of \$189,110, that are in default. 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.

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

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 above. Other than as described above, we are currently not aware of any litigation pending or threatened for any reason other than collection of funds due and already recorded nor are we 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.

ITEM 4.

SUBMISSION OF MATTERS TO A VOTE OF ITS SECURITY HOLDERS.

None.

PART II

ITEM 5.

MARKET FOR COMMON EQUITY AND RELATED STOCKHOLDER MATTERS AND SMALL BUSINESS ISSUER PURCHASES OF EQUITY

## Edgar Filing: ITRONICS INC - Form 10KSB

(a). Market Information. The Company's common shares are traded on the over-the-counter market under the symbol ITRO.OB, and quoted in the National Quotation Bureau, Inc.'s "pink sheets" and on the NASD Electronic Bulletin Board. In 2003 the Company's stock began trading on the Frankfurt, Germany Stock Exchange under the symbol ITG. In 2004 the Company's stock began trading on the Berlin Bremen Stock Exchange (Germany) under the symbol ITG.

The following table sets forth the high and low bid prices for the Company's common stock for each quarter for 2006, 2007, and through March 31, 2008.

|          | <u>High Bid</u> | <u>Low Bid</u> |
|----------|-----------------|----------------|
| 3/31/06  | \$0.08          | \$0.04         |
| 6/30/06  | \$0.05          | \$0.02         |
| 9/30/06  | \$0.04          | \$0.01         |
| 12/31/06 | \$0.02          | \$0.01         |
| 3/31/07  | \$0.03          | \$0.01         |
| 6/30/07  | \$0.03          | \$0.01         |
| 9/30/07  | \$0.02          | \$0.004        |
| 12/31/07 | \$0.005         | \$0.002        |
| 3/31/08  | \$0.02          | \$0.003        |

These quotations reflect inter-dealer prices without retail markup, markdown, or commissions, and may not represent actual transactions.

(b) On March 31, 2008 the number of record holders of the Common Shares was approximately 1,052.

### (c) Dividends.

The Company has paid no dividends.

### Recent Sales of Unregistered Securities

:

In October 2007 we issued an aggregate of 5,000,000 common shares John W. Whitney, our President, upon conversion of \$18,500 in short term loans.

In October 2007, we issued an aggregate of 214,286 shares of common stock valued at \$1,500 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 third quarter of 2007.

## Edgar Filing: ITRONICS INC - Form 10KSB

In October 2007, we issued an aggregate of 30,000 shares of common stock valued at \$210 to two employees as compensation for services performed on our behalf in their capacities as employees of our Company for the third quarter of 2007.

In November 2007 we issued an aggregate of 7,761,710 shares of common stock valued at \$15,523 to Wayne Baker as compensation for consulting services performed on our behalf in 2007.

In November 2007 we issued an aggregate of 1,600,000 shares of common stock valued at \$200,000 to one accredited investor upon the conversion of the principal portion of his Series 2000 Convertible Note.

During the fourth quarter of 2007 we issued an aggregate of 382,925,910

common shares to four accredited investors upon the conversion of \$387,545 in callable secured convertible notes.

On October 23, 2007, the Company entered into a Securities Purchase Agreement with three accredited investors (the "Investors") for an aggregate amount of (i) \$275,000 in secured convertible notes, and (ii) warrants to purchase 15,000,000 shares of the Company's common stock (the "Financing"). The Company anticipates that the proceeds of the Financing will be used to advance its eight part business plan which was summarized in its press release issued by the Company on June 3, 2005. The Financing will provide working capital to expand GOLD n GRO fertilizer sales, EPA registration of the GOLD n GRO Guardian deer repellent fertilizer, certain capital improvements to expand production capacity, and payment of existing debt obligations.

The Financing was completed in one closing. The closing consisted of gross proceeds of \$275,000, less financing costs of \$15,000, for net proceeds of \$260,000.

The Investors received three year convertible notes (the "Notes") bearing simple interest at 8% per annum. The Notes are convertible into the Company's common stock at a price equal to the lesser of (i) \$0.10 or (ii) 55% of the average of the lowest 3 trading prices during the 20 trading day period ending one trading day before the conversion date. In addition, we granted the Investors a further security interest in substantially all of our assets, including the assets of our wholly owned subsidiaries, and intellectual property.

The parties entered into a Registration Rights Agreement whereby we are required to file a registration statement with the Securities and Exchange Commission within 180 days of closing, registering the common stock underlying the secured convertible notes and the warrants. If the registration statement is not declared effective within 180 days from the date of closing, we are required to pay liquidated damages to the investors. In the event that we breach any representation or warranty in the Securities Purchase Agreement, we may be required to pay liquidated damages in shares or cash, at our election, equal to two percent of the outstanding principal amount of the secured convertible notes per month plus accrued and unpaid interest.

The Investors received seven year warrants to purchase a total of 15,000,000 common shares of the Company at a purchase price of \$0.004 per share.

Other than under these Agreements and under certain specified circumstances, should we issue shares of common stock below the market price, the exercise price of the warrants will be reduced accordingly.

The conversion price of the secured convertible notes and the exercise price of the warrants may be adjusted in certain circumstances such as if we pay a stock dividend, subdivide or combine outstanding shares of common stock into a greater or lesser number of shares, or take such other actions as would otherwise result in dilution of the selling stockholder's position.

The Investors have agreed to restrict their ability to convert their secured convertible notes or exercise their warrants and receive shares of our common stock such that the number of shares of common stock held by them in the aggregate and their affiliates after such conversion or exercise does not exceed 4.9% of the then issued and outstanding shares of common stock.

In addition to the above terms, the Company has agreed to restructure the current and all previous unpaid Callable Secured Convertible Notes ("the Notes") by increasing the discount on the conversion price from 50% to 60%, such that the conversion price is 40% of the average of the lowest 3 trading prices during the 20 trading day period ending one trading day before the conversion date, instead of the 55% as stated in the Notes and related Securities Purchase Agreements.

On December 27, 2007, the Company entered into a Securities Purchase Agreement with three accredited investors (the "Investors") for an aggregate amount of (i) \$200,000 in secured convertible notes, and (ii) warrants to purchase 15,000,000 shares of the Company's common stock (the "Financing"). The Company anticipates that the proceeds of the Financing will be used to advance its eight part business plan which was summarized in its press release issued by the Company on June 3, 2005. The Financing will provide working capital to expand GOLD n GRO fertilizer sales, EPA registration of the GOLD n GRO Guardian deer repellent fertilizer, certain capital improvements to expand production capacity, and payment of existing debt obligations.

The Financing was completed in one closing. The closing consisted of gross proceeds of \$200,000, less financing costs of \$15,000, for net proceeds of \$185,000.

The Investors received three year convertible notes (the "Notes") bearing simple interest at 8% per annum. The Notes are convertible into the Company's common stock at a price equal to the lesser of (i) \$0.10 or (ii) 35% of the average of the lowest 3 trading prices during the 20 trading day period ending one trading day before the conversion date. In addition, we granted the Investors a further security interest in substantially all of our assets, including the assets of our wholly owned subsidiaries, and intellectual property.

The parties entered into a Registration Rights Agreement whereby we are required to file a registration statement with the Securities and Exchange Commission within 180 days of closing, registering the common stock underlying the secured convertible notes and the warrants. If the registration statement is not declared effective within 180 days from the date of closing, we are required to pay liquidated damages to the investors. In the event that we breach any representation or warranty in the Securities Purchase Agreement, we may be required to pay liquidated damages in shares or cash, at our election, equal to two percent of the outstanding principal amount of the secured convertible notes per month plus accrued and unpaid interest.

The Investors received seven year warrants to purchase a total of 15,000,000 common shares of the Company at a purchase price of \$0.001 per share.

Other than under these Agreements and under certain specified circumstances, should we issue shares of common stock below the market price, the exercise price of the warrants will be reduced accordingly.

The conversion price of the secured convertible notes and the exercise price of the warrants may be adjusted in certain circumstances such as if we pay a stock dividend, subdivide or combine outstanding shares of common stock into a greater or lesser number of shares, or take such other actions as would otherwise result in dilution of the selling stockholder's position.

The Investors have agreed to restrict their ability to convert their secured convertible notes or exercise their warrants and receive shares of our common stock such that the number of shares of common stock held by them in the aggregate and their affiliates after such conversion or exercise does not exceed 4.9% of the then issued and outstanding shares of common stock.

In addition to the above terms, the Company has agreed to restructure all previous unpaid Callable Secured Convertible Notes ("the Notes") by increasing the discount on the conversion price from 60% to 65%, such that the conversion price is 35% of the average of the lowest 3 trading prices during the 20 trading day period ending one trading day before the conversion date, instead of the 55% as stated in the Notes and related Securities Purchase Agreements.

We issued options to purchase an aggregate of 9,000 shares of common stock to Michael C. Horsley, our Controller, on November 1, 2007. The options are exercisable at \$0.15 per share and expire three years after grant.

We issued options to purchase an aggregate of 62,000 shares of common stock to four of our employees in October and November 2007. The options are exercisable at \$0.15 to \$0.16 per share per share and expire in three years to ten years from grant.

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.

## ITEM 6.

### MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

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.

#### General Overview

We are the inventor and developer of the "Beneficial Use Photochemical, Silver, and Water Recycling" technology that produces environmentally beneficial GOLD'n GRO fertilizers and silver bullion.



We are a process technology company that has developed what we believe is a unique technology for photochemical recycling. We, through our subsidiary, Itronics Metallurgical, Inc., extract more than 99% of the silver and virtually all of the other toxic heavy metals from used photoliquids and use this "Beneficial Use Photochemical, Silver and Water Recycling" technology to produce environmentally beneficial chelated multinutrient liquid fertilizer products sold under the trademark GOLD n GRO, deer repellent/fertilizer products to be sold under the trademark GOLD n GRO Guardian, and silver bullion. We also provide process planning and technical services to the mining industry and are operating and continuing to develop an internet website to provide gold mining company profiles to parties interested in the gold mining and precious metals industry.

Our fertilizer is sold primarily through Western Farm Service, Inc. (WFS), a wholly owned subsidiary of Agrium, Inc. (a NYSE company). Our distribution agreement with WFS gives them exclusive rights to sell our fertilizer products in Arizona, California, Hawaii, Idaho, Oregon, and Washington, which represented 99% of our fertilizer sales in 2007 and 95% of such sales in 2006. This agreement is discussed in more detail in the Business section. Our plans to increase GOLD n GRO fertilizer sales, including plans to expand the product line, expand to more geographical regions in the U.S., enter new market segments, and add new distributors, are also discussed in more detail in the Business section.

We obtain a significant portion of our raw materials to manufacture fertilizer from used photoliquids. A byproduct of our fertilizer manufacturing process is silver. We sell three types of silver: silver bullion, 5 troy ounce 99.9% pure Silver Nevada Miner numismatic bars, and recycled film containing silver. Our processed silver bullion is sold to a commercial refiner under standard industry terms, which include pricing the silver based on published market quotes and applicable service fees. The Silver Nevada Miner bars sell to the consumer collectibles market. Recycled film is primarily X-ray film from hospitals that we sort and sell to a commercial film recycler; we are paid based on the value of contained silver, 30 to 45 days after shipment.

Our fertilizer manufacturing process uses several commodities. We separate silver from photochemicals, then we add zinc and other raw materials to the demetallized liquid to make our fertilizer formulations. Prices for fertilizer raw materials are generally increasing over time. We maintain limited quantities of these commodities and purchase them on a just in time basis. When prices of these commodities rise, we pass this cost on to our customers, so commodity price fluctuations have not had a significant impact on our results of operations.

The majority of our raw material inventory is comprised of silver in photochemical solutions. The table below indicates that silver prices were relatively stable in 2001 to 2003, then rose dramatically in 2004 through 2007. We regularly compare our weighted average cost of silver per ounce to current market prices; historically we have not had impairment losses. The average London spot price of silver per ounce is shown as follows:

| <u>Year</u> |             |             |             |             |             |             |             |
|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| Year        | <u>2001</u> | <u>2002</u> | <u>2003</u> | <u>2004</u> | <u>2005</u> | <u>2006</u> | <u>2007</u> |
| Silver      | \$4.36      | \$4.60      | \$4.88      | \$6.67      | \$7.32      | \$11.55     | \$13.38     |

We also provide consulting services to the mining industry. To supplement this business line, we launched an internet website. Our plans with regard to the website are discussed more fully in the Growth Plan and Implementation section below.

Critical Accounting Policies and Estimates.

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires that management make a number of assumptions and estimates that affect the reported amounts of assets, liabilities, revenues and expenses in our consolidated financial statements and accompanying notes. Management bases its estimates on historical information and assumptions believed to be reasonable. Although these estimates are based on management's best knowledge of current events and circumstances that may impact the Company in the future, actual results may differ from these estimates.

Our critical accounting policies are those that affect our financial statements materially and involve a significant level of judgment by management.

#### Revenue Recognition.

We operate two divisions: Photochemical Fertilizer and Technical Services. Within the fertilizer division, revenue is derived from three sources (1) sales of fertilizer, (2) photochemical recycling including pick up and transportation of photochemical waste and sales of Photochemical Silver Concentrators, and (3) sales of silver. Fertilizer and retail silver sales are recognized when goods are shipped to our customers. We pay 1% of invoice amount to our primary fertilizer distributor in order to receive accelerated payment terms. The fee is netted against fertilizer sales. Sales of silver bullion and silver in film are recorded when the silver content and the sales price are determined, which is approximately two weeks after shipment for silver bullion and 30 to 45 days after shipment for film. Returns since inception have been nominal; therefore, the Company has not established a returns allowance. Photochemical recycling fees are recognized in income after the used photochemical solution is removed from our customer sites and transported to our manufacturing facility.

Within the technical services division, revenue is derived from consulting services. Revenue is recognized in income as services are rendered. When the Company is responsible for subcontractor services and related expenses, such pass-through costs are included in both revenue and cost of revenues. Markups, if any, are included in revenues.

#### Inventory.

Inventory is carried on the balance sheet at the lower of cost or market value using the average cost valuation method. Because a large part of our inventory is silver contained in used photochemical materials and the market value of silver changes daily on the commodities market, we regularly monitor the carrying value of our silver inventory to ensure it is carried at the lower of cost or its current market value. If silver on the open market were less than our carrying value, we would write down the carrying value of our inventory by reducing recorded inventory and increasing cost of sales. If the amount of the write down were material, we would separately include the item in our statement of operations.

#### Convertible Debt Derivative

The fair value of the conversion feature and the prepayment penalty are estimated using the Black-Scholes option pricing model and taking a weighted average value based on various probabilities that the debt would be paid off prior to maturity at specified dates and therefore incurring the prepayment penalty. This model requires management to use significant assumptions in applying the model to estimate the fair value. As the Company's stock price is highly volatile, and the underlying debt amounts are relatively large, the valuation of the derivatives is subject to material gains and losses from period to period.

## Recent Accounting Pronouncements

In December 2006 the FASB staff issued *FSP EITF 00-19-2 "Accounting for Registration Payment Arrangements"* to specify the accounting treatment of contingent obligations to make future payments or otherwise transfer consideration under a registration payment arrangement. Our callable secured convertible debt includes an obligation for us to file registration statements with the Securities and Exchange Commission (SEC) to register sufficient common shares for the note holders to convert the debt into common stock frames and also obligates us to have the registration statements declared effective by the SEC. This new standard requires us to evaluate the contingent future payments under the criteria of a probable loss under FAS 5. The Company adopted this new standard effective for the first fiscal quarter of 2007. The new standard has not had a significant impact on the Company's financial position or results of operations.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157 ("*SFAS 157*"), "*Fair Value Measurements*," which defines fair value, establishes guidelines for measuring fair value and expands disclosures regarding fair value measurements. SFAS 157 does not require any new fair value measurements but rather eliminates inconsistencies in guidance found in various prior accounting pronouncements. SFAS 157 is effective for fiscal years beginning after November 15, 2007 with earlier adoption permitted. The Company is currently evaluating the impact of SFAS 157, but does not expect the adoption of SFAS 157 to have a material impact on our consolidated financial position, results of operations or cash flows.

In February 2006, the FASB issued Statement of Financial Accounting Standards No. 155 ("*SFAS 155*"), "*Accounting for Certain Hybrid Financial Instruments*". SFAS 155 simplifies the accounting for certain derivatives embedded in other financial instruments by allowing them to be accounted for as a whole if the holder elects to account for the whole instrument on a fair value basis. SFAS 155 is effective for all financial instruments acquired, issued or subject to a re-measurement event occurring in fiscal years beginning after September 15, 2006. Earlier adoption is permitted, provided the Company has not yet issued financial statements, including for interim periods, for that fiscal year. The Company adopted SFAS 155 in the first quarter of 2007 and it has not had a material impact on our consolidated financial position, results of operations or cash flows.

## Results of Operations

The primary factors affecting our revenue fluctuation between periods in fertilizer sales are seasonality and weather conditions. Sales are greater during the growing season, and are negatively affected by cold winter weather and rainy weather. In most of our markets there are two primary fertilization seasons, spring and fall, with spring being the stronger of the two. The spring season generally starts in March and goes through June and the fall season generally starts in September and runs into December. Adverse weather conditions delay the start of, or can significantly shorten, a growing season. Farmers do not fertilize their crops in rainy or cold weather; therefore they do not buy fertilizer; consequently, our distributor does not buy fertilizer from us. Additionally, we have experienced varying lengths of time for acceptance in the market of our new fertilizer products; farmers are inherently very slow to accept new products so market penetration time can be lengthy. Our short history in the fertilizer market demonstrates that new products, if successful, obtain meaningful sales typically between two and four years after product launch.

The primary factors affecting the revenue fluctuation between periods in photochemical recycling revenue are our need to acquire this material for use in fertilizer production and our ability to store this material until it is needed. We have an unusual business model in that we need to sell our photowaste management services in order to acquire a raw material necessary for the production of our fertilizer products, as opposed to purchasing it from suppliers as most businesses do. Our management goal is to combine the incoming volume of photowastes with existing stored

photowastes to meet the peaks in demand for fertilizer products. In the liquid fertilizer industry, the practice of both our distributor and the ultimate consumer, the farmer, is to purchase fertilizer on a just in time basis, to minimize their storage requirements and related costs. For this same reason, we process our photowastes as needed for fertilizer production. Because of this, the need to seek new customers to expand the service side of our business is driven by fertilizer sales. There is also a seasonal factor in the consumer photography portion of our photowaste management services business, with the Christmas holiday season being the busiest, followed by the early summer, school graduation period. At present volumes of photowaste, this is not a significant factor, but it could become one as we grow.

The primary factor affecting the revenue fluctuation between periods in sales of silver bullion is our dependence on the timing of processing used photochemical wastes, which is primarily dependent on fertilizer manufacturing and related sales. Our silver in solution is separated from the photowaste materials during processing of the photowastes for use in fertilizer manufacturing. As described above, the timing of processing of photowastes is dependent on fertilizer sales, therefore sales of silver bullion is also dependent on the level of fertilizer sales. Market price changes will also contribute to silver revenue fluctuations by increasing or decreasing revenues depending on whether the silver price increases or decreases.

Comparison of the Year Ended December 31, 2007 with the Year Ended December 31, 2006

We reported consolidated revenues of \$2,342,296 for the year ended December 31, 2007, compared to \$1,871,918 for the prior year, an increase of 25%. Revenues for the GOLD n GRO Fertilizer segment increased by \$471,600, or 26%. Revenues from the Mining Technical Services segment declined \$1,200, or 4%. We reported a gross profit of \$124,200 for the year ended December 31, 2007 compared to a gross profit of \$75,200 for the year ended December 31, 2006, an improvement of \$49,000, or 65%. The consolidated net loss for 2007 was \$10,482,500 or \$0.021 per share compared to a 2006 consolidated net loss of \$3,809,900 or \$0.016 per share, an increased loss of \$6,672,600, or 175%.

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

PHOTOCHEMICAL FERTILIZER

|                         | <u>Year Ended December 31,</u> |              |
|-------------------------|--------------------------------|--------------|
|                         | <u>2007</u>                    | <u>2006</u>  |
| Revenue                 |                                |              |
| Fertilizer              | \$ 1,663,361                   | \$ 1,297,282 |
| Photochemical recycling | \$ 334,965                     | \$ 128,033   |

Edgar Filing: ITRONICS INC - Form 10KSB

|                                |               |               |
|--------------------------------|---------------|---------------|
| Silver                         | \$ 316,815    | \$ 418,265    |
| Total Segment Revenue          | \$ 2,315,141  | \$ 1,843,580  |
| Gross profit (loss)            | \$ 130,998    | \$ 83,462     |
| Operating income (loss)        | \$(2,199,386) | \$(1,682,464) |
| Net income (loss) before taxes | \$(9,881,206) | \$(3,370,803) |

Revenues for the Photochemical Fertilizer segment totaled \$2,315,100 in 2007, compared to \$1,843,600 in 2006, an increase of \$471,600, or 26%.

Fertilizer sales were \$1,663,400 (1,958 tons) and \$1,297,300 (1,746 tons) for 2007 and 2006, respectively. This represents an increase of 28% in dollars and an increase in tonnage of 12%. Our fertilizer product sales are presently grouped into three primary categories, Chelated Liquid Micro-nutrients, Chelated Liquid Multi-nutrients, and Chelated Secondary Nutrients. The Micro-nutrient category includes five products, which includes the two zinc products, GOLD n GRO 9-0-1+7% Zn and GOLD n GRO 9-0-2+3% Zn. These zinc products were introduced in 2001 and 2004, respectively. The Multi-nutrient category has a total of six products, which includes the GOLD n GRO 4-0-9+6.6% S Base Liquid, which was introduced in 2003. The Secondary Nutrient category includes GOLD n GRO 11-0-0+5% Ca which was introduced in 2006 and GOLD n GRO 8-0-0+3% Mg which was registered in 2007. Sales of bulk Micro-nutrients were \$1,362,500 (1,438 tons) and \$1,080,000 (1,259 tons) for 2007 and 2006, respectively, an increase of 26% in dollars and 14% in tonnage. Sales of bulk Multi-nutrients were \$201,700 (483 tons) and \$172,200 (479 tons) for 2007 and 2006, respectively, an increase of 17% in dollars and an increase of 1% in tonnage. Sales of bulk Secondary Nutrients were \$49,300 (37 tons) and \$10,800 (9 tons) for 2007 and 2006, respectively. The increase in total sales dollars, was achieved by both volume and sales price increases during 2007.

Photochemical recycling revenue was \$335,000 and \$128,000 in 2007 and 2006, respectively, an increase of 162%. Excluding the current year sale of a Photochemical Silver Concentrator for \$163,500, photochemical recycling revenue increased 34% on increased volume of 186%. In October and November 2006 we obtained two new large scale wholesale customers and in April 2007 we added a third wholesale customer. The addition of these customers is expected to increase photochemical raw material (on an unconcentrated basis) to a level about 50% greater than the volume at the end of 2004 when our contract with Shutterfly was ended (Shutterfly supplied 65% of our 2004 photochemical raw materials).

We previously developed statistical information that more than 50 million gallons of used liquid silver-bearing photochemicals are generated in the United States annually. Using conversion ratios developed for the GOLD'n GRO fertilizers, this is enough volume to support manufacture and sale of more than 100 million gallons of liquid fertilizer products, or about 500,000 tons, so we believe the raw material is available in the market to meet future manufacturing needs. Based on 2007 production usage, we estimate that current supplies of photochemical raw material in storage at our manufacturing plant, combined with ongoing receipts of material from other existing customers, is sufficient to meet fertilizer production needs through 2008, depending on fertilizer sales volumes. We anticipate that with continuing sales growth, we will need to obtain new large scale photochemical recycling customers to meet the demand.

We are in contact with both small and large photochemical generators, and are actively marketing Photochemical Silver Concentrators. The concentrators allow us to receive the raw materials needed to manufacture our fertilizer in much smaller volume, resulting in a higher content of chemicals desirable for fertilizer manufacturing, reducing the storage problems we were facing. The Photochemical Silver Concentrators are manufactured under contract by a third party to meet the specifications of each customer. Concentrators typically sell for \$20,000 to \$200,000. By using a third party manufacturer to produce the Concentrators, we are outsourcing the fixed and variable costs that are associated with assembling them. Primarily, these are the facilities space needed to assemble the various parts and the specialized equipment and labor required for the assembly. Generally, we have self financed the production of Concentrators sold in the past. In the future, we anticipate that non-governmental customers will advance the funds

necessary to acquire the parts and labor needed to produce the Concentrators. For our most recent governmental customer, we borrowed the funds needed to fulfill the contract from an unrelated individual. We anticipate using similar arrangements for future Concentrators sold to governmental customers.

Silver revenue was \$316,800 and \$418,300 for 2007 and 2006, respectively, a decrease of \$101,500, or 24%. Sales of all silver or silver bearing products were \$293,900 (21,818 ounces) for 2007, compared to \$399,200 (33,690 ounces) for 2006. This is a decrease of 26% in dollars and 35% in ounces. The decrease is primarily from decreased sales of processed silver bullion due to a combination of closing the refinery during the first quarter for installation of a scrubber for air quality purposes and to problems with our power supply in to the refinery. The power supply issue has been reduced in recent months, but not eliminated. We are continuing to work with the local power company to solve the problem.

Combined cost of sales and operating expenses for the segment amounted to \$4,514,500 in 2007, compared to \$3,526,000 in 2006, an increase of 28%. Cost of sales increased approximately \$424,000, primarily due to an increase of raw material costs of \$267,000 from increased sales, \$70,000 in increased payroll and related costs, and \$27,700 in transportation costs related to increased travel for the new wholesale photowaste customers. The changes in revenues and cost of sales resulted in a 2007 gross profit of \$131,000 compared to a gross profit of \$83,500 in 2006, an improvement of \$47,500, or 57%. Operating costs increased \$564,500 due primarily to increases of \$379,900 in sales and marketing, \$59,800 in research and development, and \$119,300 in general and administrative costs. Sales and marketing expenses increased primarily due to increased corporate marketing. The increase in research and development costs is related primarily to the EPA registration of the GOLD n GRO Guardian deer repellent. General and administrative expenses increased primarily due to \$161,700 in consulting services for seeking operational funding, which was partially offset by a reduction in payroll and related costs of \$54,200.

A significant portion of our silver inventory is contained in byproducts from our refining process. We have developed new procedures to more cost effectively obtain this silver and initial plans were to install the necessary equipment in 2006 and recover the majority of it during 2006. The project was delayed by the necessity of installing air purification equipment in the refinery. The air purification system was substantially completed in March 2007. Plans were developed to determine the specifications of the equipment needed to process the byproducts and obtain the silver. We estimate there will be a two stage process of equipment installation. The equipment for the first stage was received in early 2008 and a temporary installation has been completed. Silver recovery is expected to begin during the second quarter of 2008. Planning is underway for the second stage, and, subject to funding, is expected to be completed in the third quarter of 2008. In order to determine the amount of the silver contained in these materials, we developed an estimate of recoverable silver ounces. Accordingly, we recorded a recoverability reserve of \$70,200 based on our estimate of recoverable silver at December 31, 2006. The portion of silver that we estimate will be recovered in 2008 was deemed to be slow moving inventory, and accordingly, we recorded a reserve of \$34,000. Our review of these reserves determined that the reserves were adequate as of December 31, 2007.

These changes in revenues and operating expenses resulted in a segment operating loss of \$2,199,400 in 2007, compared to \$1,682,500 in 2006, an increased loss of \$516,900 or 31%.

Other income (expense) increased to a net expense of \$7,681,800 for 2007, compared to a net expense of \$1,688,300 in 2006, an increased net expense of \$5,993,500. The primary reason for the increased expense is an increase of the loss on derivatives of \$6,256,700, which is related to the callable secured convertible debt financing obtained in July 2005 and subsequent dates. This increase was partially offset by a decrease in interest expense of \$87,100 related to the convertible debt financing and other income of \$205,900 from the sale of a membership interest in our worker s compensation mutual insurance company.

The changes in operating loss and other expenses resulted in a segment net loss before taxes of \$9,881,200 for 2007 compared to \$3,370,800 for 2006, an increased loss of \$6,510,400 or 193%.

MINING TECHNICAL SERVICES

|                                | <u>Year Ended December 31,</u> |             |
|--------------------------------|--------------------------------|-------------|
|                                | <u>2007</u>                    | <u>2006</u> |
| Revenue                        | \$27,155                       | \$ 28,338   |
| Gross profit (loss)            | \$(6,838)                      | \$ (8,269)  |
| Operating income (Loss)        | \$(744,042)                    | \$(542,042) |
| Net income (loss) before taxes | \$(601,318)                    | \$(439,082) |

Mining technical services revenue totaled \$27,200 for 2007 compared to \$28,300 for 2006, a decrease of 4%. Included in these revenue figures are pass-through expenses of \$1,500 and \$2,500 for 2007 and 2006, respectively. Excluding these amounts, revenues amounted to \$25,600 and \$25,800 for 2007 and 2006, respectively, a nominal decrease. The number of clients we serve and the amount of work needed by those clients varies from period to period.

Combined cost of sales and operating expenses totaled \$771,200 for 2007 compared to \$570,400 for 2006, an increase of 35%. Research and development expense increased \$41,700. Research and development expense is related to the development of the insidemetals.com website. The majority of this expense is an allocation of personnel costs. Sales and marketing increased \$152,500 due to the addition of a marketing position in October 2006 and to increased advertising related to the insidemetals.com website.

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 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 years ended December 31, 2006 and 2005 we allocated costs of approximately \$248,500 and \$206,900, respectively, to the development of the web site. The site was launched in mid-August 2005 and we are now fine-tuning the general presentation and functionality of the site, as well as improving the profiled mining company information. We expect this level of spending to decline beginning in the first quarter of 2008. As improvements to the site are completed and information maintenance becomes routine, we will adjust or redirect staff resources as needed. A program to solicit advertising customers was developed and is being offered to gold exploration companies beginning in the first quarter of 2007. We hired a manager of marketing and sales in October 2006. He was responsible for marketing efforts for both the insidemetals.com website and for technical consulting services to the mining industry.

As no revenue was generated from this work, the position was eliminated in February 2008. We are presently evaluating the steps we need to take to improve the revenue growth from the website.

The above changes in revenues and operating expenses resulted in a segment operating loss of \$744,000 for 2007, compared to \$542,000 for 2006, an increased operating loss of \$202,000 or 37%.

Other income (expense) is a net gain of \$142,700 for 2007, compared to a net gain of \$103,000 in 2006, an improvement of \$39,800. The improvement is due to the sale of a membership interest in our worker's compensation mutual insurance company.

The changes in operating loss and other income resulted in a segment net loss before taxes of \$601,300 for 2007, compared to \$439,100 for 2006, an increased loss of \$162,200, or 37%.

#### Changes in Financial Condition; Capitalization

We had a cash balance of \$93,000 as of December 31, 2007 compared to a cash overdraft of \$13,800 as of December 31, 2006. Net cash used by operations was \$1,890,900 in 2007 compared to \$1,698,200 in 2006. Operating resources utilized to finance the 2007 operations include approximately \$859,400 in expenses paid with our common stock, \$151,000 in increased accounts payable, and \$225,900 in deferred management salaries. Cash amounting to approximately \$61,400 was invested in property and equipment in 2007, primarily for equipment in the manufacturing plant. Sale of our interests in our workers' compensation mutual insurance company provided \$348,000 in cash from investing activities. The primary financing source of cash in 2007 was \$1,960,000 in proceeds from callable secured convertible debt, less \$140,100 in debt issuance costs.

Total assets increased from \$4,265,500 at December 31, 2006 to \$4,355,900 at December 31, 2007. Current assets increased \$193,700. The primary changes in current assets were increases in cash of \$93,000 and \$341,600 in inventory, which were partially offset by decreases in accounts receivable of \$18,900 and \$221,900 in prepaid expenses. The increase in inventory is primarily from silver in our photowaste products due to the refinery issues discussed above. The reduction in prepaid expenses was primarily due to a \$250,000 2007 corporate marketing program paid in common stock at the end of 2006 that was not renewed for 2008.

Property and equipment decreased by \$91,200 due to investment in equipment totaling \$118,200, which was offset by an increase in accumulated depreciation and amortization of \$209,500. Other assets decreased \$12,200 due to the amortization of deferred loan fees related to the callable secured convertible debt financing.

Total liabilities increased from \$11,695,000 at December 31, 2006 to \$20,019,800 at December 31, 2007, an increase of \$8,324,800. Of this amount, current liabilities increased \$8,896,300 and long term liabilities decreased \$571,500. The primary increase in liabilities was due to the change in estimated fair value of our callable secured convertible Notes. The Notes must be accounted for as derivative liabilities and recorded at estimated fair value at each reporting date, which was \$13,003,800 at December 31, 2007 and \$4,876,200 at December 31, 2006. The increase in the estimated fair value of convertible debt derivatives of \$8,127,600 in 2007 was primarily due to the addition of \$2.06 million in Notes, offset by the conversion of \$1.021 million in Notes, a reduction in our stock market price as of December 31, 2007 compared to previous periods, and an increase of the discount to market upon conversion of Notes from 45% at December 31, 2006 to 65% at December 31, 2007. In addition, all outstanding warrants and options are required to be recorded as derivative liabilities at estimated fair value, which was \$231,200 at December 31, 2007 and \$380,100 at December 31, 2006. The value of the warrants and options decreased primarily due to the decrease in our stock market price compared to previous periods. A more detailed discussion of the factors affecting the estimated fair value of our derivatives follows:

In estimating the fair value of warrants and options and determining the gain or loss on the derivative for each period, the most significant factor is the stock price at the end of each period. As the stock price goes up, the value of warrants and options goes up, and consequently there is a greater loss on derivatives. As the stock price goes down, the value of the warrants and options goes down and consequently there is a greater gain on derivatives. As of December 31, 2007, the stock price was \$0.0026 and at December 31, 2006 it was \$0.013. This decrease in stock price resulted in a reduction in the value of the warrants and options and consequently, there was a \$156,200 gain on warrant and option derivatives for the year ended December 31, 2007.



The factors affecting the valuation of the convertible debt derivatives are more complex. As the stock price goes up, that would tend to increase the value of the derivative and therefore increase the loss. However, an increased stock price also results in fewer shares needed to convert the debt, which tends to lower the value and reduce the loss. The reverse is true as the stock price goes down. Another factor that affects the valuation model is the length of time it takes to convert the debt. We estimate that length by first determining the number of shares it takes to convert the debt based on the stock price on the balance sheet date. We then estimate how many shares will be issued to convert debt on a monthly basis based on recent conversion history from our investors. In general, the investors have increased the frequency of conversions and the number of shares converted as the stock price has gone down. Also affecting the conversion practice of the investors is recent changes in interpretation of the securities laws by the SEC as to the frequency of filing registration statements. It was originally contemplated under the general concept of this type of financing that registration statements could be filed as frequently as needed and with as many shares being registered as needed to meet the terms of the agreements. In recent months, the SEC has determined to restrict registration filings for the same investor group to once every six months and to restrict the number of shares being registered to approximately one third of the outstanding shares held by non-affiliates. This factor has tended to lengthen the estimated time it will take to convert the debt which increases the value of the debt derivatives, and therefore increases the loss on derivatives. However, beginning in the third quarter of 2007, some of our Notes have been outstanding over two years. At that point the investors can convert the debt into stock under Rule 144 without limitation, except for the 4.99% of outstanding shares under the terms of the agreements. Consequently, there has been a substantial increase in the frequency of conversions and in the number of shares being issued for each conversion. This would tend to shorten the time period necessary to convert the Notes into common stock. In the Black-Scholes option pricing model, this decreases the value of the derivatives, and therefore, increases the gain on derivatives. Conversely, at December 31, 2007 the lowered market price, combined with the increase in the market price discount from 45% to 65%, the number of shares needed to convert the debt is over 6 billion shares, which has substantially increased the length of time needed to convert all of the debt. At December 31, 2006 we had estimated a period of 16 months to convert the debt, while at December 31, 2007 the estimated period was 35 months. These factors resulted in a loss on convertible debt derivatives of \$6,954,400 for the year ended December 31, 2007.

Current liabilities increased primarily due to the increase in convertible debt derivatives of \$8,127,600 discussed above. Current liabilities also increased due to increases in accounts payable of \$151,000, interest payable to management of \$70,000, current maturities of convertible notes and accrued interest of \$193,800, current maturities of long term debt of \$391,500, and current maturities of capital lease obligations of \$75,000. The current portion of long term debt and capital lease obligations increased due to the respective obligations being in default at December 31, 2007, requiring the classification of all the debt as current liabilities.

In connection with the callable secured convertible debt discussed above, we registered 50 million shares in February 2006 and increased the authorized shares in March 2006 to 1 billion shares. We also completed registrations of 75 million shares each in October 2006 and June 2007.

#### Working Capital/Liquidity

During the year ended December 31, 2007, the working capital deficit was increased by \$8,702,500 to a deficit balance of \$18,842,100. The primary changes in working capital are the increase in callable secured convertible debt financing as discussed above. The Company has had limited cash liquidity since the third quarter of 2000. The Company has sought and obtained the funding described above, which has not been sufficient to maintain all obligations on a current basis. The cash shortage is primarily because fertilizer sales in 2007 and prior years did not expand to the extent anticipated, so operating losses were not reduced as expected. Second, the \$15 million equity line of credit agreement with Swartz Private Equities, LLC (Swartz) was not able to function to meet the Company's ongoing working capital needs and was allowed to expire on February 27, 2004. As a result, various private placements of stock with attached three year warrants were undertaken beginning in the fourth quarter of 2002 into 2005. In addition, the Company sold GPXM and other shares for net proceeds of \$229,400 during the year ended December 31, 2006. We obtained callable secured convertible debt financing beginning in 2005 and received proceeds

of \$1,960,000, less debt issuance costs of \$140,100 in 2007 and proceeds of \$1,941,200, less debt issuance costs of \$247,600 in 2006. Subsequent to December 31, 2007, we received net proceeds of \$300,000 in additional callable secured convertible debt financing. We anticipate these proceeds will provide for the Company's working capital needs to April 2008.

We are actively working to establish longer term financing that will provide capital sources for the Company's financing needs over a three to five year period. Once this plan is established, needs for financing will be adjusted and the plan will be extended annually.

ITEM 7.

FINANCIAL STATEMENTS

The response to this Item is submitted under Item 13.

-

-

ITEM 8.

CHANGE IN AND DISAGREEMENTS WITH ACCOUNTANTS ON

ACCOUNTING AND FINANCIAL DISCLOSURE

To our knowledge, there is no accounting or financial disclosure dispute involving any present or former accountant.

ITEM 8A CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

As required by Rule 13a-15 under the Exchange Act, our management, including our Chief Executive Officer and our Chief Financial Officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of December 31, 2007.

Disclosure controls and procedures refer to controls and other procedures designed to ensure that information required to be disclosed in the reports we file or submit under the Securities Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating and implementing possible controls and procedures.

Management conducted its evaluation of disclosure controls and procedures under the supervision of our Principal Executive and Financial Officer and our Principal Accounting Officer. Based on that evaluation, our Principal Executive and Financial Officer and Principal Accounting Officer concluded that because of the material weakness in internal control over financial reporting described below, our disclosure controls and procedures were not effective as of December 31, 2007.

#### Management's Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act. Our management is also required to assess and report on the effectiveness of our internal control over financial reporting in accordance with Section 404 of the Sarbanes-Oxley Act of 2002 ("Section 404"). Management assessed the effectiveness of our internal control over financial reporting as of December 31, 2007. In making this assessment, we used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control - Integrated Framework. During our assessment of the effectiveness of internal control over financial reporting as of December 31, 2007, management identified material weaknesses related to the following:

##### Accounting and Reporting Oversight

Because of our size, we have ineffective segregation of duties relative to key financial reporting functions. However, one person in our company, our Principle Accounting Officer/Controller has extensive US GAAP accounting and SEC reporting experience. However, we do not have anyone else on staff with sufficient knowledge to review his work for completeness and accuracy. We do not have anyone with financial expertise on our Board so we have been unable to form an audit committee to perform oversight of this function.

In order to correct the foregoing weaknesses, we have taken the following remediation measures:

We continue to search for independent directors; however, given our current financial condition, we expect we will not be successful until we can become profitable and/or adequately funded.

##### 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 or subsequent to our last evaluation that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART III

ITEM 9.

DIRECTORS, EXECUTIVE OFFICERS, CONTROL PERSONS AND CORPORATE GOVERNANCE; COMPLIANCE WITH SECTION 16(A) OF THE EXCHANGE

A. I. Directors and Executive Officers - Summary Information.

The following are the directors and executive officers of the Company:

| <u>Name</u>         | <u>Age as of<br/>12/31/07</u> | <u>Position</u>  | <u>Position Held Since</u> |
|---------------------|-------------------------------|--|----------------------------|
| Dr. John W. Whitney | 61                            | President/Treasurer<br>Director                              | May 1988                   |
| Howland S. Green    | 54                            | Northeast Manager<br>of GOLD n GRO sales<br>Director         | April 2005                 |
| Gregory S. Skinner  | 53                            | Secretary  | December 1990              |
| Duane H. Rasmussen  | 77                            | Vice President;<br>Vice President and<br>General Manager-IMI | November 1997<br>May 1994  |

1) For directors, the term of office is until the next annual meeting of shareholders. For officers, the term of office is until the next annual meeting of the Board of Directors, presently scheduled to be held immediately following the annual meeting of the shareholders.

II. Narrative Information Concerning the Directors and Executive

Officers of the Company.

John W. Whitney:

In addition to being the President and a Director of the Company, 1988 to present, Dr. Whitney is the President and a Director of each of the operating subsidiaries, Itronics Metallurgical, Inc. and Whitney & Whitney, Inc. Dr. Whitney also serves as the General Manager of American Hydromet, a joint venture.

He received his Ph.D. in Mineral Economics from Pennsylvania State University in 1976, his M.S. in Mineralogy from the University of Nebraska in 1971, and his B.S. in Geology from the University of Nebraska in 1970. Dr. Whitney has served as President of Whitney & Whitney, Inc. since its formation in 1977.

Prior to his serving as W&W full-time president, Dr. Whitney worked as a consultant for the Office of Technology Assessment, U.S. Congress, doing analysis of various Alaskan mineral issues (1977-1978), a consultant for various government agencies, including the office of Mineral Policy Analysis in the U.S. Department of Interior, and the Washington office of the U.S. Bureau of Mines, consulting firms, law firms and mining companies on a variety of mineral planning issues (1976-1977), as a consultant for BKW Associates, Inc. evaluating mining investment opportunities in Mexico and the Philippines (1973-1975), and as a geologist-mineralogist for Humble Oil & Refining Company and GeoTerrex Ltd. (1971-1972).

Dr. Whitney is an internationally recognized consultant in the field of Metal and Material Resource Economics. Dr. Whitney has presented seminars for various clients on Mining Economics, and has taught a three-credit graduate course on International Metal Economics for the University of Arizona's College of Mines. Dr. Whitney is an Honorary Faculty Member of the Academy for Metals and Materials under the seal of the American Society for Metals. Dr. Whitney has made numerous presentations and written a number of publications on various technical subjects within his broad area of expertise. Dr. Whitney is coinventor of the American Hydromet process technology and holds four patents. Dr. Whitney was selected as Nevada's Inventor of the Year for 2000 and became a member of the Inventor's Hall of Fame at the University of Nevada, Reno.

Howland S. Green

Mr. Green was appointed as our director and as the Northeast Manager of GOLD n GRO Sales in April 2005. He received a B.Sc. degree in plant science and landscape architecture from the University of Rhode Island in 1981. He founded the Holly Ridge Nursery in Kingston, Rhode Island in 1989 and was its owner and President until the business was sold in September 2005. He is the concept creator and a founder of the North American Deer Management Network. Mr. Green researched and developed the Mirrepel and subsequently co-developed the GOLD n GRO Guardian systemic deer and rabbit repellents. Through his ownership of the Holly Ridge Nursery he has gained extensive knowledge of the landscape construction and maintenance and wholesale and retail nursery markets. He has also served as consultant to "Ask This Old House".

Gregory S. Skinner, Esq.

Mr. Skinner has served as secretary and general counsel of the Company and its subsidiaries since December 1990. He obtained his B.A. degree in Economics from the University of California at Berkeley in 1976. He obtained his J.D. degree from Hastings College of the Law, University of California at San Francisco in 1979. He is licensed to practice law in the states of California and Nevada. He retired from the practice of law on January 1, 2003 and is "of counsel" to the law office of Watson & Rounds, a Professional Corporation (WR). Prior to December 31, 2002 he was a shareholder in Skinner, Watson & Rounds, which had offices located in Reno, Las Vegas, and Incline Village, Nevada. Prior to becoming Secretary of Itronics Inc., Mr. Skinner has provided legal services and advice to Whitney

& Whitney, Inc. since 1980.

Duane H. Rasmussen:

Mr. Rasmussen has served as Vice President and General Manager of IMI since May 1994. He became Vice President of the Company in November 1997. He initially joined the Company in 1991 as Assistant Manager and Business Consultant for W&W. He received his B.S. degree in Chemical Engineering from the University of Wisconsin in 1953 and his M.B.A. in Industrial Management in 1955 from the same University. He served as President of Screen Printing Systems, Inc. from 1987 to 1990 and from 1995 to October 1998. Other business experience includes approximately 20 years with Jacobs Engineering Group, Inc. in varying capacities, including Project Manager, Regional Sales Manager, Regional Vice President, and Group Vice President.

B. AUDIT COMMITTEE

At present the Company does not have an audit committee and consequently the entire Board serves as the audit committee. The Board presently consists of two members, none of whom are independent. The Company has interviewed several qualified individuals for the position of Audit Committee Financial Expert on the Board of Directors. All have declined to serve, with the primary reason being personal liability issues, especially the perceived view that being the "financial expert" increases the individual's personal exposure over that of being a regular Board member.

C. CODE OF ETHICS

The Board of Directors has adopted a Code of Business Conduct and Ethics (Code) that is applicable to the Company's directors, principal executive and financial officer, principal accounting officer or controller, and persons performing similar functions. A copy of the Code is included in this report as Exhibit 14. A copy of the Code may be obtained by anyone, without charge, by requesting a copy either by telephoning (775) 689-7696 and asking for investor relations or by e-mailing the Company at [www.itronics.com](http://www.itronics.com). If requesting by e-mail, please indicate a preference of a reply by e-mail or by physical mail.

-

ITEM 10.

EXECUTIVE COMPENSATION.

Summary of Cash and Certain Other Compensation

The following table sets forth information as to the compensation of the Chief Executive Officer and the four most highly compensated officers whose compensation for the year ended December 31, 2007 exceeded \$100,000:

Summary Compensation Table:

Edgar Filing: ITRONICS INC - Form 10KSB

| Name and<br>Principal | Calendar    | Nonqualified  |                 | All Other           | Total        |
|-----------------------|-------------|---------------|-----------------|---------------------|--------------|
|                       |             | Compensation  | Deferred        |                     |              |
| <u>Position</u>       | <u>Year</u> | <u>Salary</u> | <u>Earnings</u> | <u>Compensation</u> | <u>Total</u> |
| Dr. John W. Whitney:  |             |               |                 |                     |              |
| President, Treasurer  | 2007        | \$131,000     | \$33,006        | \$ 3,138            | \$167,144    |
| and Director (1) (2)  | 2006        | \$126,788     | \$28,310        | \$ 3,138            | \$158,236    |
| Duane H. Rasmussen    |             |               |                 |                     |              |
| Vice President, VP    |             |               |                 |                     |              |
| and General Manager   |             |               |                 |                     |              |
| IMI (3)               | 2007        | \$132,000     | \$25,420        | -                   | \$157,420    |
|                       | 2006        | \$132,000     | \$21,731        | -                   | \$153,731    |

(1) The 2007 and 2006 salary amounts include \$98,566 and \$74,600, respectively, that were not paid currently.

Dr Whitney has \$709,566 in unpaid salary as of December 31, 2007, of which \$506,000 is committed to be converted into 15,250,000 common shares. The shares will be issued when sufficient cash is available to pay required payroll tax withholdings. This unpaid salary has accumulated since July 2001 and interest at 12% per annum accrues on the unpaid balance. The interest rate is based on the rate accruing to investors on convertible debt private placements in effect in 2001. Interest earned was \$79,372 and \$68,080 for 2007 and 2006, respectively. Of the 2007 amount, \$67,104 remained unpaid at December 31, 2007. The Nonqualified Deferred Compensation Earnings amounts in the above table represent accrued interest in excess of a defined interest rate using 120% of the July 2001 federal long term applicable rate.

(2) The salary amounts listed above include \$6,000 and \$1,788 for 2007 and 2006, respectively, that represent compensation paid in common stock for service as a director of the Company.

(3) The 2007 and 2006 salary amounts include \$72,500 and \$72,500, respectively, that were not paid currently.

Mr. Rasmussen has \$559,500 in unpaid salary as of December 31, 2007, of which \$154,000 is committed to be converted into 1,925,000 common shares. The shares will be issued when sufficient cash is available to pay required payroll tax withholdings. This unpaid salary has accumulated since July 2001 and interest at 12% per annum accrues on the unpaid balance. The interest rate is based on the rate accruing to investors on convertible debt private placements in effect in 2001. Interest earned was \$61,130 and \$52,260 for 2007 and 2006, respectively. Of the 2006 and 2007 amounts, \$63,845 remained unpaid at December 31, 2007. An additional total of \$37,430 in interest earned from July 2004 to June 2005 remains unpaid and will be paid by issuing 500,703 restricted common shares. The Nonqualified Deferred Compensation Earnings amounts in the above table represent accrued interest in excess of a defined interest rate using 120% of the July 2001 federal long term applicable rate.

Outstanding Equity Awards at Fiscal Year-End

:

|                     | Number of<br>Securities<br><br>Underlying<br>Unexercised |              |                                |
|---------------------|--|--------------|--------------------------------|
|                     | Options at   | Option       | Option                         |
|                     | <u>12/31/07</u>  | Exercise     | <u>Expiration</u>              |
| <u>Name</u>         | <u>Exercisable</u>                                       | <u>Price</u> | <u>Date</u>                    |
| Dr. John W. Whitney | 1,000,000  | \$0.25       | One year after employment ends |
|                     | 3,000,000  | \$0.30       | One year after employment ends |
|                     | 550,000  | \$0.15       | One year after employment ends |
| Total               | 4,550,000  |              |                                |
|                     |  |              |                                |
| Duane H. Rasmussen  | 425,000  | \$0.15       | One year after employment ends |

Director Compensation:

| <u>Name</u>         | Stock         |              |
|---------------------|---------------|--------------|
|                     | <u>Awards</u> | <u>Total</u> |
| Dr. John W. Whitney | \$ 6,000      | \$ 6,000     |
| Howland S. Green    | \$ 6,000      | \$ 6,000     |

The compensation plan for all directors was \$1,500 per quarter in common stock beginning with the fourth quarter of 2006.



ITEM 11.

SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

a) Equity Compensation Plan Information

|  | Number of securities to be issued upon exercise of outstanding options, warrants and rights | Weighted-average exercise price of outstanding options, warrants and rights | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) |
|--|---|---|---|
| <u>Plan Category</u>                                       | <u>(a)</u>  | <u>(b)</u>  | <u>(c)</u>  |
| Equity compensation plans approved by security holders     | -0-   | \$-0-   | -0-   |
| Equity compensation plans not approved by security holders | 6,264,000   | \$0.240   | 2,393,583   |
|  |   |   |   |
| <b>Total</b>   | <b>6,264,000</b>  | <b>\$0.240</b>  | <b>2,393,583</b>  |

b) Security Ownership of Certain Beneficial Owners.

The following table sets forth certain data with respect to those persons known to the Company, as of March 31, 2008, to be the beneficial owners of more than 5% of the outstanding shares of common stock of the Company:

Amount and Nature of Beneficial Ownership

| Name and Address of Beneficial Owner                | Common Shares                |                                      | Percent of Class |
|---|------------------------------|--------------------------------------|------------------|
|   | Common Shares Presently Held | Which May Be Acquired Within 60 days |                  |
| John W. Whitney<br>P.O. Box 10725<br>Reno, NV 89510 |                              |                                      |                  |
|   | <u>Total</u>                 |                                      |                  |

Edgar Filing: ITRONICS INC - Form 10KSB

|                 |            |            |            |     |
|-----------------|------------|------------|------------|-----|
| (1) (2) (3) (4) | 33,081,313 | 20,300,000 | 53,381,313 | 5.2 |
|-----------------|------------|------------|------------|-----|

(1) Director

(2) Officer

(3) Includes 72,768 shares owned by Maureen E. Whitney, Dr. Whitney's wife.

(4) Dr. Whitney's options include compensatory options of 1,000,000 common shares at \$0.25 per share, 3,000,000 common shares at \$0.30 per share, and 550,000 common shares at \$0.15 per share. The options are exercisable at any time until one year after Dr. Whitney leaves the employment of the Company. The Common Shares Which May Be Acquired Within 60 Days also includes 15,250,000 shares that are to be issued to Dr. Whitney when sufficient cash is available to pay payroll tax withholdings and 500,000 common shares to be issued in connection with his service on the Board of Directors.

c) Security Ownership of Management.

The following table sets forth as of March 31, 2008, certain information, with respect to director and executive officer ownership of common stock in the Company:

Amount and Nature of Beneficial Ownership

| Name and<br>Address of<br><u>Beneficial Owner</u>                   | Common Shares<br>Which May Be<br>Common Shares<br><u>Presently Held</u> | Common Shares<br>Acquired Within<br><u>60 days(1)</u> | Common Shares<br><u>Total</u> | Percent<br>of<br>Class<br><u>(2)</u> |
|---|---|---|-------------------------------|--------------------------------------|
| Dr. John W. Whitney<br>P.O. Box 10725<br>Reno, NV 89510 (3) (4) (5) | 33,081,313  | 20,300,000  | 53,381,313                    | 5.2                                  |
| Howland S. Green<br>895 Liberty Lane<br>West Kingston, RI 02892     | 1,899,483   | 1,500,000   | 3,399,483                     | 0.3                                  |
| Duane H. Rasmussen<br>P.O. Box 10725<br>Reno, NV 89510 (4)          | 2,202,973   | 2,850,703   | 5,053,676                     | .5                                   |

All directors and  
executive officers as

|                     |            |            |            |     |
|---------------------|------------|------------|------------|-----|
| a group (4 persons) | 37,836,088 | 24,650,703 | 62,486,791 | 6.1 |
|---------------------|------------|------------|------------|-----|

(1) Dr. Whitney's options include compensatory options of 1,000,000 common shares at \$0.25 per share, 3,000,000 common shares at \$0.30 per share, and 550,000 common shares at \$0.15 per share. The options are exercisable at any time until one year after Dr. Whitney leaves the employment of the Company. The Common Shares Which May Be Acquired Within 60 Days also includes 15,250,000 shares that are to be issued to Dr. Whitney when sufficient cash is available to pay payroll tax withholdings and 500,000 common shares to be issued in connection with his service on the Board of Directors.

In April 2005 Mr. Green was granted a compensatory option to acquire 1,000,000 of the Company's restricted common shares at \$0.10 per share. The first 500,000 shares subject to the option became exercisable when the Federal EPA accepted the registration application for the GOLD n GRO Guardian and the second 500,000 shares subject to the option became exercisable when the Federal EPA issued the registration for the GOLD n GRO Guardian. The entire option is exercisable for two years after the EPA registration was received in March 2008. The Common Shares Which May Be Acquired Within 60 Days includes 500,000 common shares to be issued in connection with his service on the Board of Directors.

Mr. Rasmussen was granted a compensatory option to acquire 425,000 restricted common shares at \$0.15 per share. This option is exercisable at any time until one year after Mr. Rasmussen leaves the employment of the Company. The Common Shares Which May Be Acquired Within 60 Days also includes 2,425,703 shares that are to be issued to Mr. Rasmussen when sufficient cash is available to pay payroll tax withholdings.

(2) The percent of class is based on the sum of 999,996,999 shares outstanding as of March 31, 2008 plus, for each individual, the number of common shares as to which the named individual has the right to acquire beneficial ownership within 60 days of March 31, 2008

(3) Director

(4) Officer

(5) Includes 72,768 shares owned by Maureen E. Whitney, Dr. Whitney's wife.

c) Changes in Control

The Company is not aware of any arrangement which at some later date results in changes in control of the Company.

ITEM 12.

CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE.

## Edgar Filing: ITRONICS INC - Form 10KSB

Advances from an officer/stockholder totaled \$143,025 and \$161,525 at December 31, 2007 and 2006, respectively.

\$779,073 and \$796,200 of the accrued management salaries as of December 31, 2007 and 2006, respectively, is for salary in arrears due to several officer/stockholders and employee/stockholders. In addition, salary in arrears of \$746,800 and \$514,800 for 2007 and 2006, respectively, are included in stock to be issued at the respective year ends. These amounts represent the portion of salaries earned but unpaid that the officers/employees/stockholders have agreed to accept in the Company's common stock and have relinquished their right to receive cash. When the stock is eventually issued, it will be issued at the market price on the date of the respective agreements. The number of shares to be issued is 18,173,958 and 6,348,958 for 2007 and 2006, respectively. Issuance of the stock is pending sufficient cash available to pay the related federal withholding taxes. Interest expense at 12% per annum on salaries due officer and employee/stockholders amounted to \$168,146 and \$143,478, respectively, in 2007 and 2006.

Interest expense on related party loans amounted to \$18,851 and \$19,383 for the years ended December 31, 2007 and 2006, respectively. Accrued interest on related party loans and accrued salaries totaled \$157,181 and \$87,211 at December 31, 2007 and 2006, respectively.

During 2003, WWI's lease of a vehicle utilized by Dr. Whitney was completed. Dr. Whitney purchased the vehicle by financing it through a commercial lender. The purchase price was \$21,741 and the monthly payment for four years is \$531. WWI is leasing the vehicle from Dr. Whitney by making the monthly payments to the commercial lender and acquired ownership of the vehicle when the loan was paid off in 2007.

-

-

### Director Independence

The Company had two directors who served on the Board during 2007. Dr. John W. Whitney is the President and Treasurer, and as such he is not independent. Howland S. Green serves as the Northeast Manager of GOLD n GRO sales, and as such he is not independent.

-

-

### ITEM 13.

### FINANCIAL STATEMENTS AND EXHIBITS

#### I. Index of Financial Statements and Exhibits

| <u>1. Index of Financial Statements:</u>                     | <u>Page No.</u> |
|--|-----------------|
| REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM      | 45              |
| Consolidated Balance Sheets as of December 31, 2007 and 2006 | 47              |
| Consolidated Statements of Operations for the Years ended    |                 |

## Edgar Filing: ITRONICS INC - Form 10KSB

|   |    |
|---|----|
| December 31, 2007 and 2006  | 49 |
| Consolidated Statements of Stockholders' Equity (Deficit)<br>for the Years ended December 31, 2007 and 2006 | 50 |
| Consolidated Statements of Cash Flows for the Years ended<br>December 31, 2007 and 2006                     | 51 |
| Notes to Consolidated Financial Statements  | 53 |
| <br>  |    |
| <b>2. <u>Index of Exhibits:</u></b>   |    |
| 14 Code of Business Conduct and Ethics  | 84 |
| 21 List of significant subsidiaries   | 85 |
| 31 Rule 15d-14(a) Certification   | 86 |
| 32 Section 1350 Certification   | 88 |

### STATEMENTS AND SCHEDULES

Schedules not included are omitted for the reason that they are not applicable or not required.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders  
of Itronics, Inc

We have audited the accompanying consolidated balance sheet of Itronics Inc. and subsidiaries (the "Company") as of December 31, 2007, and the related consolidated statements of operations, stockholders' equity (deficit) and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit. The consolidated financial statements of the Company as of December 31, 2006, were audited by other auditors whose report dated April 11, 2007, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The Company has determined that it is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2007, and the results of its operations and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As of December 31, 2007, the Company has an accumulated deficit of \$42,143,980, a negative working

capital of \$18,842,148, and a stockholders' deficit balance of \$15,663,973, and is in default on various leases and loans. The Company's ability to continue as a going concern is contingent upon the Company's ability to generate sufficient cash either through operations or through capital injections from debt or equity offerings, to meet obligations as they become due. These conditions raise substantial doubt about the Company's ability to continue as a going concern. Management's plans regarding this matter are described in Note 14. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ Moore Stephens Wurth Frazer and Torbet, LLP

Walnut, California

April 14, 2008

Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders

Itronics, Inc.

We have audited the accompanying consolidated balance sheets of Itronics Inc. and subsidiaries (the "Company") as of December 31, 2006, and the related consolidated statements of operations, stockholders' deficit and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audit in accordance with standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company has determined that it is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes, on a test basis, examination of evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company as of December 31, 2006, and the results of its consolidated operations and cash flows for the year then ended., in conformity with accounting principles generally accepted in the United States of America.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As of December 31, 2006, the Company has an accumulated deficit of \$31,661,456, a negative working capital of \$10,139,616, and a stockholders' deficit balance of \$7,429,505, and is in default on various leases and loans. The Company's ability to continue as a going concern is contingent upon (a) future profitable operations and (b) the ability to generate sufficient cash to meet obligations as they become due. These conditions raise substantial doubt about the Company's ability to continue as a going concern. Management's plans regarding this matter are described in Note 14. The financial statements do not include any adjustments that might result from the outcome of

this uncertainty.

/s/CACCIAMATTA ACCOUNTANCY CORPORATION

Irvine, California

April 11, 2007

ITRONICS INC. AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS  
DECEMBER 31, 2007 AND 2006

ASSETS

|  | <u>2007</u> |  | <u>2006</u> |
|--|-------------|--|-------------|
| CURRENT ASSETS   |             |  |             |
| Cash   | \$ 92,987   |  | \$ -        |
| Accounts receivable, less allowance for<br>doubtful accounts, 2007, \$4,600; 2006, \$4,600 | 17,561      |  | 36,493      |
| Inventories  | 889,996     |  | 548,399     |
| Prepaid expenses   | 94,952      |  | 316,872     |
|  |             |  |             |
| Total Current Assets   | 1,095,496   |  | 901,764     |
|  |             |  |             |
| PROPERTY AND EQUIPMENT   |             |  |             |



Edgar Filing: ITRONICS INC - Form 10KSB

|   |           |             |        |             |
|---|-----------|-------------|--------|-------------|
| Land  |           | 215,000     |        | 215,000     |
| Building and improvements   |           | 1,312,409   |        | 1,167,315   |
| Design and construction in progress,<br>manufacturing facility                        |           | 97,110      |        | 234,347     |
| Equipment and furniture   | 2,879,938 | 2,543,682   |        |             |
| Vehicles  | 222,298   | 200,557     |        |             |
| Equipment under capital<br>lease-equipment and furniture                              | 466,571   | 692,438     |        |             |
| Equipment under capital<br>lease-vehicles   |           | -           | 21,741 |             |
|   |           | 5,193,326   |        | 5,075,080   |
| Less: Accumulated depreciation and amortization                                       |           | 2,341,004   |        | 2,131,542   |
| Total Property and Equipment  |           | 2,852,322   |        | 2,943,538   |
| OTHER ASSETS  |           |             |        |             |
| Intangibles   |           | 76,500      |        | 76,500      |
| Deferred loan fees, less accumulated amortization 2007,<br>\$580,849; 2006, \$328,120 |           | 323,042     |        | 335,629     |
| Deposits  |           | 8,508       |        | 8,108       |
| Total Other Assets  |           | 408,050     |        | 420,237     |
|   |           | \$4,355,868 |        | \$4,265,539 |

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

LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)

|  | <u>2007</u> |  | <u>2006</u> |
|--|-------------|--|-------------|
| CURRENT LIABILITIES                                    |             |  |             |
| Bank overdraft   | \$ -        |  | \$ 13,834   |
| Accounts payable                                       | 672,163     |  | 521,188     |
| Accrued management salaries                            | 779,873     |  | 799,948     |
| Accrued expenses                                       | 272,267     |  | 206,830     |
| Insurance contracts payable                            | 13,761      |  | 12,597      |
| Interest payable to officer/stockholders               | 157,181     |  | 87,211      |
| Interest payable, long-term debt and lease obligations | 225,533     |  | 202,366     |
| Current maturities of long-term debt                   | 436,523     |  | 45,065      |
| Current maturities of capital lease obligations        | 463,996     |  | 389,032     |

Edgar Filing: ITRONICS INC - Form 10KSB

|  |            |  |            |
|--|------------|--|------------|
| Advances from stockholder  | 143,025    |  | 161,525    |
| Current maturities of capital lease due stockholder  | -          |  | 3,333      |
| Current maturities of convertible notes and accrued interest                                       | 3,497,838  |  | 3,304,027  |
| Convertible debt derivatives   | 13,003,762 |  | 4,876,175  |
| Warrant and option liability   | 231,224    |  | 380,083    |
| Other  | 40,498     |  | 38,166     |
|  |            |  |            |
| Total Current Liabilities  | 19,937,644 |  | 11,041,380 |
|  |            |  |            |
| LONG-TERM LIABILITIES  |            |  |            |
| Long-term debt, less current maturities  | 82,197     |  | 504,131    |
| Capital lease obligations, less current maturities   | -          |  | 149,533    |
|  |            |  |            |
| Total Long-Term Liabilities  | 82,197     |  | 653,664    |
|  |            |  |            |
| Commitments and Contingencies  | -          |  | -          |
|  |            |  |            |
| Total Liabilities  | 20,019,841 |  | 11,695,044 |
|  |            |  |            |
| STOCKHOLDERS' EQUITY (DEFICIT)   |            |  |            |
| Preferred stock, par value \$0.001 per share;<br>authorized 999,500 shares; issued and outstanding |            |  |            |
| 2006, 0 shares; 2005, 0 shares   |            |  | -          |
| Common stock, par value \$0.001 per share;<br>authorized 1,000,000,000 shares; issued and          |            |  |            |

Edgar Filing: ITRONICS INC - Form 10KSB

|  |              |  |              |
|--|--------------|--|--------------|
| outstanding 2007, 999,996,999; 2006, 337,581,957 | 999,997      |  | 337,582      |
| Additional paid-in capital                       | 24,692,645   |  | 23,305,788   |
| Accumulated deficit                              | (42,143,980) |  | (31,661,456) |
| Common stock to be issued                        | 787,365      |  | 583,868      |
| Accumulated other comprehensive income           | -            |  | -            |
| Common stock options outstanding, net            | -            |  | 4,713        |
|  |              |  |              |
| Total Stockholders Equity (Deficit)              | (15,663,973) |  | (7,429,505)  |
|  |              |  |              |
|  | \$4,355,868  |  | \$ 4,265,539 |

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

ITRONICS INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF OPERATIONS  
FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006

|                           | <u>2007</u> |  | <u>2006</u> |
|---------------------------|-------------|--|-------------|
| REVENUES                  |             |  |             |
| Photochemical fertilizer  | \$2,315,141 |  | \$1,843,580 |
| Mining technical services | 27,155      |  | 28,338      |
|                           |             |  |             |
| Total Revenues            | 2,342,296   |  | 1,871,918   |
|                           |             |  |             |

Edgar Filing: ITRONICS INC - Form 10KSB

|   |             |  |             |
|---|-------------|--|-------------|
| COST OF REVENUES (exclusive of depreciation and |             |  |             |
| amortization shown separately below)            |             |  |             |
| Photochemical fertilizer                        | 2,184,143   |  | 1,760,118   |
| Mining technical services                       | 33,993      |  | 36,607      |
|   |             |  |             |
| Total Cost of Revenues                          | 2,218,136   |  | 1,796,725   |
|   |             |  |             |
| Gross Profit (Loss) (exclusive of               |             |  |             |
| depreciation and amortization shown             |             |  |             |
| separately below)                               | 124,160     |  | 75,193      |
|   |             |  |             |
| OPERATING EXPENSES                              |             |  |             |
| Depreciation and amortization                   | 209,462     |  | 228,017     |
| Research and development                        | 395,369     |  | 293,934     |
| Sales and marketing                             | 1,257,506   |  | 725,165     |
| Delivery and warehousing                        | 132,440     |  | 108,116     |
| General and administrative                      | 1,072,811   |  | 944,467     |
|   |             |  |             |
| Total Operating Expenses                        | 3,067,588   |  | 2,299,699   |
|   |             |  |             |
| Operating Loss                                  | (2,943,428) |  | (2,224,506) |
|   |             |  |             |
| OTHER INCOME (EXPENSE)                          |             |  |             |
| Interest  | (1,089,554) |  | (1,176,607) |
| Loss on derivative instruments                  | (6,798,204) |  | (541,474)   |

Edgar Filing: ITRONICS INC - Form 10KSB

|  |                |  |               |
|--|----------------|--|---------------|
| Gain (loss) on sale of investments             | 348,026        |  | 97,728        |
| Other  | 636            |  | 34,974        |
|  |                |  |               |
| Total Other Income (Expense)                   | (7,539,096)    |  | (1,585,379)   |
|  |                |  |               |
| (Loss) before provision for income tax         | (10,482,524)   |  | (3,809,885)   |
| Provision for income tax                       | -              |  | -             |
|  |                |  |               |
| Net Loss                                       | (10,482,524)   |  | (3,809,885)   |
|  |                |  |               |
| Other comprehensive income                     |                |  |               |
| Unrealized gains (losses) on securities        | -              |  | 39,889        |
|  |                |  |               |
| Comprehensive Loss                             | \$(10,482,524) |  | \$(3,769,996) |
|  |                |  |               |
| Weighted average number of shares outstanding, |                |  |               |
| basic and diluted                              | 496,301,587    |  | 235,294,220   |
|  |                |  |               |
| Loss per share, basic and diluted              | \$(0.021)      |  | \$(0.016)     |

The accompanying notes are an integral part of these financial statements

ITRONICS INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (DEFICIT)

FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006

|  |                     |  |            |  |             |
|--|---------------------|--|------------|--|-------------|
|  | <u>COMMON STOCK</u> |  |            |  | ACCUMULATED |
|  |                     |  | ADDITIONAL |  | COMMON      |
|  |                     |  |            |  | OTHER       |

Edgar Filing: ITRONICS INC - Form 10KSB

|                         | NUMBER<br>OF |           |              |                |              |               |
|-------------------------|--------------|-----------|--------------|----------------|--------------|---------------|
|                         | SHARES       |           | PAID-IN      | ACCUMULATED    | STOCK<br>TO  | COMPREHENSIVE |
|                         | (1,000_s)    | AMOUNT    | CAPITAL      | DEFICIT        | BE<br>ISSUED | INCOME        |
| Balance, Dec. 31, 2005  | 197,148      | \$197,148 | \$21,646,307 | \$(27,851,571) | \$573,993    | \$(39,889)    |
| Issue of common stock:  |              |           |              |                |              |               |
| For cash                | 100          | 100       | 7,400        | -              |              | -             |
| For services            | 24,350       | 24,350    | 412,703      | -              | (3,725)      | -             |
| For debt conversion     | 108,723      | 108,723   | 1,114,839    | -              | 13,600       | -             |
| For asset acquisition   | 7,261        | 7,261     | 124,539      | -              | -            | -             |
| Net (loss) for the year |              |           |              |                |              |               |
| ended Dec. 31, 2006     | -            | -         | -            | (3,809,885)    | -            | -             |
| Other comprehensive     |              |           |              |                |              |               |
| income for the year     |              |           |              |                |              |               |
| ended Dec. 31, 2006     | -            | -         | -            | -              | -            | 39,889        |
| Common stock options    |              |           |              |                |              |               |
| outstanding             | -            | -         | -            | -              | -            | -             |
| Balance, Dec. 31, 2006  | 337,582      | 337,582   | 23,305,788   | (31,661,456)   | 583,868      | -             |
| Issue of common stock   |              |           |              |                |              |               |
| For cash                |              |           |              |                |              |               |
| For services            | 99,274       | 99,274    | 588,713      | -              | 217,097      | -             |

Edgar Filing: ITRONICS INC - Form 10KSB

|                         |         |           |              |                |           |     |
|-------------------------|---------|-----------|--------------|----------------|-----------|-----|
| For debt conversion     | 555,410 | 555,410   | 698,057      | -              | (13,600)  | -   |
| For asset acquisition   | 7,731   | 7,731     | 100,087      | -              | -         | -   |
| Net (loss) for the year |         |           |              |                |           |     |
| ended Dec. 31, 2007     | -       | -         | -            | (10,482,524)   | -         | -   |
| Other comprehensive     |         |           |              |                |           |     |
| income for the year     |         |           |              |                |           |     |
| ended Dec. 31, 2007     | -       | -         | -            | -              | -         | -   |
| Common stock options    |         |           |              |                |           |     |
| outstanding             | -       | -         | -            | -              | -         | -   |
|                         |         |           |              |                |           |     |
| Balance, Dec. 31, 2007  | 999,997 | \$999,997 | \$24,692,645 | \$(42,143,980) | \$787,365 | \$- |

The accompanying notes are an integral part of these financial statements

ITRONICS INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006

|   | <u>2007</u>    |  | <u>2006</u>   |
|---|----------------|--|---------------|
| Cash flows from operating activities                                    |                |  |               |
| Net loss  | \$(10,482,524) |  | \$(3,809,885) |
| Adjustments to reconcile net loss to cash used by operating activities: |                |  |               |
| Depreciation and amortization   | 462,191        |  | 498,947       |
| Interest on convertible notes   | 528,365        |  | 581,889       |



Edgar Filing: ITRONICS INC - Form 10KSB

|  |             |  |             |
|--|-------------|--|-------------|
| Loss on change in derivative instruments     | 6,798,204   |  | 541,474     |
| Inventory reserve                            | -           |  | 104,161     |
| (Gain) loss on sale of marketable securities | (348,026)   |  | (97,728)    |
| Addition of silver in solution inventory by  |             |  |             |
| offsetting photochemical processing fees     | (320,232)   |  | (198,841)   |
| Gain on debt forgiveness                     | -           |  | (34,833)    |
| Other  | -           |  | 52          |
| Stock and option compensation                | 13,584      |  | 4,300       |
| Expenses paid with issuance of common stock: |             |  |             |
| Interest expense                             | -           |  | 7,483       |
| Consulting expenses                          | 552,887     |  | 27,840      |
| Director fees                                | 16,388      |  | 3,976       |
| Salaries                                     | 290,142     |  | 145,992     |
| Expenses paid with issuance of debt          |             |  |             |
| (Increase) decrease in:                      |             |  |             |
| Trade accounts receivable                    | 18,932      |  | (15,381)    |
| Inventories                                  | 40,591      |  | 138,379     |
| Prepaid expenses, deposits and other         | (327)       |  | 8,112       |
| Increase (decrease) in:                      |             |  |             |
| Accounts payable                             | 150,973     |  | 147,740     |
| Accrued management salaries                  | 225,925     |  | 200,048     |
| Accrued expenses and contracts payable       | 162,070     |  | 48,084      |
| Net cash used by operating activities        | (1,890,857) |  | (1,698,191) |
|  |             |  |             |
| Cash flows from investing activities:        |             |  |             |

Edgar Filing: ITRONICS INC - Form 10KSB

|  |           |  |           |
|--|-----------|--|-----------|
| Acquisition of property and equipment            | (61,428)  |  | (29,835)  |
| Sale of investments                              | 348,026   |  | 229,374   |
| Acquisition of intangibles                       | (400)     |  | -         |
| Net cash provided (used) by investing activities | 286,198   |  | 199,539   |
|  |           |  |           |
| Cash flows from financing activities:            |           |  |           |
| Proceeds from sale of stock                      | -         |  | 7,500     |
| Proceeds from officer/stockholder advances       | 8,000     |  | 10,212    |
| Proceeds from debt                               | 1,960,000 |  | 1,941,167 |
| Debt issuance costs                              | (140,142) |  | (247,602) |
| Bank overdraft                                   | (13,834)  |  | 13,834    |
| Payments on debt                                 | (116,378) |  | (250,719) |
| Net cash provided by financing activities        | 1,697,646 |  | 1,474,392 |
|  |           |  |           |
| Net increase (decrease) in cash                  | 92,987    |  | (24,260)  |
| Cash, beginning of year                          | -         |  | 24,260    |
|  |           |  |           |
| Cash, end of year                                | \$ 92,987 |  | \$ -      |

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

ITRONICS INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2006

(continued)

Edgar Filing: ITRONICS INC - Form 10KSB

|   | <u>2007</u> | <u>2006</u> |
|---|-------------|-------------|
| Supplemental Disclosures of Cash Flow                 |             |             |
| Information:  |             |             |
| Cash paid during the period for interest              | \$ 205,917  | \$ 232,706  |
| Schedule of non-cash financing transactions:          |             |             |
| Settlement of debt/accruals by                        |             |             |
| issuance of common stock:                             |             |             |
| Convertible notes and accrued interest                | 1,221,367   | 1,237,162   |
| Short-term debt due an officer/stockholder            | 18,500      | -           |
| Accrued management salaries                           | 246,000     | -           |
| Marketable securities received for sale of investment | 138,353     | -           |
| Acquisition of assets by issuance of common stock:    |             |             |
| Equipment   | 56,818      | 131,800     |
| Inventory   | 61,956      | -           |
| Warrants issued for debt issuance costs               | -           | 17,595      |
| Amounts withheld from proceeds of debt, unrelated:    |             |             |
| Prepaid interest                                      | -           | -           |
| Deferred loan costs                                   | 100,000     | 30,000      |
| Accounts payable                                      | -           | 28,833      |

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

ITRONICS INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
DECEMBER 31, 2007 AND 2006

NOTE 1 - Summary of Significant Accounting Policies:

Company's Activities:

Itronics Inc., through its subsidiaries, (the Company) is involved in photochemical recycling and related silver recovery, liquid fertilizer manufacturing, and mining technical services.

Financial Statement Estimates and Assumptions:

The preparation of financial statements in conformity with accounting principles generally accepted in the U.S. requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. For example, the Company estimates the fair value of its derivative instruments using the Black-Scholes option pricing model. As the Company's stock price is highly volatile, and the underlying debt amounts are relatively large, the valuation of the derivatives is subject to material swings from period to period. The Company measures the silver received in photochemical liquids and estimates the amount, recoverability, and ultimate realizable value of the silver in ending inventory.

Principles of Consolidation:

The consolidated financial statements include the accounts of

Itronics Inc. and its subsidiaries:

|   | 2007              | 2006              |
|---|-------------------|-------------------|
|   | <u>PERCENTAGE</u> | <u>PERCENTAGE</u> |
| Whitney & Whitney, Inc.                           | 100.00            | 100.00            |
| Itronics Metallurgical, Inc.                      | 100.00            | 100.00            |
| Itronics California, Inc.                         | 100.00            | 100.00            |
| Nevada Hydrometallurgical Project (A Partnership) | 92.50             | 92.50             |
| American Hydromet (A Joint Venture)               | 82.53             | 82.53             |
| American Gold & Silver (A Limited Partnership)    | 47.77             | 47.77             |
| Itronics Gold n Minerals, Inc.                    | 100.00            | N/A               |

Whitney & Whitney, Inc. is the general partner for American Gold & Silver. As such, the Company has control over American Gold & Silver and has included it in its consolidation.

American Gold & Silver and Nevada Hydrometallurgical Project possess no material tangible assets or liabilities.

No amount for minority interests is reflected in the consolidated balance sheets as the equity of minority interests in the net losses exceed the carrying value of the minority interests.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

No amount for minority interests is reflected in the consolidated statement of operations since losses applicable to the minority interest in each subsidiary exceed the minority interest in the equity capital of each subsidiary. As a result, losses applicable to the minority interest are charged against the majority interest. When future earnings materialize, the majority interest will be credited to the extent of such losses previously absorbed.

All significant intercompany accounts and transactions have been eliminated in the consolidation.

Revenue recognition:

The Company manufactures fertilizer from used photochemical liquids. Revenues are generated in three distinct areas: (1) fees associated with removing used photochemical liquids from customer sites and sales of photochemical concentrators, (2) sales of fertilizer and (3) sales of silver. Fertilizer and retail silver sales are recognized when goods are shipped to our customers. We pay 1% of invoice amount to our primary fertilizer distributor in order to receive accelerated payment terms. The fee is netted against fertilizer sales. Sales of silver bullion and silver in film are recorded when the silver content and the sales price are determined, which is approximately two weeks after shipment for silver bullion and 30 to 45 days after shipment for film. Returns and allowances have been nominal. Service fees from photochemical recycling are recorded after the photochemical liquids have been picked up and transported from our customers to our manufacturing facility.

The Company provides consulting services to various entities in the mining industry. Revenue is recognized as services are delivered. When the mining technical services segment of the Company is responsible for the procurement of materials and equipment, property, or subcontracts in its consulting business, it includes such amounts in both revenues and cost of sales. The amount of such pass-through costs included in both mining consulting revenues and cost of revenues for the years ended December 31, 2007 and 2006 were \$1,541 and \$2,547, respectively. In addition, the Company periodically receives property or other payments on behalf of its clients and disburses the funds to a designated third party. When the Company has little or no risk of loss in the process, such payments are netted and not included in gross revenues or cost of revenues. Such payments amounted to \$-0- for the years ended December 31, 2007 and 2006, respectively.

The Company bills its customers for its approximate costs for delivering merchandise sold to the customer. Such amounts are included in revenues. The related shipping costs are included in Delivery and Warehousing expenses in the Operating Expense section of the Consolidated Statements of Operations. Such costs were \$132,440 and \$108,116 for the years ended December 31, 2007 and 2006, respectively.

Cash and Cash Equivalents:

At present, cash includes only deposits in checking and money market accounts and does not include any cash equivalents.

ITRONICS INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

Accounts Receivable Allowance Account:

The Company uses the allowance method to account for uncollectible accounts receivable.

Marketable Securities:

The Company periodically has investments in marketable securities, received as payment from technical services customers. All of these equity securities are available for sale and are recorded at fair value. The change in fair value is recorded as an unrealized gain or loss in other comprehensive income. Upon sale of the security, the company recognizes a realized gain or loss, based on specific identification of security sold. Unrealized losses are charged against net earnings when a decline in fair value is determined to be other than temporary. The Company held no marketable securities as of December 31, 2007 and 2006.

Inventories:

Inventory is carried on the balance sheet at the lower of cost or market value using the average cost valuation method and consists primarily of silver bearing materials, raw materials and fertilizer. Because a large part of our inventory is silver and the market price of silver changes daily on the commodities market, we regularly monitor the carrying value of our silver inventory to ensure it is carried at the lower of cost or its current market value. If silver on the open market were less than our carrying value, we would write down the carrying value of our inventory by reducing recorded inventory and increasing cost of sales. If the amount of the write down were material, we would separately include the item in our statement of operations. The raw material and work in progress balances below include \$640,484 and \$405,631 in silver bearing unprocessed photochemicals or partially processed materials as of December 31, 2007 and 2006, respectively. The Company also evaluates the recoverability of silver contained in the various raw materials and refining byproducts and estimates how long it will take to recover the estimated silver ounces contained in the materials. In 2006, the Company recorded a recoverability reserve of \$70,199 and a slow moving reserve of \$33,962. The \$104,161 reserve expense is included in Cost of Revenues in the Consolidated Statement of Operations for the year ended December 31, 2006. The Company's review of the silver content and recoverability of our silver inventory determined that these reserves are adequate as of December 31, 2007.

Following is a summary of finished goods, work in progress, and raw materials inventories as of December 31, 2007 and 2006:

ITRONICS INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

|                             | <u>2007</u> |  | <u>2006</u> |
|-----------------------------|-------------|--|-------------|
| Finished goods              | \$46,211    |  | \$ 19,275   |
| Work in progress            | 522,273     |  | 340,594     |
| Raw materials               | 425,673     |  | 292,691     |
|                             | 994,157     |  | 652,560     |
| Less: Silver recoverability |             |  |             |
| and slow moving reserves    | 104,161     |  | 104,161     |
|                             |             |  |             |
| Net Inventory               | \$889,996   |  | \$548,399   |

Accounts Receivable and Inventory Factoring:

The Company factors some of its receivables and inventory with unrelated third parties. A liability is recorded when cash is received; interest is recorded over the period the liability is outstanding. The liability and accrued interest is repaid within a day or two of when the Company is paid by the customer. Interest rates range from 2 to 3% per month, or 24 to 36% annually. Additionally, while the Company does not have any formal limits on the amounts it can factor, typically no more than \$120,000 in assets is factored at any given time. As of December 31, 2007 and 2006 all factoring arrangements were paid in full.

Property and Equipment:

Property and equipment are stated at cost. Costs associated with creating website content and graphics are capitalized under EITF 00-2, "Accounting for Web Site Development Costs." Depreciation is computed by accelerated and straight-line methods. Depreciation expense was \$177,785 and \$182,001 for the years ended December 31, 2007 and 2006, respectively. Capital lease equipment is amortized using accelerated and straight-line methods. Amortization expense on capital lease equipment was \$31,677 and \$46,016 for the years ended December 31, 2007 and 2006, respectively. Accumulated amortization on capital lease equipment is \$308,449 and \$439,103 at December 31, 2007 and 2006, respectively. Property and equipment is depreciated or amortized over the following periods. Capitalized interest on major capital projects was \$-0- and \$28,656 in 2007 and 2006, respectively.



|   |               |
|---|---------------|
| Building and improvements                             | 20 - 40 years |
| Equipment and furniture                               | 3 - 20 years  |
| Vehicles  | 5 years       |
| Equipment under capital lease-equipment and furniture | 5 - 20 years  |
| Equipment under capital lease-vehicles                | 5 years       |

Repairs and maintenance, including website maintenance and administration, are charged to operations as incurred.

Intangible Assets:

Intangible assets are amortized as follows:

ITRONICS INC. AND SUBSIDIARIES  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
 DECEMBER 31, 2007 AND 2006

|                    | <u>METHOD</u>      | <u>YEARS</u> |
|--------------------|--------------------|--------------|
| Deferred loan fees | Effective Interest | 3-15         |

Estimated aggregate amortization expense for the succeeding five years is:

|      |           |
|------|-----------|
| 2008 | \$170,729 |
| 2009 | 93,022    |
| 2010 | 41,666    |
| 2011 | 3,255     |
| 2012 | 3,255     |

Convertible Debt Derivatives:

The Company has obtained callable secured convertible debt financing (Notes) in 2006 and 2005. The Notes are potentially convertible into an unlimited number of common shares. Accordingly, the Company has accounted for the Notes in accordance with SFAS 133, *Accounting for Derivative Instruments*, EITF 00-19, *Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock*, and DIG's B38 and B39, *Embedded Derivatives*:

## Edgar Filing: ITRONICS INC - Form 10KSB

*Evaluation of Net Settlement with Respect to the Settlement of a Debt Instrument through Exercise of an Embedded Put Option or Call Option and Embedded Derivatives: Application of Paragraph 13(b) to Call Options That Are Exercisable Only by the Debtor, respectively, which require the beneficial conversion features and the prepayment penalties to be treated as embedded derivatives and recorded as a liability based on their relative estimated fair values. In addition, all warrants and options that are exercisable during the period that the Notes are outstanding are required to be recorded as liabilities at their fair value. The fair value of the conversion feature and the prepayment penalty (when applicable) are estimated using the Black-Scholes option pricing model and taking a weighted average value based on various probabilities that the debt would be paid off prior to maturity at specified dates and therefore incurring the prepayment penalty. In accordance with SFAS No. 133, *Accounting for Derivative Instruments*, the Company is required to adjust the carrying value of the derivative instruments to its fair value at each balance sheet date and recognize any change since the prior balance sheet date as a component of Other Income (Expense). These derivatives are more fully discussed in Note 4 below.*

### Research and Development:

Wages, benefits, rent, and other costs, including costs to plan and populate databases and content on our web site development costs are expensed as incurred as research and development in accordance with SFAS 2 *Accounting for Research and Development Costs*, and EITF 00-2 *Accounting for Web Site Development Costs*.

## ITRONICS INC. AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

### Advertising:

The Company advertises its products in various trade publications and general newspaper supplements. It also promotes the Company in various business publications, television, and internet media. Such advertising costs include the creative process, costs of production, and placement costs of the ads themselves. All advertising costs are expensed as incurred. Total advertising expense was \$309,014 and \$143,760 for the years ended December 31, 2007 and 2006, respectively.

### Income Taxes:

The Company has accounted for income taxes to conform to the requirements of Statements of Financial Accounting Standards (SFAS) No. 109, *Accounting for Income Taxes*. Under the provisions of SFAS 109, an entity recognizes deferred tax assets and liabilities for future tax consequences of events that have already been recognized in the

Company's financial statements or tax returns. The measurement of deferred tax assets and liabilities is based on provisions of the enacted tax law. The effects of future changes in tax laws or rates are not anticipated. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

#### Loss per Common Share:

Loss per common share is calculated based on the consolidated net loss for the period divided by the weighted average number of common shares outstanding during 2007 and 2006. Common stock equivalents are not included,

as their effect would be antidilutive.

Following is a reconciliation of Net Income (Loss) and Weighted average number of shares outstanding, in the computation of earnings (loss) per share (EPS) for the years ended December 31, 2007 and 2006.

|   | <u>2007</u>    |  | <u>2006</u>   |
|---|----------------|--|---------------|
| Net Loss                                      | \$(10,482,524) |  | \$(3,809,885) |
| Less: Preferred stock dividends               | -              |  | -             |
|   |                |  |               |
| Basic EPS loss available to                   |                |  |               |
| common stockholders                           | \$(10,482,524) |  | \$(3,809,885) |
|   |                |  |               |
| Weighted average number of shares outstanding | 496,301,587    |  | 235,294,220   |
|   |                |  |               |
| Common equivalent shares                      | -              |  | -             |
|   |                |  |               |
|   | 496,301,587    |  | 235,294,220   |
|   |                |  |               |
| Per share amount                              | \$(0.021)      |  | \$(0.016)     |

Warrants, options, and shares to be issued, totaling 6,627,107,258 and 661,931,877 shares as of December 31, 2007 and 2006, respectively, would dilute

EPS, and accordingly are not included in the computation of EPS.

#### ITRONICS INC. AND SUBSIDIARIES

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

Common Stock:

The Company's common shares have, subject to the provisions of any series of Preferred Stock, certain rights including one vote per share on a non-cumulative basis and a ratable portion of any dividends that may be declared by the Board of Directors. The Company may from time to time issue common shares that are restricted under Rule 144 of the Securities and Exchange Commission. Such restrictions require the shareholder to hold the shares for a minimum of six months before sale. In addition, officers, directors and more than 10% shareholders are further restricted in their ability to sell such shares.

Stock Based Compensation:

The Company adopted the provisions of SFAS 123(R), *Share-Based Payments*, on January 1, 2006. Accordingly, compensation costs for all share-based awards to employees are measured based on the grant date fair value of those awards and recognized over the period during which the employee is required to perform service in exchange for the award (generally over the vesting period of the award). We have no awards with market or performance conditions. Effective January 1, 2006 and for all periods subsequent to that date, SFAS 123(R) supersedes our previous accounting under Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25"). In March 2005, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 107 ("SAB 107") relating to SFAS 123(R). The Company has applied the provisions of SAB 107 in its adoption of SFAS 123(R).

The Company adopted SFAS 123(R) using the modified prospective transition method, which provides for certain changes to the method for valuing share-based compensation. The valuation provisions of SFAS 123(R) apply to new awards and to awards that are outstanding at the effective date and subsequently modified or cancelled. Estimated compensation expense for awards outstanding at the effective date will be recognized over the remaining service period using the compensation cost calculated for pro forma disclosure purposes under FASB Statement No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123"). Our consolidated financial statements for the years ended December 31, 2007 and 2006 reflect the impact of SFAS 123(R). In accordance with the modified prospective transition method, our consolidated financial statements for prior periods were not restated to reflect, and do not include, the impact of SFAS 123(R).

Stock-based compensation expense recognized during the period is based on the value of the portion of share-based payment awards that is ultimately expected to vest during the period. Share-based compensation expense recognized in our consolidated statement of operations for the years ended December 31, 2007 and 2006 included compensation expense for share-based payment awards granted prior to, but not yet vested as of, December 31, 2005 based on the grant date fair value estimated in accordance with the pro forma provisions of SFAS 123. For share awards granted prior to 2006, expenses are amortized under the straight-line method prescribed by SFAS 123. As share-based compensation expense recognized in the consolidated statements of operations for the years ended December 31, 2007 and 2006 is based on awards ultimately expected to vest, it has been reduced for estimated forfeitures. SFAS 123(R) requires

ITRONICS INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Based on our evaluation of our present employees with unvested options, we estimated no forfeitures.

Total share-based compensation expense recognized under SFAS 123R for the years ended December 31, 2007 and 2006 was \$13,584 and \$4,300, respectively, and is included in general and administrative expenses. In addition to this share-based compensation for employees, the Company periodically issues options or warrants to consultants for services provided. The amount of such compensation was \$-0- and \$17,595 for the years ended December 31, 2007 and 2006, respectively. The 2006 amount was capitalized as debt issuance costs and is being amortized using the effective interest method.

We have no formal stock option plan. Options granted to date have been negotiated with individual employees and can be separated into three categories. Executive officers have been granted options on a periodic basis. The majority of these options expire one year after the officer leaves employment and they all vested on the grant date. The last such grant for these individuals was in 2004. Members of the management team are granted three year options for each quarter of continued employment. These options vest upon grant. These individuals also received a one time grant of options in 2004 that expire one year after the employee leaves employment. These options vested immediately. The third category of option grant is for sales and marketing representatives. The options to these employees are granted after each year of employment, have ten year exercise periods, with a portion vesting upon grant and a portion vesting after three years of service from the grant date. These employees also earn stock bonuses for each quarter of continued employment. The maximum number of options and stock bonus shares that can be earned by the management and sales representative employees was 3,286,000 and 3,430,000 as of December 31, 2007 and 2006, respectively. The number of shares remaining to be issued or granted was 2,393,583 and 2,864,917 as of December 31, 2007 and 2006, respectively.

In addition to the above option program, certain employees, directors and various consultants receive the majority of their compensation in common shares. Shares issued for consulting services include such services as transportation, contracting, and corporate marketing and investor relations programs. Shares issues to employees, directors, and consultants are valued at the closing market price of our common stock on the transaction date. Total expense paid in common stock for employees, directors, and consultants was \$859,417 and \$185,291 for the years ended December 31, 2007 and 2006, respectively. These expenses are allocated between the two segments and between expense categories in the Consolidated Statements of Operations based on the type of service provided.

The option compensation amounts for employees and consultants are estimated for each quarter using the Black-Scholes option pricing model. Volatility is calculated each reporting period and the calculation involves matching data points of our common share market price to the length of the option period. The following assumptions were used for 2007 and 2006 in estimating the fair value of the options:

ITRONICS INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

|                | <u>2007</u> | <u>2006</u> |
|----------------|-------------|-------------|
| Dividend yield | 0%          | 0%          |

## Edgar Filing: ITRONICS INC - Form 10KSB

|   |                |                 |
|---|----------------|-----------------|
| Risk-free interest rate                             | 3.80% to 4.88% | 4.50% to 4.875% |
| Expected life                                       | 3-10 years     | 3-10 years      |
| Expected volatility                                 | 94.7 to 107.5  | 82.1% to 102.3% |
| Weighted average exercise price granted during year | \$0.163        | \$0.185         |

Additional information about compensatory as well as non-compensatory options and warrants is presented in Note 7 below.

### Asset Impairment:

The Company monitors conditions that may affect the carrying value of its long-lived and intangible assets when events and circumstances indicate that the carrying value of the assets may be impaired. The Company determines impairment based on the asset's ability to generate cash flow greater than the carrying value of the asset. If projected undiscounted cash flows are less than the carrying value of the asset, the asset is adjusted to its fair value.

### Non-monetary Transactions:

The Company periodically enters into non-monetary transactions. These transactions are recorded based on the fair value of the asset, goods or services received or surrendered, whichever is more clearly evident and at such time as the earnings process is complete. When material non-monetary transactions occur, the Company discloses the transaction and basis for valuing the transaction in the period the transaction occurs. Additionally, pursuant to SFAS No. 95, "Statement of Cash Flows," the Company discloses non-cash investing and financing activities.

### Contingencies:

From time to time, the Company may become party to claims against it. Management evaluates these claims as they arise as probable, reasonably possible and remote. A liability is recorded when management estimates a loss is probable. Potential costs that arise are disclosed when management believes a loss is reasonably possible and that amount can be estimated.

### Recent Accounting Pronouncements

In December 2006 the FASB staff issued *FSP EITF 00-19-2 "Accounting for Registration Payment Arrangements"* to specify the accounting treatment of contingent obligations to make future payments or otherwise transfer consideration under a registration payment arrangement. Our callable secured convertible debt includes an obligation for us to file registration statements with the Securities and Exchange Commission (SEC) to register sufficient common shares for the note holders to convert the debt into common stock frames and

ITRONICS INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

also obligates us to have the registration statements declared effective by the SEC. This new standard requires us to evaluate the contingent future payments under the criteria of a probable loss under FAS 5. The Company adopted this new standard effective for the first fiscal quarter of 2007. The new standard has not had a significant impact on the Company's financial position or results of operations.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157 ("*SFAS 157*"), "*Fair Value Measurements*," which defines fair value, establishes guidelines for measuring fair value and expands disclosures regarding fair value measurements. SFAS 157 does not require any new fair value measurements but rather eliminates inconsistencies in guidance found in various prior accounting pronouncements. SFAS 157 is effective for fiscal years beginning after November 15, 2007 with earlier adoption permitted. The Company is currently evaluating the impact of SFAS 157, but does not expect the adoption of SFAS 157 to have a material impact on our consolidated financial position, results of operations or cash flows.

In February 2006, the FASB issued Statement of Financial Accounting Standards No. 155 ("*SFAS 155*"), "*Accounting for Certain Hybrid Financial Instruments*". SFAS 155 simplifies the accounting for certain derivatives embedded in other financial instruments by allowing them to be accounted for as a whole if the holder elects to account for the whole instrument on a fair value basis. SFAS 155 is effective for all financial instruments acquired, issued or subject to a re-measurement event occurring in fiscal years beginning after September 15, 2006. Earlier adoption is permitted, provided the Company has not yet issued financial statements, including for interim periods, for that fiscal year. The Company adopted SFAS 155 in the first quarter of 2007 and it has not had a material impact on our consolidated financial position, results of operations or cash flows.

NOTE 2 - Reclassification:

The prior year's financial statements have been reclassified, where necessary, to conform with the current year presentation.

NOTE 3 - Long-Term Debt:

Long-term debt at December 31, 2007 and 2006 is comprised of the following (all debt payments are applied to outstanding interest owed at date of payment prior to being applied to the principal balance). The carrying amount, except for the callable secured convertible notes which are accounted for as derivative instruments, approximates fair value. The fair value of long-term debt is based on current rates at which the Company could borrow funds with similar remaining maturities.

## ITRONICS INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

|  | <u>DECEMBER 31,</u> |  |             |
|--|---------------------|--|-------------|
|  | <u>2007</u>         |  | <u>2006</u> |
| <u>Notes due to unrelated parties:</u>                 |                     |  |             |
|  |                     |  |             |
| Note payable secured by real property due May 2016.    |                     |  |             |
| Monthly payment is \$6,601, including interest         |                     |  |             |
| at 12% per annum.                                      | \$418,456           |  | \$445,653   |
|  |                     |  |             |
| Financing contract secured by equipment due May 2006.  |                     |  |             |
| Monthly payment is \$806, including interest at 17.99% | 14,589              |  | 14,589      |
|  |                     |  |             |
| City of Reno Special Assessment District for road      |                     |  |             |
| and access improvements. Payable in 40 equal semi-     |                     |  |             |
| annual payments plus interest at 6% percent per annum. | 85,675              |  | 88,954      |
|  |                     |  |             |
| Less current portion due within one year               | (436,523)           |  | (45,065)    |
|  |                     |  |             |
| Total long-term liabilities due to unrelated parties   | \$ 82,197           |  | \$ 504,131  |

|  | <u>DECEMBER 31,</u> |  |             |
|--|---------------------|--|-------------|
|  | <u>2007</u>         |  | <u>2006</u> |
|  |                     |  |             |



Edgar Filing: ITRONICS INC - Form 10KSB

|   |             |  |              |
|---|-------------|--|--------------|
|   |             |  |              |
| <u>Convertible Promissory Notes:</u>  |             |  |              |
|   |             |  |              |
| Three year convertible promissory notes due at varying dates through February 2006, including interest at 9% to 12% per annum. The notes and accrued interest are convertible into the Company s restricted common stock at prices ranging from \$0.10 to \$1.18 per share at the election of the note holders. | \$1,437,000 |  | \$ 1,637,000 |
|   |             |  |              |
| Accrued interest on convertible promissory notes  | 2,060,838   |  | 1,667,027    |
|   |             |  |              |
|   |             |  |              |
| Less current portion due within one year  | (3,497,838) |  | (3,304,027)  |
|   |             |  |              |
| Total Long Term Convertible Promissory Notes and Accrued Interest   | \$ -        |  | \$ -         |

|  |                     |  |             |
|--|---------------------|--|-------------|
| <u>Callable Secured Convertible Promissory Notes:</u>                          | <u>DECEMBER 31,</u> |  |             |
|  | <u>2007</u>         |  | <u>2006</u> |
| Callable secured convertible promissory notes (more fully described in Note 4) | \$4,364,420         |  | \$2,983,616 |
|  |                     |  |             |
| Less portion included in convertible debt derivatives                          | (4,364,420)         |  | (2,983,616) |

|                                       |      |  |      |
|---------------------------------------|------|--|------|
|                                       |      |  |      |
| Long term portion of callable secured |      |  |      |
| convertible promissory notes          | \$ - |  | \$ - |

## ITRONICS INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

|  | <u>DECEMBER 31,</u> |  |             |
|--|---------------------|--|-------------|
|  | <u>2007</u>         |  | <u>2006</u> |
| <u>Loans from Stockholders/Related Transactions:</u> |                     |  |             |
| Advances from officer/stockholder. Due on demand,    |                     |  |             |
| with interest accruing at 12% per annum.             | \$143,025           |  | \$161,525   |
|  |                     |  |             |

| Long-term debt matures as follows: |                |              |  | CALLABLE     |                     |
|------------------------------------|----------------|--------------|--|--------------|---------------------|
|                                    |                |              |  | SECURED      |                     |
|                                    | UNRELATED      | CONVERTIBLE  |  | CONVERTIBLE  |                     |
| <u>YEAR</u>                        | <u>PARTIES</u> | <u>NOTES</u> |  | <u>NOTES</u> | <u>STOCKHOLDERS</u> |
| 2008                               | \$436,523      | \$ 3,497,838 |  | \$ 824,355   | \$ 143,025          |
| 2009                               | 3,690          | -            |  | 1,500,000    | -                   |
| 2010                               | 3,915          | -            |  | 2,040,065    | -                   |
| 2011                               | 4,153          | -            |  | -            | -                   |
| 2012                               | 4,406          | -            |  | -            | -                   |
| 2013-2023                          | 66,033         | -            |  | -            | -                   |

|  |           |  |              |  |            |
|--|-----------|--|--------------|--|------------|
|  |           |  |              |  |            |
|  | \$518,720 |  | \$ 3,497,838 |  | \$ 143,025 |
|  |           |  |              |  |            |

All of the convertible notes and accrued interest, totaling \$3,497,838, are in default. The Company is formulating a plan to seek extensions of these notes. No collection action has been taken by the note holders. When these notes came due in 2006, they were convertible into 22,229,551 common shares. If the Company is successful in negotiating extensions of these notes, the convertible options may be renewed and the eventual number of potential options could be significantly higher than the amount that expired.

The Company's mortgage loan on the manufacturing facility is in default due to delinquent property taxes totaling \$13,535. The lender is aware of the situation and has taken no collection action. As a result of the default, the entire principal balance, in the amount of \$418,456, is included in current liabilities.

A financing contract on equipment, with a balance of \$14,589, is in default and is included in current liabilities. The lender has referred the loan to an attorney, but no further action has been taken.

#### NOTE 4 Callable Secured Convertible Debt

Beginning in July 2005, the Company has arranged a series of callable secured convertible debt financings (Notes) with an accredited investment group totaling \$6,310,000. The Notes bear interest at rates ranging from 6% to 8% and

are due three year from issuance. In connection with these financings, the Company has issued warrants to acquire common stock in varying amounts and at varying exercise prices. During 2007 the Company signed Notes that added accrued interest totaling \$342,170 to the outstanding principal balance. These Notes bear interest at 2% and have a three year term. Following is a summary of the financings:

#### ITRONICS INC. AND SUBSIDIARIES

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

|             | ORIGINAL      | CONVERTED    | PRINCIPAL       | NUMBER OF     | WARRANT      |
|-------------|---------------|--------------|-----------------|---------------|--------------|
|             | PRINCIPAL     | TO           | BALANCE         | WARRANTS      | EXERCISE     |
| <u>DATE</u> | <u>AMOUNT</u> | <u>STOCK</u> | <u>12/31/07</u> | <u>ISSUED</u> | <u>PRICE</u> |
| July 2005   | \$1,250,000   | \$1,250,000  | \$ -            | 1,153,846     | \$0.15       |
| August 2005 | 1,000,000     | 175,645      | 824,355         | 923,077       | \$0.15       |

## Edgar Filing: ITRONICS INC - Form 10KSB

|                    |             |             |             |             |          |
|--------------------|-------------|-------------|-------------|-------------|----------|
| January 2006       | 500,000     | -           | 500,000     | 961,539     | \$0.15   |
| February 2006      | 500,000     | -           | 500,000     | 461,539     | \$0.15   |
| July 2006          | 500,000     | 500,000     | -           | 20,000,000  | \$0.05   |
| November 2006      | 500,000     | -           | 500,000     | 20,000,000  | \$0.04   |
| January 2007       | 500,000     | -           | 500,000     | 20,000,000  | \$0.01   |
| March 2007         | 500,000     | 362,106     | 137,894     | 20,000,000  | \$0.01   |
| June 2007          | 335,000     | -           | 335,000     | 10,000,000  | \$0.01   |
| August 2007        | 250,000     | -           | 250,000     | 20,000,000  | \$0.0014 |
| October 2007       | 275,000     | -           | 275,000     | 15,000,000  | \$0.004  |
| December 2007      | 200,000     | -           | 200,000     | 15,000,000  | \$0.001  |
|                    |             |             |             |             |          |
| Totals             | \$6,310,000 | \$2,287,751 | 4,022,249   | 143,500,001 |          |
|                    |             |             |             |             |          |
| Accrued interest   |             |             |             |             |          |
| added to principal |             |             | 342,171     |             |          |
|                    |             |             |             |             |          |
| Balance 12/31/07   |             |             | \$4,364,420 |             |          |
|                    |             |             |             |             |          |

The Notes are convertible into common shares at the lesser of \$0.10 or 35% of the market price of the Company's common stock, as defined. The Company may prepay the Notes at 150% of the outstanding principal and accrued interest balance, if sufficient authorized shares are available to convert all of the outstanding principal and accrued interest. Additionally, the Notes are secured by substantially all of the Company's assets. The Notes are further secured by 14,550,558 Company common shares owned by an officer/stockholder.

The Notes are potentially convertible into an unlimited number of common shares. Accordingly, the Company has accounted for the Notes under SFAS 133, EITF 00-19 and DIG's B38 and B39 which require the beneficial conversion features and the prepayment penalties of each of the Notes to be treated as embedded derivatives, to be recorded as a collective liability equal to the estimated fair value of the embedded derivatives. As of December 31, 2007 and 2006 the Notes were convertible into 6,450,658,596 and 586,181,548 common shares, respectively, and the conversion and prepayment (for 2006) features had estimated fair values of \$13,003,762 and \$4,876,175, respectively. As of December 31, 2007, the Company did not have enough authorized shares to allow conversion of all of the outstanding debt into stock. Consequently, the prepayment option was not available and no value for the prepayment feature was

included in the computation of the estimated fair value of the derivative for December 31, 2007.

In addition, all warrants and options that are exercisable during the period that the Notes are outstanding are required to be recorded as liabilities at their fair value. At December 31, 2007 and 2006 warrants and options to acquire a total of 156,729,001 and 58,599,501 common shares,

ITRONICS INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

respectively, were outstanding and had estimated fair values of \$231,224 and \$380,083, respectively.

The Company estimates the fair value of the embedded conversion and prepayment options of the callable secured convertible debt in a single pricing model with an embedded weighted average calculation. The assumptions used are to (1) determine the number of shares it would take to convert the debt under the terms of the agreements as of the balance sheet date; (2) estimate the future rate of debt conversions by the investors based on recent conversion history; (3) estimate the debt balance at specified dates, using 6 month intervals, based on the conversion rate determined in step 2; (4) value each of the components, including the conversions and the prepayment balances determined in step 3, using the Black-Scholes option pricing model; and (5) compute the estimated fair value of the combined derivatives by taking a weighted average of the values of the debt derivative and the prepayment options for the estimated prepayment dates based on estimated probability of occurrence of each event. Based on the Company's operating history and lack of cash, 90% of the weight was assigned to the option of not prepaying the debt for 2006. Steps 2 and 5 were applicable only to 2006, as the prepayment feature of the Notes was not available for 2007. Volatility rates ranged from 90% to 118% for 2007 and 87% to 109% for 2006. Risk free interest rates ranged from 2.76% to 5.07% for 2007 and 4.625% to 4.75% for 2006. Volatility is calculated each reporting period and the calculation involves matching data points of our common share market price to the length of the option period. Fluctuations in volatility between individual derivatives and between periods are primarily due to the length of the option period.

The Company estimates the fair value of warrants and options using the Black-Scholes option pricing model and assumes all warrants and options would be exercised on their respective expiration dates. Volatility and risk free interest rate ranges are included in the ranges listed above.

The following table is a summary of the transactions and adjustments that comprised the calculation of the estimated fair value of the derivatives from January 1, 2006 to December 31, 2007:

ITRONICS INC. AND SUBSIDIARIES  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
 DECEMBER 31, 2007 AND 2006

|                                      | Convertible       | Warrant          |
|--------------------------------------|-------------------|------------------|
|                                      | Debt              | And Option       |
|                                      | <u>Derivative</u> | <u>Liability</u> |
| Estimated fair value as of           |                   |                  |
| December 31, 2005                    | \$ 3,621,220      | \$ 134,212       |
| Additional borrowing in 2006         | 2,000,000         | -                |
| Accrued interest                     | 208,142           | -                |
| Warrants issued for services and     |                   |                  |
| expensed or capitalized in 2006      | -                 | 17,594           |
| Debt conversions into common shares  | (1,266,384)       | -                |
| Year to date adjustment to Estimated |                   |                  |

Edgar Filing: ITRONICS INC - Form 10KSB

|   |              |            |
|---|--------------|------------|
| Fair Value at December 31, 2006           | 313,197      | 228,277    |
|   |              |            |
| Estimated Fair Value at December 31, 2006 | 4,876,175    | 380,083    |
|   |              |            |
| Additional borrowing in 2007              | 2,060,000    | -          |
| Accrued interest                          | 134,554      | -          |
| Options issued for services and           |              |            |
| expensed or capitalized in 2006           |              | 7,337      |
| Debt conversions                          | (1,021,367)  | -          |
| Year to date adjustment to Estimated      |              |            |
| Fair Value at December 31, 2007           | 6,954,400    | (156,196)  |
|   |              |            |
| Estimated Fair Value at December 31, 2006 | \$13,003,762 | \$ 231,224 |

The fair value of the beneficial conversion option, prepayment penalties, warrants and options are estimated each reporting period with the change in fair value recorded as gain or loss on derivative instruments. As the Company's common stock is highly volatile, material gains or losses for the change in estimated fair value are likely to occur in future periods.

Following is a summary of the gains and (losses) on derivative instruments by reporting period for the years ended December 31, 2007 and 2006:

|                              | Year Ended    |              |
|------------------------------|---------------|--------------|
|                              | December 31,  |              |
|                              | <u>2007</u>   | <u>2006</u>  |
| Convertible debt derivative  | \$(6,954,400) | \$ (313,197) |
| Warrant and option liability | 156,196       | (228,277)    |
|                              |               |              |

|                          |               |             |
|--------------------------|---------------|-------------|
| Combined derivative Loss | \$(6,798,204) | \$(541,474) |
|--------------------------|---------------|-------------|

In connection with the above described financings, the Company entered into Registration Rights Agreements with the Noteholders that either require the Company to use its best efforts to file a registration statement within 120 days of funding or to file a registration statement within 10 days of written demand from the Noteholders. The 2005 Agreements required the Company to increase the authorized shares by October 31, 2005 or use its best efforts to do so. The Agreement specifies penalties of 2% per month for failing to register the shares timely and 3% per month for failing to increase the authorized shares. The Company registered 50 million shares in February 2006

## ITRONICS INC. AND SUBSIDIARIES

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

and increased the authorized shares in March 2006. Because it used its best efforts, the Company did not incur any penalties. The Company completed registrations of 75 million shares each in October 2006 and June 2007. After converting their debt into the 75 million common shares from the June 2007 registration, the Noteholders began utilizing Rule 144 to convert their debt into common shares as several of the Notes qualified for Rule 144 treatment since they were more than two years old. In February 2008 Rule 144 was revised to allow sale of shares after being held for six months. The holding period for debt instruments begins on the date of the investment due to the shortened time period, the Company anticipates that the Noteholders will utilize Rule 144 for future debt conversions and that no future registrations will be necessary.

In December 2007 the Company had issued substantially all of its authorized shares. A shareholder meeting to increase the authorized shares to 20 billion from 1 billion shares was scheduled for March 27, 2008. We did not receive enough votes to have a quorum, so the meeting was rescheduled to April 18, 2008. The Company anticipates that sufficient votes will be received to pass the proposal. Consequently, the Company believes it is using its best efforts to be in compliance with the terms of the various Registration Rights Agreements as of December 31, 2007, and therefore believes the probability of incurring any penalties is remote.

During 2007 the Noteholders converted a total of \$1,021,367 of the Notes into 546,758,396 common shares. During the period of February 15, 2006 to December 31, 2006, the Noteholders converted a total of \$1,266,384 of the Notes into 111,222,642 common shares.

#### NOTE 5 - Major Customers:

Fertilizer sales for the years ended December 31, 2007 and 2006 include \$1,643,256 and \$1,239,354, respectively, to one major customer, which represents 99% and 95%, respectively, of fertilizer sales for the years ended December 31, 2007 and 2006. These sales represented 71% and 67% of total GOLD n GRO Fertilizer segment sales for the years ended December 31, 2007 and 2006, respectively. Receivables from this major customer as of December 31, 2007 and 2006 amounted to \$1,809 and \$19,442, which represented 28% of GOLD n GRO fertilizer segment accounts receivable at December 31, 2007.

Silver sales for the years ended December 31, 2007 and 2006 include \$231,092 and \$258,089, respectively, which represents 73% and 62%, respectively, of silver sales for the years ended December 31, 2007 and 2006, to one major



customer in the precious metals refining industry. These sales represented 10% and 14% of the GOLD n GRO Fertilizer segment sales, for the years ended December 31, 2007 and 2006, respectively. Receivables from this major customer as of December 31, 2007 and 2006 amounted to \$-0- and \$11,387, respectively, which represented -0-% of GOLD n GRO fertilizer accounts receivable at December 31, 2007.

Technical services revenues for the years ended December 31, 2007 and 2006 were spread among several customers with relatively small amounts. Revenue from the largest single customer was \$11,722 and \$19,082 for 2007 and 2006,

ITRONICS INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

respectively. The Company's major technical services customers operate within the mining industry, both nationally and internationally. Due to the nature of the Company's operations, the major sources of revenues may change from year to year.

NOTE 6 - Income Taxes:

The following is a reconciliation of the federal statutory tax and tax rate to the Company's provision for taxes and its effective tax rate.

|   | <u>2007</u>   |               |  | <u>2006</u>   |               |
|---|---------------|---------------|--|---------------|---------------|
|   |               | PERCENT       |  |               | PERCENT       |
|   |               | OF            |  |               | OF            |
|   |               | PRE-TAX       |  |               | PRE-TAX       |
|   | <u>AMOUNT</u> | <u>INCOME</u> |  | <u>AMOUNT</u> | <u>INCOME</u> |
| Federal tax at statutory rate   | \$-           | - %           |  | \$-           | - %           |
| Temporary differences,<br>primarily bad debt and<br>compensation related expenses | -             | - %           |  | -             | - %           |
| Non-deductible expenses   | -             | - %           |  | -             | - %           |
| Utilization of NOL  | -             | - %           |  | -             | - %           |

Edgar Filing: ITRONICS INC - Form 10KSB

|                          |     |      |  |     |      |
|--------------------------|-----|------|--|-----|------|
|                          |     |      |  |     |      |
| Total Income Tax Expense | \$- | 0.0% |  | \$- | 0.0% |

The Company's consolidated net operating loss available for carry-forward to offset future taxable income and tax liabilities for income tax reporting purposes expire as follows:

|                                 | Net Operating |
|---------------------------------|---------------|
| <u>Year Ending December 31:</u> | <u>Loss</u>   |
| 2008                            | 113,253       |
| 2012                            | 322,525       |
| 2018                            | 377,944       |
| 2019                            | 1,605,954     |
| 2020                            | 3,254,375     |
| 2021                            | 2,947,351     |
| 2022                            | 2,496,744     |
| 2023                            | 2,286,436     |
| 2024                            | 2,337,832     |
| 2025                            | 2,841,914     |
| 2026                            | 2,603,264     |
| 2027                            | 2,909,883     |
|                                 |               |
|                                 | \$24,097,475  |
|                                 |               |

## ITRONICS INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

The Company's total deferred tax assets and related valuation allowances at December 31, 2007 and 2006 are as follows:

|                           | <u>2007</u>  |  | <u>2006</u>  |
|---------------------------|--------------|--|--------------|
| Total deferred tax assets | \$ 8,667,571 |  | \$ 7,650,008 |
| Less valuation allowance  | (8,667,571)  |  | (7,650,008)  |
|                           |              |  |              |
| Net deferred tax asset    | \$ -         |  | \$ -         |
|                           |              |  |              |

The estimated deferred tax assets and the related 100% valuation allowance increased \$1,017,563 between 2006 and 2007.

## NOTE 7 - Stock Option and Purchase Plans:

The following table summarizes warrant and option activity for the period January 1, 2006 through December 31, 2007:

|                                 | Convertible     |                     | Employee       | <u>Total</u>  |
|---------------------------------|-----------------|---------------------|----------------|---------------|
|                                 | <u>Warrants</u> | <u>Debt Options</u> | <u>Options</u> |               |
| Under option, December 31, 2005 | 27,313,260      | 134,823,379         | 6,108,000      | 168,244,639   |
| Granted                         | 41,496,924      | 584,810,362         | 226,000        | 626,533,286   |
| Exercised                       | (100,000)       | (111,222,642)       | -              | (111,322,642) |
| Expired                         | (10,110,683)    | (22,229,551)        | (12,000)       | (32,352,234)  |
| Under option, December 31,      | 58,599,501      | 586,181,548         | 6,322,000      | 651,103,049   |

Edgar Filing: ITRONICS INC - Form 10KSB

|                                 |             |               |           |               |
|---------------------------------|-------------|---------------|-----------|---------------|
| 2006                            |             |               |           |               |
| Granted                         | 100,000,000 | 6,411,235,444 | 252,000   | 6,511,487,444 |
| Exercised                       | -           | (546,758,396) | -         | (546,758,396) |
| Expired                         | (8,134,500) | -             | (310,000) | (8,444,500)   |
| Under option, December 31, 2007 | 150,465,001 | 6,450,658,596 | 6,264,000 | 6,607,387,597 |

The average price for all warrants and options granted and exercised was \$0.0009 for the year ended December 31, 2007 and \$0.0146 for the year ended December 31, 2006.

ITRONICS INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

The following table summarizes warrants and options outstanding as of December 31, 2007:

|          |
|----------|
| Weighted |
|----------|

Edgar Filing: ITRONICS INC - Form 10KSB

|                            | No. of        | Exercise     | Average         |
|----------------------------|---------------|--------------|-----------------|
| <u>Expiration Dates</u>    | <u>Shares</u> | <u>Price</u> | <u>Exercise</u> |
|                            |               |              | <u>Price</u>    |
| <u>Warrants:</u>           |               |              |                 |
| December 2014              | 15,000,000    | \$ 0.001     |                 |
| August 2014                | 20,000,000    | \$0.0014     |                 |
| October 2014               | 15,000,000    | \$ 0.004     |                 |
| January 2014 to June 2014  | 50,000,000    | \$ 0.010     |                 |
| November 2013              | 20,000,000    | \$ 0.040     |                 |
| July 2013                  | 20,000,000    | \$ 0.050     |                 |
| June 2010                  | 1,000,000     | \$ 0.100     |                 |
| July 2010 to February 2011 | 3,740,001     | \$0.150      |                 |
| January 2008 to June 2008  | 5,725,000     | \$0.225      |                 |

|                |             |  |           |
|----------------|-------------|--|-----------|
| Total Warrants | 150,465,001 |  | \$ 0.0289 |
|----------------|-------------|--|-----------|

|                                  | No. of        | Exercise     | Weighted        |
|----------------------------------|---------------|--------------|-----------------|
| <u>Convertible Debt Options:</u> | <u>Shares</u> | <u>Price</u> | <u>Average</u>  |
|                                  |               |              | <u>Exercise</u> |
|                                  |               |              | <u>Price</u>    |
| August 2008 to December 2010     | 6,450,658,596 | \$0.0007     | \$0.0007        |

| <u>Employee Options:</u>       |           |          |
|--------------------------------|-----------|----------|
| February 2008 to February 2017 | 447,000   | \$0.0150 |
| One year after employment ends | 1,600,000 | 0.150    |
|                                |           |          |

Edgar Filing: ITRONICS INC - Form 10KSB

|                                |           |       |
|--------------------------------|-----------|-------|
| May 2017 to October 2017       | 75,000    | 0.160 |
| January 2015 to August 2017    | 125,000   | 0.200 |
| One year after employment ends | 1,000,000 | 0.250 |
| One year after employment ends | 3,000,000 | 0.300 |
| October 2012 to October 2013   | 17,000    | 0.500 |

|                        |           |         |
|------------------------|-----------|---------|
| Total Employee Options | 6,264,000 | \$0.240 |
|------------------------|-----------|---------|

|                            |               |           |
|----------------------------|---------------|-----------|
| Total Warrants and Options | 6,607,387,597 | \$ 0.0015 |
|----------------------------|---------------|-----------|

The 6,450,658,596 convertible debt options listed above are related to the Notes discussed in Note 4. This debt is convertible into common stock at 35% of a calculated market price. Consequently, the number of shares and the conversion price can vary up or down materially, depending on the market price of the Company's stock.

ITRONICS INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

NOTE 8 Common Stock to be Issued:

The following summarizes stock transactions commencing prior to December 31, with stock issued or to be issued subsequent to that date:

|  | <u>2007</u>   |               | <u>2006</u>   |               |
|--|---------------|---------------|---------------|---------------|
|  | <u>Amount</u> | <u>Shares</u> | <u>Amount</u> | <u>Shares</u> |
|  |               |               |               |               |

Edgar Filing: ITRONICS INC - Form 10KSB

|                                |           |            |           |            |
|--------------------------------|-----------|------------|-----------|------------|
| Payment of salaries            | \$746,935 | 18,218,958 | \$529,725 | 7,620,625  |
| Payment of director fees       | 3,000     | 1,000,000  | 3,113     | 207,500    |
| Payment of interest, employees | 37,430    | 500,703    | 37,430    | 500,703    |
| Payment of debt conversion     | -         | -          | 13,600    | 2,500,000  |
|                                |           |            |           |            |
|                                | \$787,365 | 19,719,661 | \$583,868 | 10,828,828 |

The above salary amounts include both management and non-management employees. The management portion is discussed in detail in Note 11.

NOTE 9 - Accrued Expenses:

The following is the composition of accrued expenses as of December 31:

|                                 | <u>2007</u> |  | <u>2006</u> |
|---------------------------------|-------------|--|-------------|
|                                 |             |  |             |
| Accrued vacation                | \$103,445   |  | \$91,615    |
| Federal and state payroll taxes | 47,889      |  | 19,699      |
| Sales tax                       | 1,423       |  | 516         |
| Audit and annual meeting costs  | 119,500     |  | 95,000      |
|                                 |             |  |             |
|                                 | \$272,267   |  | \$206,830   |

NOTE 10 Other Comprehensive Income

The Company held marketable securities that were available for sale, which consisted 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 an Accumulated Unrealized Holding Loss of \$-0- at December 31, 2007 and 2006. The Company realized gross gains of \$7,718 on gross proceeds of \$106,218 and gross losses of \$3,983 on gross proceeds of \$35,870 during the twelve months ended December 31, 2007, and no gains were reclassified out of accumulated other comprehensive income into earnings. The Company realized no gross losses and gross gains of \$97,728 on gross

proceeds of \$229,374 during the twelve months ended December 31, 2006, and no gains were reclassified out of accumulated other comprehensive income into earnings. The table below illustrates the amount of unrealized holding gains and losses included in other comprehensive income, net of tax effects of \$0. The

## ITRONICS INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

reclassification adjustment represents unrealized holding gains and losses transferred into earnings as securities are sold. The Company held no marketable securities as of December 31, 2007 and 2006.

Following are the components of Other Comprehensive Income:

|                                   | Year Ended December 31, |             |
|-----------------------------------|-------------------------|-------------|
|                                   | <u>2007</u>             | <u>2006</u> |
|                                   |                         |             |
| Unrealized holding gains (losses) |                         |             |
| arising during the period         | \$ -                    | \$ -        |
|                                   |                         |             |
| Reclassification adjustment       | -                       | 39,889      |
|                                   |                         |             |
| Other Comprehensive Income        | \$ -                    | \$39,889    |

## NOTE 11 - Related Party Transactions:

Promissory notes are held by an officer/stockholder at December 31, 2007 and 2006 (see Note 3 for terms).

\$779,073 and \$796,200 of the accrued management salaries as of December 31, 2007 and 2006, respectively, is for salary in arrears due to several officer/stockholders and employee/stockholders. In addition, salary in arrears of \$746,800 and \$514,800 for 2007 and 2006, respectively, are included in stock to be issued at the respective year ends. These amounts represent the portion of salaries earned but unpaid that the officers/employees/stockholders have agreed to accept in the Company's common stock and have relinquished their right to receive cash. When the stock is eventually issued, it will be issued at the market price on the date of the respective agreements. The number of shares to be issued is 18,173,958 and 6,348,958 for 2007 and 2006, respectively. Issuance of the stock is pending sufficient cash available to pay the related federal withholding taxes. Interest expense at 12% per annum on salaries due officer and employee/stockholders amounted to \$168,146 and \$143,478, respectively, in 2007 and 2006.



Edgar Filing: ITRONICS INC - Form 10KSB

Interest expense on related party loans amounted to \$18,851 and \$19,383 for the years ended December 31, 2007 and 2006, respectively. Accrued interest on related party loans and accrued salaries totaled \$157,181 and \$87,211 at December 31, 2007 and 2006, respectively.

During 2003, WWI's lease of a vehicle utilized by Dr. Whitney was completed. Dr. Whitney purchased the vehicle by financing it through a commercial lender. The purchase price was \$21,741 and the monthly payment for four years is \$531. WWI is leasing the vehicle from Dr. Whitney by making the monthly payments to the commercial lender and acquired ownership of the vehicle when the loan was paid off in 2007.

For related party transactions subsequent to December 31, 2007, see Note 17.

ITRONICS INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

NOTE 12 - Lease Commitments and Rent Expense:

Operating Leases:

The Company leases its corporate office facility under a non-cancelable agreement which expires June 30, 2010. Monthly payments begin at \$5,324 and increase annually with the final year monthly payment at \$5,534.

A wholly owned subsidiary of the Company, IMI, leases storage facilities on a month-to-month basis and, therefore, no long-term binding contractual obligation exists with regards to minimum lease payments. The monthly rent payment is \$1,100.

Future minimum rental commitments at December 31, 2007, under these operating lease agreements are due as follows:

|      |           |
|------|-----------|
| 2008 | \$ 61,855 |
| 2009 | 63,062    |
| 2010 | 33,204    |
|      |           |
|      | \$158,121 |

Total rent expense included in the statements of operations for the years ended December 31, 2007 and 2006 is \$73,521 and \$74,370, respectively.

Capital Leases:

Prior to 2004 the Company had entered into numerous equipment leases, primarily for equipment at the manufacturing facility. The leases were generally for five years, had initial interest rates ranging from 6.7% to 26.3%, with the majority being in the 18% to 21% range, and generally had \$1 buyout options at the end of the lease terms. Substantially all of these leases have been renegotiated or been subject to litigation, as discussed in Note 16, such that the original payments terms are no longer applicable. The renegotiated leases now carry interest rates ranging from 6% to 9.25%.

All of the above described leases are secured by the equipment acquired or financed under the lease.

Future minimum lease commitments at December 31, 2007 are due as follows:

ITRONICS INC. AND SUBSIDIARIES  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
 DECEMBER 31, 2007 AND 2006

|      | Unrelated      |
|------|----------------|
|      | <u>Parties</u> |
| 2008 | \$513,667      |
| 2009 | 54,000         |
| 2010 | 32,625         |
| 2011 | 27,000         |
| 2012 | 9,000          |
|      |                |

|                                     |           |
|-------------------------------------|-----------|
|                                     | 636,292   |
| Less: amounts representing interest | (172,296) |
|                                     |           |
|                                     | \$463,996 |

## NOTE 13 - Business Segments:

The Company and its subsidiaries operate two business segments as identified in Note 1. The following defines business segment

activities:

GOLD n GRO Fertilizer: Photochemical recycling,

Silver recovery, GOLD n GRO

Fertilizer production and

Sales

Mining Technical Services: Mining industry services

The GOLD n GRO fertilizer segment operates principally in Northern Nevada and California. The primary source of revenue for this segment is from the pick-up and processing of photochemicals, recovery of silver therefrom, and sales of GOLD n GRO fertilizer products. The customer base is diverse and includes organizations in the photo-processing, printing, x-ray and medical fields. Fertilizer sales are concentrated in the same geographic markets and the customer base is principally in commercial markets, including specialty agriculture which includes vegetables, fruit and nut trees, and wine and table grapes, golf courses, and turf farms.

The mining technical services segment performs its services primarily out of the Company's Reno, Nevada offices, but its source of clients is not limited to organizations based locally; it has served both national and international clients in the past.

The Company measures segment performance based on net income or loss. At present there are no intercompany revenues. Costs benefiting both segments are incurred by both the Company and by Whitney & Whitney, Inc. Such costs are allocated to each segment based on the estimated benefits to the segment. General and administrative costs incurred by the Company that have no other rational basis for allocation are divided evenly between the segments. Cost allocation percentages are reviewed annually and are adjusted based on expected business conditions for the year.

## ITRONICS INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Edgar Filing: ITRONICS INC - Form 10KSB

DECEMBER 31, 2007 AND 2006

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

|                                  | <u>2007</u>   |  | <u>2006</u>   |
|----------------------------------|---------------|--|---------------|
| Revenues                         |               |  |               |
| GOLD n GRO Fertilizer            | \$2,315,141   |  | \$1,843,580   |
| Mining Technical Services        | 27,155        |  | 28,338        |
|                                  |               |  |               |
| Consolidated Revenues            | \$2,342,296   |  | \$1,871,918   |
|                                  |               |  |               |
| Cost of Revenues                 |               |  |               |
| GOLD n GRO Fertilizer            | \$2,184,143   |  | \$1,760,118   |
| Mining Technical Services        | 33,993        |  | 36,607        |
|                                  |               |  |               |
| Consolidated Cost of Revenues    | \$2,218,136   |  | \$1,796,725   |
|                                  |               |  |               |
| Gross Profit (Loss)              |               |  |               |
| GOLD n GRO Fertilizer            | \$130,998     |  | \$83,462      |
| Mining Technical Services        | (6,838)       |  | (8,269)       |
|                                  |               |  |               |
| Consolidated Gross Profit (Loss) | \$124,160     |  | \$75,193      |
|                                  |               |  |               |
| Operating Income (Loss)          |               |  |               |
| GOLD n GRO Fertilizer            | \$(2,199,386) |  | \$(1,682,464) |
| Mining Technical Services        | (744,042)     |  | (542,042)     |

Edgar Filing: ITRONICS INC - Form 10KSB

|   |                |  |               |
|---|----------------|--|---------------|
|   |                |  |               |
| Consolidated Operating Income (Loss)        | \$(2,943,428)  |  | \$(2,224,506) |
| Other Income (Expense)                      |                |  |               |
| GOLD n GRO Fertilizer                       | \$(7,681,820)  |  | \$(1,688,339) |
| Mining Technical Services                   | 142,724        |  | 102,960       |
|   |                |  |               |
| Consolidated Other Income (Expense)         | \$(7,539,096)  |  | \$(1,585,379) |
|   |                |  |               |
| Net Income (Loss)                           |                |  |               |
| GOLD n GRO Fertilizer                       | \$(9,881,206)  |  | \$(3,370,803) |
| Mining Technical Services                   | (601,318)      |  | (439,082)     |
|   |                |  |               |
| Consolidated Net Income (Loss) before taxes | \$(10,482,524) |  | \$(3,809,885) |

ITRONICS INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

Edgar Filing: ITRONICS INC - Form 10KSB

| Other segment information:                                 | <u>2007</u> |  | <u>2006</u> |
|--|-------------|--|-------------|
| Capital expenditures by business segment:                  |             |  |             |
| GOLD n GRO Fertilizer                                      | \$ 14,913   |  | \$159,383   |
| Mining Technical Services                                  | 103,333     |  | 2,252       |
|  |             |  |             |
| Consolidated Capital Expenditures                          | \$118,246   |  | \$161,635   |
|  |             |  |             |
| Depreciation and amortization expense by business segment: |             |  |             |
| GOLD n GRO Fertilizer                                      |             |  |             |
| Depreciation   | \$171,129   |  | \$177,754   |
| Amortization   | 29,205      |  | 41,370      |
|  |             |  |             |
|  | 200,334     |  | 219,124     |
| Mining Technical Services                                  |             |  |             |
| Depreciation   | 6,656       |  | 4,247       |
| Amortization   | 2,472       |  | 4,646       |
|  |             |  |             |
|  | 9,128       |  | 8,893       |
|  |             |  |             |
| Consolidated Depreciation and Amortization                 | \$209,462   |  | \$228,017   |

General and administrative expenses of \$282,134 and \$293,191 incurred by Itronics Inc. were equally divided between the two segments for 2007 and 2006, respectively.

ITRONICS INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
DECEMBER 31, 2007 AND 2006

Edgar Filing: ITRONICS INC - Form 10KSB

Identifiable assets by business segment (net of accumulated depreciation, accumulated amortization, and allowance for doubtful accounts):

|   | 2007                                    |  | 2006                                    |  |
|---|---|--|---|--|
|   | PHOTO-<br>CHEMICAL<br><u>FERTILIZER</u> | MINING<br>TECHNICAL<br><u>SERVICES</u> | PHOTO-<br>CHEMICAL<br><u>FERTILIZER</u> | MINING<br>TECHNICAL<br><u>SERVICES</u> |
| <u>ASSET DESCRIPTION</u>                                  |   |  |   |  |
| Current Assets  |   |  |   |  |
| Cash  | \$95,930                                | \$ 973                                 | \$ -                                    | \$ -                                   |
| Accounts receivable, net                                  | 7,243                                   | 10,318                                 | 35,102                                  | 1,391                                  |
| Inventories   | 889,996                                 | -                                      | 548,399                                 | -                                      |
| Prepaid expenses  | 40,318                                  | 4,452                                  | 55,061                                  | 2,913                                  |
|   |   |  |   |  |
|   | 1,033,487                               | 15,743                                 | 638,562                                 | 4,304                                  |
| Property and Equipment, net                               |   |  |   |  |
| Land  | 215,000                                 | -                                      | 215,000                                 | -                                      |
| Building and improvements                                 | 1,074,124                               | -                                      | 961,473                                 | -                                      |
| Construction in progress,<br>manufacturing facility       | 97,110                                  | -                                      | 234,347                                 | -                                      |
| Equipment and furniture                                   | 1,280,083                               | 20,403                                 | 1,232,796                               | 14,455                                 |
| Vehicles  | 5,305                                   | 2,175                                  | 10,391                                  | -                                      |
| Equipment under capital lease-<br>equipment and furniture | 97,557                                  | 60,565                                 | 203,044                                 | 65,509                                 |
| Equipment under capital lease-<br>Vehicles                | -                                       | -                                      | -                                       | 6,523                                  |
|   |   |  |   |  |



Edgar Filing: ITRONICS INC - Form 10KSB

|                    |             |           |  |             |          |
|--------------------|-------------|-----------|--|-------------|----------|
|                    | 2,769,179   | 83,143    |  | 2,857,051   | 86,487   |
|                    |             |           |  |             |          |
| Other Assets, net  |             |           |  |             |          |
| Intangibles        | 76,500      | -         |  | 76,500      |          |
| Deposits           | 4,427       | 3,483     |  | 4,427       | 3,483    |
| Deferred loan fees | 27,391      | -         |  | 30,646      | -        |
|                    |             |           |  |             |          |
|                    | 108,318     | 3,483     |  | 111,573     | 3,483    |
|                    |             |           |  |             |          |
|                    | \$3,910,984 | \$102,369 |  | \$3,607,186 | \$94,274 |

ITRONICS INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

## Reconciliation of segment assets to consolidated assets:

|                                 | <u>2007</u>  |  | <u>2006</u>  |
|---------------------------------|--------------|--|--------------|
| Total Assets:                   |              |  |              |
| GOLD n GRO Fertilizer           | \$3,910,984  |  | \$3,607,186  |
| Mining Technical Services       | 102,369      |  | 94,274       |
| Total Segment Assets            | 4,013,353    |  | 3,701,460    |
| Itronics Inc. assets            | 28,787,327   |  | 27,028,313   |
| Less: inter-company elimination | (28,444,812) |  | (26,464,234) |
| Consolidated Assets             | \$4,355,868  |  | \$4,265,539  |

## NOTE 14 - Going Concern:

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 \$10,482,524 during the year ended December 31, 2007, a negative working capital of \$18,842,148, and a stockholders' deficit balance of \$15,663,973 as of December 31, 2007. 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.

In order to solve the Company's liquidity problems, management has implemented a plan of financing its operations through the private placements of common shares, convertible debt, conversion of debt to common shares, and payment of consulting and other labor services with common shares. The Company obtained financing of \$2.06 million and \$2 million in 2007 and 2006, respectively, through the issuance of callable secured convertible debt. During the first quarter of 2008, the Company obtained \$310,000 from the issuance of callable secured convertible debt. For the immediate future, the Company plans to obtain additional debt financing from this investor group. For the longer term, the Company is in discussions with several investment groups regarding debt and equity financing. We must receive approval, which shall not be unreasonably withheld, from the current investor group prior to receiving any funding from a new investor. The current investor group also has the right of first refusal to provide funds under the same terms as any proposed new funding.

In addition to continuing the above described efforts, development of the technology necessary to manufacture fertilizer from photochemicals has been completed. In March 1998 the Company's subsidiary, Itronics Metallurgical, Inc., signed a definitive manufacturing and distribution agreement with Western

ITRONICS INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

Farm Services, Inc. (WFS). The agreement gives WFS the exclusive license and right to manufacture and market the GOLD n GRO line of fertilizer products in the states of Arizona, California, Hawaii, Idaho, Oregon and Washington. The agreement is for five years, with five year renewal options. In March 2003, the companies entered the second five year term of the agreement and in March 2008, the companies entered into the third five year term.

Subsequent to December 31, 2007, the Company received its EPA registration for the GOLD n GRO Guardian deer repellent fertilizer. The Company believes this development will assist in the efforts to obtain the long term financing discussed above.

NOTE 15 - Off-Balance Sheet Risks and Concentration of Credit Risk:

The Company occasionally maintains bank deposits in excess of federally insured limits. The Company's risk is managed by maintaining its accounts in one of the top five largest banks in the country.

As described in Note 5, substantially all the Company's fertilizer sales are concentrated with one major fertilizer distribution customer. In addition, substantially all of those sales are in California, primarily in the Central Valley. Having the majority of such sales concentrated in one region makes the Company's sales more vulnerable to variability caused by weather patterns or economic downturns than if sales were geographically diversified. The Company's plan is to expand geographically to mitigate such effects in the future. At any point in time, a significant portion of the Company's accounts receivable is concentrated with this fertilizer distribution company. This concentration of credit risk is somewhat mitigated due to the fact that the distribution company is one of the largest fertilizer distribution companies in the country.

Increase or decrease in photochemical recycling service and silver extraction revenues has a direct relationship with federal, state, and local regulations and enforcement of said regulations. Fertilizer revenues are impacted by crop cycles, seasonal variations, and weather patterns.

The ability to recognize a net profit from silver recovery sales is based on the fair market value of silver (London five day average) at the time the photochemicals are obtained versus the fair market value of silver when recovered silver is sold. Most customers are given an 80% silver credit against recycling services based on the content of silver in the photochemicals. If the fair market value of silver declines, our ability to recover our costs could be impacted.

NOTE 16 - Legal Proceedings and Contingencies

As of December 31, 2007 we have accrued for liabilities, including interest, of \$544,965 which relate to various lawsuits and claims for the collection of the funds due. These include 8 leases totaling \$366,358 (reflected in Capital Lease Obligations) plus \$62,435 in additional interest

ITRONICS INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

(reflected in Accrued Interest) and one trade payable totaling \$85,801 (reflected in Accounts Payable) plus \$30,371 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 three cases that are seeking \$251,522, which we believe are probable. The creditors have received judgments in these cases, but have taken no further collection action. The Company will continue to accrue interest until these cases are settled or paid in full.

The Company has two cases, that originally sought \$171,853, that we deem to have a remote possibility of incurring an additional unrecorded loss. The Company has negotiated payment agreements on these cases and, as of December 31, 2007, the recorded liability was \$163,128. We are delinquent in our payments under the respective settlement agreements, but we are in contact with the lender's legal representative and no collection action has been taken.

In addition to the above leases that are subject to litigation, there are four leases, with a recorded liability of \$189,110, that are in default. 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.

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

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 above. Other than as described above, we are currently not aware of any litigation pending or threatened for any reason other than collection of funds due and already recorded nor are we 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.

NOTE 17 - Subsequent Events:

In March 2008 the Company arranged additional callable secured convertible debt financing in the amount of \$310,000 each from the same investor group as discussed in Note 4 above. The notes have a three year term and have interest rates of 8% per annum. The Company received net proceeds of \$300,000 from the financing and issued a total of 10,000,000 seven year warrants at an exercise price of \$0.0001 per share.

ITEM 14.PRINCIPAL ACCOUNTANT FEES AND SERVICES

Following is a summary of the aggregate fees billed for professional service by the Company's principal accountant.

|                    | <u>2007</u> |  | <u>2006</u> |
|--------------------|-------------|--|-------------|
| Audit fees         | \$102,253   |  | \$134,608   |
| Audit related fees | -           |  | -           |
| Tax fees           | -           |  | -           |
| All other fees     | -           |  | -           |
|                    |             |  |             |
| Total              | \$102,253   |  | \$134,608   |

The Company does not have an audit committee and consequently the entire Board of Directors serves in that capacity. The Board's pre-approval policy regarding professional services provided by the Company's principal accountant is to pre-approve the engagement of the principal accountant for the performance of all professional services. The policy does provide a waiver of pre-approval in the event that such services, in the aggregate, will be less than 5% of the audit fee, such services are not recognized as non-audit fees at the time of the engagement, and pre-approval is obtained from a designated member of the Board prior to the engagement. Until such time as an audit committee is appointed, the designated individual is the Principal Executive Officer, currently the President of the Company.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

Date: April , 2008 By: /S/ JOHN W. WHITNEY

John W. Whitney

President, Treasurer and Director

(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.

Date: April, 2008 By: /S/ JOHN W. WHITNEY

John W. Whitney

President, Treasurer and Director

(Principal Executive and Financial  
Officer)

Date: April, 2008 By: /S/ MICHAEL C. HORSLEY

Michael C. Horsley

Controller

(Principal Accounting Officer)

Date: April, 2008 By: /S/ HOWLAND S. GREEN

Howland S. Green

Director

EXHIBIT 14

ITRONICS INC.

CODE OF BUSINESS CONDUCT AND ETHICS

March 25, 2004

The Board of Directors of Itronics Inc. has adopted the following Code of Business Conduct and Ethics (the Code). This Code is applicable to all directors, officers, and other senior management personnel (Management) of Itronics Inc. and its subsidiaries. The purpose of this Code is to promote the highest standards of ethical conduct of business.

Management will practice honesty, integrity and good faith in every aspect of dealing with other Company personnel, shareholders, the public, customers, suppliers and government authorities. All persons are to be treated with dignity and respect.

Management will respect and obey all applicable federal, state, and local laws and regulations. Management will not only follow the letter of the law, but the spirit as well.



## Edgar Filing: ITRONICS INC - Form 10KSB

Management will do its utmost to avoid real or perceived conflicts of interest in our business dealings. Apparent conflicts of interest are to be disclosed to the appropriate person promptly.

Management will prepare reports and other disclosures to be disseminated to the public or to be filed with the Securities and Exchange Commission or other governmental authorities in a full, fair, accurate, timely, and understandable manner. The needs of our investors and the investing public will always be the foremost priority in preparing such reports or disclosures.

Trading of the Company's securities will be conducted under all applicable laws and rules of the Securities and Exchange Commission. Management will not take unfair advantage of any publicly undisclosed information it may have regarding the operations of the Company and its subsidiaries.

Each member of Management is responsible to conduct him or herself in accordance with this Code. Any observed violations are to be reported to the appropriate person promptly. Violations of this Code subject the individual to disciplinary action and possible termination.

Management includes directors, the principal executive officer, the principal accounting officer or controller, or employees performing similar functions.

The appropriate person to discuss any questions about this Code, observed violations of the Code, or potential conflicts of interest is the principal executive officer, which is currently the President of the Company.

ITRONICS INC. AND SUBSIDIARIES

SIGNIFICANT SUBSIDIARIES

STATE OF NAMES UNDER WHICH

NAME INCORPORATION THEY DO BUSINESS

Whitney & Whitney, Inc. Nevada Same

Itronics Metallurgical, Inc Nevada Same

Itronics California, Inc. California Same

Nevada Hydrometallurgical Project

(A Partnership) Nevada Same

American Hydromet

(A Joint Venture) Nevada Same

Itronics Gold n Minerals, Inc. Nevada Same