

Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

REUNION INDUSTRIES INC  
Form 10-Q  
November 14, 2001

UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549-1004

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2001

OR

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

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

Commission File Number 33-64325

REUNION INDUSTRIES, INC.

(Exact name of Registrant as specified in its charter)

DELAWARE

06-1439715

(State of Incorporation)

(I.R.S. Employer Identification No.)

11 STANWIX STREET, SUITE 1400  
PITTSBURGH, PENNSYLVANIA 15222

(Address of principal executive offices, including zip code)

(412) 281-2111

(Registrant's telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

At October 31, 2001, 15,590,619 shares of common stock, par value \$.01 per share, were outstanding.

Page 1 of 39 pages.

# Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

## FORWARD-LOOKING STATEMENTS AND ASSOCIATED RISKS

This report contains certain forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act which are intended to be covered by the safe harbors created thereby. The forward-looking statements contained in this report are enclosed in brackets [] for ease of identification. Note that all forward-looking statements involve risks and uncertainties, including, without limitation, factors which could cause the future results and shareholder values to differ materially from those expressed in the forward-looking statements. Although the Company believes that the assumptions underlying the forward-looking statements contained in this report are reasonable, any of the assumptions could be inaccurate and, therefore, there can be no assurances that the forward-looking statements included or incorporated by reference in this report will prove to be accurate. In light of the significant uncertainties inherent in the forward-looking statements included or incorporated by reference herein, the inclusion of such information should not be regarded as a representation by the Company or any other person that the Company's objectives and plans will be achieved. In addition, the Company does not intend to, and is not obligated to, update these forward-looking statements after filing and distribution of this report, even if new information, future events or other circumstances have made them incorrect or misleading as of any future date.

- 2 -

## REUNION INDUSTRIES, INC.

### INDEX

	Page No.
	-----
PART I. FINANCIAL INFORMATION	
Item 1. Financial Statements	
Condensed Consolidated Balance Sheet at September 30, 2001 (unaudited) and December 31, 2000	4
Condensed Consolidated Statement of Income (Loss) and Comprehensive Income (Loss) for the three and nine months ended September 30, 2001 and 2000 (unaudited)	5
Condensed Consolidated Statement of Cash Flows for the nine months ended September 30, 2001 and 2000 (unaudited)	7
Notes to Condensed Consolidated Financial Statements	8
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	21
Item 3. Quantitative and Qualitative Disclosures About Market Risk	34
PART II. OTHER INFORMATION	
Item 1. Legal Proceedings	35

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

Item 3. Defaults Upon Senior Securities	37
Item 5. Other Information	38
Item 6. Exhibits and Reports on Form 8-K	
(b) Reports on Form 8-K	39
 SIGNATURES	 39

- 3 -

### PART I. FINANCIAL INFORMATION

#### Item 1. Financial Statements

REUNION INDUSTRIES, INC.  
CONDENSED CONSOLIDATED BALANCE SHEET  
AT SEPTEMBER 30, 2001 AND DECEMBER 31, 2000  
(in thousands)

	At September 30, 2001 ----- (unaudited)	At December 31, 2000* -----
<b>ASSETS:</b>		
Cash and cash equivalents	\$ 1,284	\$ 1,826
Receivables, net	33,640	31,777
Advances to employees	213	233
Inventories, net	17,549	21,781
Other current assets	2,243	3,307
	-----	-----
Total current assets	54,929	58,924
Property, plant and equipment, net	30,631	31,166
Due from related parties	1,586	3,950
Goodwill, net	26,496	18,837
Deferred tax assets, net	12,678	12,678
Net assets of discontinued operations	220	9
Other assets, net	3,657	4,391
	-----	-----
Total assets	\$130,197 =====	\$129,955 =====
 <b>LIABILITIES AND STOCKHOLDERS' EQUITY:</b>		
Debt in default	\$ 70,252	\$ -
Revolving credit facility	-	19,367
Current maturities of debt	73	4,061
Trade payables	18,759	21,662
Due to related parties	798	224
Accrued interest on debt in default	1,675	-
Other current liabilities	9,562	15,133
	-----	-----
Total current liabilities	101,119	60,447
Long-term debt	4,848	42,656
Long-term debt - related parties	4,615	4,015
Other liabilities	55	1,278
	-----	-----

Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

Total liabilities	110,637	108,396
Commitments and contingent liabilities	-	-
Stockholders' equity	19,560	21,559
	-----	-----
Total liabilities and stockholders' equity	\$130,197	\$129,955
	=====	=====

See accompanying notes to condensed consolidated financial statements.

\* - Certain amounts have been reclassified for comparative purposes.

- 4 -

REUNION INDUSTRIES, INC.  
CONDENSED CONSOLIDATED STATEMENT OF INCOME (LOSS)  
AND COMPREHENSIVE INCOME (LOSS)  
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2001 AND 2000  
(in thousands, except per share information) (unaudited)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2001	2000	2001	2000
	-----	-----	-----	-----
Operating revenue:				
Metals Group	\$ 30,019	\$ 35,384	\$100,374	\$106,634
Plastics Group	8,713	13,308	31,698	31,955
	-----	-----	-----	-----
Total sales	38,732	48,692	132,072	138,589
	-----	-----	-----	-----
Cost of sales:				
Metals Group	26,617	28,327	81,844	84,909
Plastics Group	7,866	11,456	27,423	27,089
	-----	-----	-----	-----
Total cost of sales	34,483	39,783	109,267	111,998
	-----	-----	-----	-----
Gross profit	4,249	8,909	22,805	26,591
Selling, general & administrative	5,419	6,223	17,591	16,713
Other (income) expense, net	604	(4,931)	1,803	(4,310)
	-----	-----	-----	-----
Operating profit (loss)	(1,774)	7,617	3,411	14,188
Interest expense, net	2,253	2,886	7,005	7,930
Equity in loss of continuing operations of affiliate	-	-	-	296
	-----	-----	-----	-----
Income (loss) from continuing operations before income taxes	(4,027)	4,731	(3,594)	5,962
Provision for (benefit from) income taxes	(1,307)	20	(1,135)	(322)
	-----	-----	-----	-----
Income (loss) from continuing operations	(2,720)	4,711	(2,459)	6,284
Loss from discontinued operations, net of tax of \$-0-	-	(337)	-	(767)
	-----	-----	-----	-----
Income (loss) before extraordinary items	(2,720)	4,374	(2,459)	5,517
	-----	-----	-----	-----
Extraordinary items, net of tax of \$-0-:				

Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

Write-off of deferred financing costs	-	(80)	-	(1,581)
Equity in loss of extraordinary item of affiliate	-	-	-	(271)
	-----	-----	-----	-----
Loss from extraordinary items	-	(80)	-	(1,852)
	-----	-----	-----	-----
Net income (loss) and comprehensive income (loss)	(2,720)	4,294	(2,459)	3,665
Preferred stock dividend accretions	-	-	-	(95)
	-----	-----	-----	-----
Income (loss) applicable to common stockholders	\$ (2,720)	\$ 4,294	\$ (2,459)	\$ 3,570
	=====	=====	=====	=====

- 5 -

REUNION INDUSTRIES, INC.  
CONDENSED CONSOLIDATED STATEMENT OF INCOME (LOSS)  
AND COMPREHENSIVE INCOME (LOSS)  
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2001 AND 2000 (continued)  
(in thousands, except per share information) (unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2001	2000	2001	2000
	-----	-----	-----	-----
Basic earnings (loss) per common share:				
Continuing operations	\$ (0.17)	\$ 0.31	\$ (0.16)	\$ 0.49
Discontinued operations	-	(0.02)	-	(0.06)
Extraordinary items	-	(0.01)	-	(0.15)
	-----	-----	-----	-----
Income (loss) per common share	\$ (0.17)	\$ 0.28	\$ (0.16)	\$ 0.28
	=====	=====	=====	=====
Weighted average shares outstanding	15,587	15,236	15,585	12,564
	=====	=====	=====	=====
Diluted earnings (loss) per common share:				
Continuing operations	\$ (0.17)	\$ 0.31	\$ (0.16)	\$ 0.49
Discontinued operations	-	(0.02)	-	(0.06)
Extraordinary items	-	(0.01)	-	(0.15)
	-----	-----	-----	-----
Income (loss) per common share	\$ (0.17)	\$ 0.28	\$ (0.16)	\$ 0.28
	=====	=====	=====	=====
Weighted average shares outstanding	15,636	15,387	15,651	12,624
	=====	=====	=====	=====

See accompanying notes to condensed consolidated financial statements.

- 6 -

REUNION INDUSTRIES, INC.  
CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS  
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2001 AND 2000  
(in thousands)  
(unaudited)

Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

	Nine Months Ended	
	September 30,	
	2001	2000
	-----	-----
Cash provided by (used in) operating activities	\$ (2,907)	\$ 2,086
	-----	-----
Cash flow from investing activities:		
Proceeds from sale of business	-	9,990
Capital expenditures	(2,517)	(3,511)
Acquisition of NPSAC common stock	(10)	-
Acquisition of Kingway common stock	-	(100)
Cash acquired in merger	-	2,666
	-----	-----
Cash provided by (used in) investing activities	(2,527)	9,045
	-----	-----
Cash flow from financing activities:		
Proceeds from issuance of debt	-	30,800
Net change in revolving credit facilities	7,991	23,495
Borrowings	534	-
Repayments of debt	(4,305)	(62,323)
Repayments of debt - related party	-	(1,076)
Payments of deferred financing costs and closing fees	-	(1,404)
	-----	-----
Cash provided by (used in) financing activities	4,220	(10,508)
	-----	-----
Net increase (decrease) in cash and cash equivalents	(1,214)	623
Change in cash of discontinued operations	672	(49)
Cash and cash equivalents, beginning of year	1,826	252
	-----	-----
Cash and cash equivalents, end of period	\$ 1,284	\$ 826
	=====	=====

See accompanying notes to condensed consolidated financial statements.

- 7 -

REUNION INDUSTRIES, INC.  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 2001

NOTE 1: CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair statement of the results of operations have been included. The results of operations for the three and nine month periods ended September 30, 2001 are not necessarily indicative of the results of operations for the full year. When reading the financial information contained in this Quarterly Report, reference should be made to the financial statements, schedules and notes contained in Reunion's Annual Report on Form 10-K for the year ended December 31, 2000.

Recent Accounting Pronouncements

The Financial Accounting Standards Board issued Statements of Financial Accounting Standards (SFAS) No. 141, "Business Combinations." This statement

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

eliminates the pooling-of-interest method for business combinations and changes the criteria for recognizing intangible assets apart from goodwill. This statement is effective for purchases completed after June 30, 2001. The Company has not engaged in any acquisitions since June 30, 2001. Acquisitions prior to June 30, 2001 were recorded as purchases in accordance with Accounting Principles Board Opinion No. 16.

The Financial Accounting Standards Board issued SFAS No. 142, "Goodwill and Other Intangible Assets." This statement eliminates the amortization of goodwill and indefinite lived intangible assets and requires such assets be reviewed for impairment at least annually. This statement is effective for goodwill and intangible assets acquired prior to July 1, 2001 upon adoption, which is required for fiscal years beginning after December 15, 2001. The Company is beginning the process of evaluating the adoption and effects of this statement on the Company. During the three and nine month periods ended September 30, 2001, the Company recorded goodwill amortization of \$0.5 million and \$1.4 million, respectively. The effect on basic earnings per share had the Company adopted the non-amortization of goodwill provisions of SFAS 142 at the beginning of 2001 would be a \$0.02 per share increase for the three months ended and a \$0.07 per share increase for the nine months ended September 30, 2001.

The Financial Accounting Standards Board issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." This statement supersedes SFAS 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of" but retains many of its fundamental provisions. SFAS 144 also supersedes Accounting Principles Board Opinion No. 30, "Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions" but retains its provision to separately report discontinued operations and extends that reporting to a component of an entity, as defined therein, that either has been disposed of or is classified as held for sale, thus broadening the presentation of discontinued operations to include more disposal transactions. This statement is effective for fiscal years beginning after December 15, 2001 but early adoption is permitted. As discussed in note 2, the Company's management is in the early stages of developing a corporate-wide restructuring

- 8 -

plan, the elements of which will include asset dispositions and facility shut-downs. If the restructuring plan is approved by the Company's Board of Directors in the fourth quarter of 2001, early adoption of SFAS 144 could have a significant impact on the classification of amounts related to the restructuring plan included in its consolidated financial statements at and for the year ended December 31, 2001.

### NOTE 2: RECENT DEVELOPMENTS AND OTHER MATTERS

#### Restructuring and Other Actions

As the result of downturns in several of the markets served by the Company and the resulting decrease in the Company's ability to absorb costs, management of the Company has determined to develop a plan to restructure its continuing businesses and dispose of or shut-down certain non-strategic businesses. These actions will be designed to improve productivity and operating performance.

#### 2001 Covenant Compliance

For the quarter ended March 31, 2001 and for each fiscal quarter thereafter in 2001, the Bank of America (BOA) financing and security agreement

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

required the Company to maintain a minimum fixed charge coverage ratio of 1.25:1 and maximum funded debt to EBITDA ratios of 3.75:1, 3.50:1, 3.25:1 and 3.00:1.

In April 2001, the Company entered into a letter agreement with Bank of America whereby, as long as the Company maintained both a fixed charge coverage ratio of at least 1.00:1 and had a funded debt to EBITDA ratio of no more than 4.50:1 as of the September 30, 2001 and December 31, 2001 calculation dates, and as long as the Company was in compliance on all other covenants, the Bank of America would not accelerate any of its loans.

For the quarter ended September 30, 2001, the Company's fixed charge coverage ratio was 0.79:1 and the funded debt to EBITDA ratio was 5.61:1. As a result, the Company is in default under its BOA financing and security agreement.

The Company and Bank of America entered into various amendments to the BOA financing and security agreement during 2000. The December 12, 2000 amendment required the Company to maintain a minimum availability under the revolving credit facility of \$1.5 million. Through the second quarter of 2001, the Company had complied with this requirement. However, due to the downturn in several of the markets served by the Company during the third quarter of 2001 and the resulting decrease in the quality of the Company's borrowing base, ineligible receivables and inventory increased. Based on the borrowing base formulas as set forth in the BOA financing and security agreement, this increase in ineligibles resulted in a decrease in borrowing availability under the revolving credit facility and the Company's inability to maintain a minimum availability of \$1.5 million. As a result, the Company is in default under its BOA financing and security agreement.

Semi-Annual Interest on 13% Senior Notes due November 1, 2001

The Company was unable to fund its \$1.616 million semi-annual interest payment on its 13% senior notes as it had insufficient funds available under its revolving credit facility. Failure to make the November 1 interest payment is a default under the indenture which supports the 13% Senior Notes. Under the terms of the indenture, the Company has thirty days to cure the default.

- 9 -

Acquisition of NPS Acquisition Corp. and Note Payable Assumption

On January 17, 2001, the Company acquired NPS Acquisition Corp. (NPSAC) (f/k/a Naptech Pressure Systems) from Charles E. Bradley, Sr. (Mr. Bradley), the Company's chairman of the board and chief executive officer. NPSAC is based in Clearfield, Utah and manufactures seamless steel pressure vessels, an existing Metals Group segment.

The purchase price was \$10,000 plus the non-cash assumption of \$10.3 million of NPSAC's liabilities, including a 15% per annum \$6.9 million note payable to Shaw Group, the former owner of Naptech Pressure Systems and \$0.6 million of notes payable to Stanwich Financial Services Corp., a related party. Simultaneously with the acquisition, Reunion paid Shaw Group \$2.0 million of the note payable in cash from funds available under its revolving credit facility with Bank of America (BOA). The remainder of the note payable of \$4.9 million was then restructured to include quarterly principal payments of \$0.6 million for eight quarters which began on February 28, 2001. Reunion made the first two payments from funds available under its revolving credit facility. The Company was unable to fund the third payment due August 31, 2001 as it had insufficient funds available under its revolving credit facility. The note is unsecured and subordinate to the BOA term loan and

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

revolving credit facilities.

The estimated fair value of assets acquired included approximately \$1.4 million of cash, receivables, inventories and other current assets, approximately \$0.3 million of fixed assets and \$1.3 million of deferred tax assets which are fully reserved by a valuation allowance. The purchase price in excess of net assets acquired of \$8.6 million was recorded as goodwill and is being amortized over 15 years. NPSAC's deferred tax assets are comprised primarily of net operating losses.

### Repayment of \$120,000 of 13% Senior Notes

Chatwins Group was required to make sinking fund payments to redeem \$12.5 million principal amount of the senior notes on May 1 in each of 2000 through 2003 at face value plus accrued interest and to offer to purchase \$25 million of the senior notes on June 1, 2000 at face value plus accrued interest. In February 2000, Chatwins Group solicited the holders of the \$49,975,000 of 13% senior notes outstanding asking them to waive their right to participate in the June 1, 2000 \$25.0 million purchase offer, of which \$47,450,000 agreed to waive such right resulting in a maximum purchase offer obligation on June 1, 2000 of \$2,525,000.

As such, on June 1, 2000 Reunion made the required offer to purchase \$2,525,000 of senior notes, of which holders of only \$120,000 of senior notes tendered. However, the \$25.0 million of 13% senior notes repaid from the merger proceeds was applied against Reunion's obligations for sinking fund payments and the purchase offer as follows (in thousands):

	May 1, 2000	June 1, 2000	May 1, 2001	Total
	-----	-----	-----	-----
Sinking fund payment or purchase offer obligation	\$ 12,500	\$ 120	\$ 12,500	\$ 25,120
\$25.0 million applied to obligations	(12,500)	(120)	(12,380)	(25,000)
	-----	-----	-----	-----
Maximum required payment	\$ -	\$ -	\$ 120	\$ 120
	=====	=====	=====	=====

- 10 -

Therefore, \$120,000 principal amount of 13% senior notes was repaid by the Company on May 1, 2001 from funds available under its revolving credit facility. Of the remaining \$24.855 million of senior notes, \$12.5 million is scheduled to be repaid in May 2002 and \$12.355 million is scheduled to be repaid in May 2003.

### Solicitation of Consent of Senior Noteholders

The Company is required to make sinking fund payments on its \$24.855 million of senior notes of \$12.5 million on May 1, 2002 and \$12.355 million on May 1, 2003. On September 4, 2001, the Company solicited the consent of its senior noteholders to extend the sinking fund payment dates by two years. The solicitation expired on November 2, 2001. As part of the solicitation, the Company reserved the right to terminate it if holders of less than \$22.0 million principal amount of senior notes consented. The Company has exercised its right to terminate the solicitation.

### Additional Shares of Reunion Common Stock

In the merger, Reunion issued 9,500,000 shares of common stock to holders of Chatwins Group's common stock. The merger agreement also provided that up

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

to an additional 500,000 shares of Reunion common stock would be issued to former Chatwins Group common stockholders if the former Chatwins Group businesses and the acquired Kingway business achieve specified performance levels in 2000. A determination of the number of shares to be issued was made by the board of directors at its meeting held on May 15, 2001. Such additional shares totaled 348,995 and were issued on May 29, 2001. The closing price of Reunion's common stock on that date was \$1.30 per share. The issuance of the additional shares was recorded as a merger purchase price adjustment to goodwill.

### Payment of \$680,000 Industrial Revenue Development Bonds

Upon the sale of its domestic grating operations in September 1999, the Company retained an obligation for a \$680,000 note payable due May 1, 2001 related to an industrial development revenue bond issue by Orem City, Utah. This note payable was repaid in May 2001 from funds available under the Company's revolving credit facility.

- 11 -

### NOTE 3: INVENTORIES

Inventories are comprised of the following (in thousands):

	At September 30, 2001 ----- (unaudited)	At December 31, 2000 -----
Metals Group:		
Raw material	\$ 4,647	\$ 5,933
Work-in-process	3,764	4,295
Finished goods	5,108	7,214
	-----	-----
Gross inventories	13,519	17,442
Less: LIFO reserves	80	80
	-----	-----
Metals Group inventories	13,599	17,522
	-----	-----
Plastics Group:		
Raw material	2,489	2,584
Work-in-process	235	323
Finished goods	1,226	1,352
	-----	-----
Plastics Group inventories	3,950	4,259
	-----	-----
Inventories	\$ 17,549 =====	\$ 21,781 =====

### NOTE 4: DEBT IN DEFAULT AND LONG-TERM DEBT

Debt in default consists of the following (in thousands):

	At September 30, 2001 ----- (unaudited)
13% senior notes (net of discount of \$5)	\$ 24,850
BOA revolving credit facility	27,358
BOA term loan A due March 16, 2007	16,993
BOA capital expenditure facility	1,051
	-----
Total debt in default	\$ 70,252

Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

=====

Long-term debt consists of the following (in thousands):

	At September 30, 2001	At December 31, 2000
	-----	-----
	(unaudited)	
13% senior notes (net of discount of \$5)	\$ -	\$ 24,961
BOA term loan A due March 16, 2007	-	19,757
BOA capital expenditure facility	-	640
Note payable due February 28, 2003	3,645	-
Other	1,276	1,359
Other - related parties	4,615	4,015
	-----	-----
Total long-term debt	9,536	50,732
Current maturities	(73)	(4,061)
	-----	-----
Total long-term debt, less current maturities	\$ 9,463	\$ 46,671
	=====	=====

- 12 -

NOTE 5: STOCKHOLDERS' EQUITY AND EARNINGS PER SHARE

The following represents a reconciliation of the change in stockholders' equity for the nine month period ended September 30, 2001 (in thousands):

	Par Value of Common Stock	Capital in Excess of Par Value	Accum- ulated Deficit	Total
	-----	-----	-----	-----
At January 1, 2001	\$152	\$24,608	\$ (3,201)	\$ 21,559
Activity (unaudited):				
Net loss	-	-	(2,459)	(2,459)
Issuance of common stock (note 2)	3	451	-	454
Exercise of options	1	5	-	6
	-----	-----	-----	-----
At September 30, 2001	\$156	\$25,064	\$ (5,660)	\$ 19,560
	=====	=====	=====	=====

The computations of basic and diluted earnings per common share (EPS) for the three and nine month periods ended September 30, 2001 and 2000 are as follows (in thousands, except per share amounts) (unaudited):

	Income (Loss)	Shares	EPS
	-----	-----	-----
Three months ended September 30, 2001:			
Net loss, weighted average shares outstanding and basic EPS	\$ (2,720)	15,587	\$ (0.17)
			=====
Dilutive effect of stock options		49	
	-----	-----	
Net loss, weighted average shares outstanding and diluted EPS	\$ (2,720)	15,636	\$ (0.17)
	=====	=====	=====

Three months ended September 30, 2000:  
Net income, weighted average shares

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

outstanding and basic EPS	\$ 4,294	15,236	\$ 0.28
			=====
Dilutive effect of stock options		151	
		-----	
Net income, weighted average shares outstanding and diluted EPS	\$ 4,294	15,387	\$ 0.28
	=====	=====	=====

Nine months ended September 30, 2001:

Net loss, weighted average shares outstanding and basic EPS	\$ (2,459)	15,585	\$ (0.16)
			=====
Dilutive effect of stock options		66	
		-----	
Net income, weighted average shares outstanding and diluted EPS	\$ (2,459)	15,651	\$ (0.16)
	=====	=====	=====

- 13 -

Nine months ended September 30, 2000:

Net income	\$ 3,665		
Less: Preferred stock dividend accretions	(95)		
	-----		
Income applicable to common stockholders, weighted average shares outstanding and basic EPS	3,570	12,564	\$ 0.28
			=====
Dilutive effect of stock options		60	
		-----	
Income applicable to common stockholders, weighted average shares outstanding and diluted EPS	\$ 3,570	12,624	\$ 0.28
	=====	=====	=====

At September 30, 2001, the Company's stock options outstanding totaled 1,093,500, of which 270,000 during the nine month period and 280,000 during the three month period ended September 30, 2001 were at exercise prices below the average market price of the underlying security. Such options include a dilutive component of 49,174 shares for the 2001 third quarter and 65,419 shares for the 2001 year-to-date period. The remainder were at exercise prices equal to or above the average market price of the underlying security.

### NOTE 6: COMMITMENTS AND CONTINGENT LIABILITIES

#### Legal Proceedings

The Company and its subsidiaries are defendants in a number of lawsuits and administrative proceedings, which have arisen in the ordinary course of business of the Company and its subsidiaries. The Company believes that any material liability which can result from any of such lawsuits or proceedings has been properly reserved for in the Company's consolidated financial statements or is covered by indemnification in favor of the Company or its subsidiaries, and therefore the outcome of these lawsuits or proceedings will not have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

In June 1993, the U.S. Customs Service (Customs) made a demand on Chatwins Group's former industrial rubber distribution division for \$612,948 in marking duties pursuant to 19 U.S.C. Sec. 1592. The duties are claimed on importations of "unmarked" hose products from 1982 to 1986. Following

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

Chatwins Group's initial response raising various arguments in defense, including expired statute of limitations, Customs responded in January 1997 by reducing its demand to \$370,968 and reiterating that demand in October 1997. Chatwins Group restated its position and continues to decline payment of the claim. Should the claim not be resolved, Customs threatens suit in the International Courts of Claims. The Company continues to believe, based on consultation with counsel, that there are facts which raise a number of procedural and substantive defenses to this claim, which will be vigorously defended. There is no applicable insurance coverage.

In December 1999, a stockholder of Reunion filed a purported class-action lawsuit in Delaware Chancery Court alleging, among other things, that Reunion's public stockholders would be unfairly diluted in the merger with Chatwins Group. The lawsuit sought to prevent completion of the merger and, the merger having been completed, seeks rescission of the merger or awarding of damages. The lawsuit is in the initial stages of discovery. Reunion intends to vigorously contest the suit.

- 14 -

The Company has been named as a defendant in fifteen consolidated lawsuits filed in December 2000 or early 2001 in the Superior Court for Los Angeles County, California, three of which are purported class actions asserted on behalf of approximately 200 payees. The plaintiffs in these suits except one are structured settlement payees to whom Stanwich Financial Services Corp. (SFSC) is indebted. The Company and SFSC are related parties.

In addition to the Company, there are numerous defendants in these suits, including SFSC, Mr. Bradley, the sole shareholder of SFSC's parent, several major financial institutions and certain others. All of these suits arise out of the inability of SFSC to make structured settlement payments when due. Pursuant to the court's order, plaintiffs in the purported class actions and plaintiffs in the individual cases actions filed a model complaint. Except for the class allegations, the two model complaints are identical. The plaintiffs seek compensatory and punitive damages, restoration of certain alleged trust assets, restitution and attorneys' fees and costs.

The plaintiffs in one of the suits are former owners of a predecessor of SFSC and current operators of a competing structured settlement business. These plaintiffs claim that their business and reputations have been damaged by SFSC's structured settlement defaults, seek damages for unfair competition and purport to sue on behalf of the payees.

The plaintiffs allege that the Company borrowed funds from SFSC and has not repaid these loans. The plaintiffs' theories of liability against the Company are that it is the alter ego of SFSC and Mr. Bradley and that the Company received fraudulent transfers of SFSC's assets. The plaintiffs also assert direct claims against the Company for inducing breach of contract and aiding and abetting an alleged breach of fiduciary duty by SFSC.

On May 25, 2001, SFSC filed a chapter 11 bankruptcy petition in the U.S. Bankruptcy Court for the District of Connecticut. SFSC filed an adversary proceeding in the bankruptcy case against the plaintiffs seeking a declaration that the structured settlement trust assets are the property of the bankruptcy estate. On July 16, 2001, the bankruptcy court granted a temporary restraining order enjoining the plaintiffs from prosecuting their claims against the Company, SFSC, Mr. Bradley and others. As a result of this restraining order of the bankruptcy court, the Company entered a standstill agreement with the plaintiffs on August 22, 2001. Pursuant to the standstill agreement, and the stipulation of the parties to the SFSC bankruptcy case, the plaintiffs agreed to take no further action to prosecute any claim in the litigation against the Company, Mr. Bradley and others to recover any

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

structured settlement trust assets or any derivative claims or claims based on allegations of alter ego, fraudulent transfer or conversion. The plaintiffs did not agree to waive or release their direct personal claims against the Company for damages, but the plaintiffs agreed to cease and desist the prosecution of those claims until no earlier than sixty days following service of written notice to the Company stating that they have elected to unilaterally terminate the standstill agreement.

Plaintiffs filed second amended model complaints in the class actions and individual cases on August 24, 2001. Both model complaints allege causes of action against the Company for interference with contract and aiding and abetting breach of fiduciary duty. However, pursuant to the standstill agreement, the plaintiffs are taking no action to prosecute these claims against the Company at this time.

Certain of the financial institution defendants have asserted cross-complaints against the Company for implied and express indemnity and contribution and negligence. The Company denies the allegations of the plaintiffs and the cross-complainant financial institutions and intends to vigorously defend against these actions and cross-actions.

- 15 -

The Company has been named in approximately 195 separate asbestos suits filed since January 1, 2001 by two plaintiffs' law firms in Wayne County, Michigan. The claims allege that cranes from the Company's crane manufacturing location in Alliance, OH were present in various parts of McLouth Steel Mill in Wayne County, Michigan and that those cranes contained asbestos to which plaintiffs were exposed over a 40 year span. As of the date of this report, counsel for the Company has filed an answer to each complaint denying liability by the Company and asserting all alternative defenses permitted under the Court's Case Management Order. Counsel for the Company has negotiated dismissal of 95 cases without any cost to the Company.

The Company denies that it manufactured any products containing asbestos or otherwise knew or should have known that any component part manufacturers provided products containing asbestos. The Company intends to vigorously defend against these lawsuits.

On July 10, 2001, a lawsuit that alleges personal injury from asbestos exposure was filed in the Superior Court for San Francisco County in California against greater than fifty defendants, including Oneida Rostone Corporation (ORC), pre-merger Reunion's Plastics subsidiary and the Company's Plastics Group. In October 2001, Allen-Bradley Company, a former owner of the Rostone business of ORC, agreed to defend and indemnify Reunion in this lawsuit pursuant to a contractual obligation to do so.

### Environmental Compliance

Various U.S. federal, state and local laws and regulations including, without limitation, laws and regulations concerning the containment and disposal of hazardous waste, oil field waste and other waste materials, the use of storage tanks, the use of insecticides and fungicides and the use of underground injection wells directly or indirectly affect the Company's operations. In addition, environmental laws and regulations typically impose "strict liability" upon the Company for certain environmental damages. Accordingly, in some situations, the Company could be liable for clean up costs even if the situation resulted from previous conduct of the Company that was lawful at the time or from improper conduct of, or conditions caused by, previous property owners, lessees or other persons not associated with the Company or events outside the control of the Company. Such clean up costs or costs associated with changes in environmental laws and regulations could be

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

substantial and could have a materially adverse effect on the Company's consolidated financial position, results of operations or cash flows.

Except as described in the following paragraphs, the Company believes it is currently in material compliance with existing environmental protection laws and regulations and is not involved in any significant remediation activities or administrative or judicial proceedings arising under federal, state or local environmental protection laws and regulations. In addition to management personnel who are responsible for monitoring environmental compliance and arranging for remedial actions that may be required, the Company has also employed outside consultants from time to time to advise and assist the Company's environmental compliance efforts. Except as described in the following paragraphs, the Company has not recorded any accruals for environmental costs.

In February 1996, Reunion was informed by a contracted environmental services consulting firm that soil and ground water contamination exists at its Lafayette, Indiana site. Since then, the Company has expended \$299,000 of remediation costs and accrued an additional \$60,000.

- 16 -

In connection with the sale of its former oil and gas operations, pre-merger Reunion retained certain oil and gas properties in Louisiana because of litigation concerning environmental matters. The Company is in the process of environmental remediation under a plan approved by the Louisiana Department of Natural Resources Office of Conservation (LDNROC). The Company has recorded an accrual for its proportionate share of the remaining estimated costs to remediate the site based on plans and estimates developed by the environmental consultants hired by the Company. During 1999, the Company conducted remediation work on the property. The Company paid \$172,000 of the total cost of \$300,000. Regulatory hearings were held in January 2000 and 2001 to consider the adequacy of the remediation conducted to date. In August 2001, LDNROC issued its order for the Company to complete the soil remediation under the plan approved in 1999 and to perform additional testing to determine to what extent groundwater contamination might exist. The Company's environmental consultant is in the process of updating the estimate of the costs to comply with this order, [but the Company does not believe that the cost of future remediation will exceed the amount accrued]. No remediation was performed in 2000 or to date in 2001 pending the decision. However, the Company has paid \$202,000 for its share of legal and consulting services in connection with the hearings. At September 30, 2001, the balance accrued for these remediation costs is approximately \$1,116,000. Owners of a portion of the property have objected to the Company's cleanup methodology and have filed suit to require additional procedures. The Company is contesting this litigation, and believes its proposed methodology is well within accepted industry practice for remediation efforts of a similar nature. No accrual has been made for costs of any alternative cleanup methodology which might be imposed as a result of the litigation.

### NOTE 7: SEGMENT DISCLOSURES

The Company owns and operates a diverse group of industrial manufacturing operations that design and manufacture highly engineered, high-quality products for specific customer requirements, such as large-diameter seamless pressure vessels, hydraulic and pneumatic cylinders, precision plastic components, heavy-duty cranes and materials handling systems. The Company's customers include original equipment manufacturers and end-users in a variety of industries, such as transportation, power generation, chemicals, metals, home electronics, office equipment and consumer goods. The Company's business units are organized into two major operating groups:

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

The Metals Group designs, manufactures and markets a broad range of fabricated and machined industrial metal parts and products, including bridge structures and cranes, materials handling systems, seamless pressure vessels, cylinders and leaf springs. The Metals Group serves over 5,000 customers, including original equipment manufacturers and end-users.

The Plastics Group manufactures precision molded plastic parts and provides engineered plastics services to more than 500 original equipment manufacturers.

Prior to the third quarter of 2001, the Company considered these groups to be its reportable segments for financial reporting purposes. Due to the downturns in the markets for several of the Company's Metals Group products and the resulting significant variation in product line gross margins, management reevaluated the definition of its segments and has concluded that, except for the Plastics Group, which will continue to be reported as a single segment, former Metals Group product lines are now considered to be segments for financial reporting purposes.

- 17 -

The following represents the disaggregation of financial data by segment (000's) (unaudited):

	Net Sales	EBITDA(1)	Capital Spending	Total Assets(2)
	-----	-----	-----	-----
Three months ended and at September 30, 2001:				
Metals Group:				
Bridges and cranes	\$ 3,247	\$ (2,109)	\$ 194	\$ 14,720
Materials handling systems	13,827	1,672	140	16,845
Seamless pressure vessels	8,042	1,431	121	19,958
Cylinders	4,246	(285)	-	11,549
Leaf springs	657	(34)	-	1,576
	-----	-----	-----	-----
Subtotal Metals Group	30,019	675	455	64,648
Plastics Group	8,713	223	200	23,265
Corporate and other	-	(857)	1	42,064
Discontinued operations	-	-	-	220
	-----	-----	-----	-----
Totals	\$ 38,732	41	\$ 656	\$130,197
	=====	-----	=====	=====
Depreciation and amortization(3)		(1,815)		
Interest expense		(2,253)		
		-----		
Loss from continuing operations before income taxes		\$ (4,027)		
		=====		
Three months ended September 30, 2000 and at December 31, 2000:				
Metals Group:				
Bridges and cranes	\$ 5,802	\$ (745)	\$ 958	\$ 16,157
Materials handling systems	14,128	2,265	216	16,426
Seamless pressure vessels	7,723	1,876	19	21,320
Cylinders	6,938	920	22	14,152
Leaf springs	793	44	1	1,783
	-----	-----	-----	-----
Subtotal Metals Group	35,384	4,360	1,216	69,838

Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

Plastics Group	13,308	884	406	23,485
Corporate and other(4)	-	4,187	3	36,623
Discontinued operations	-	-	72	9
	-----	-----	-----	-----
Totals	\$ 48,692	9,431	\$ 1,697	\$129,955
	=====		=====	=====
Depreciation and amortization(3)		(1,814)		
Interest expense		(2,886)		
		-----		
Income from continuing operations before income taxes		\$ 4,731		
		=====		

- 18 -

	Net Sales	EBITDA(1)	Capital Spending
	-----	-----	-----
Nine months ended September 30, 2001:			
Metals Group:			
Bridges and cranes	\$ 12,625	\$ (2,648)	\$ 797
Materials handling systems	38,999	5,499	580
Seamless pressure vessels	30,695	7,136	240
Cylinders	15,776	204	-
Leaf springs	2,279	(32)	14
	-----	-----	-----
Subtotal Metals Group	100,374	10,159	1,631
Plastics Group	31,698	1,543	878
Corporate and other	-	(2,824)	8
	-----	-----	-----
Totals	\$132,072	8,878	\$ 2,517
	=====		=====
Depreciation and amortization(3)		(5,467)	
Interest expense		(7,005)	
		-----	
Loss from continuing operations before income taxes		\$ (3,594)	
		=====	
Nine months ended September 30, 2000:			
Metals Group:			
Bridges and cranes	\$ 18,657	\$ (1,280)	\$ 1,369
Materials handling systems	38,614	5,873	385
Seamless pressure vessels	22,661	5,634	230
Cylinders	23,838	3,463	48
Leaf springs	2,864	280	28
	-----	-----	-----
Subtotal Metals Group	106,634	13,970	2,060
Plastics Group	31,955	2,428	1,086
Corporate and other(4)	-	2,560	36
Discontinued operations	-	-	329
	-----	-----	-----
Totals	\$138,589	18,958	\$ 3,511
	=====		=====
Depreciation and amortization(3)		(4,770)	
Interest expense		(7,930)	
Equity in loss of continuing operations of affiliate		(296)	

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

Income from continuing operations	-----
before income taxes	\$ 5,962
	=====

- 19 -

(1) EBITDA (earnings before interest, taxes, depreciation and amortization) is the primary measure used by management in assessing performance.

(2) Corporate and other total assets at September 30, 2001 and December 31, 2000 are primarily comprised of goodwill of \$23.5 million and \$15.7 million, respectively, and deferred tax assets of \$12.7 million at each date.

(3) Excludes amortization of debt issuance expenses of \$60,000 and \$469,000 for the three month periods ended September 30, 2001 and 2000, respectively, and \$408,000 and \$1,126,000 for the nine month periods ended September 30, 2001 and 2000, respectively, which are included in interest expense.

(4) Corporate and other EBITDA for the three and nine month periods ended September 30, 2000 include a \$4.9 million gain on the sale of the Company's Irish plastics line of business.

### NOTE 8: DISCONTINUED OPERATIONS

In October 2000, the Company sold substantially all of its wine grape agricultural operations and real estate holdings and classified and began accounting for the agricultural operations as discontinued operations.

During 1999, Chatwins Group's management adopted plans to exit the grating manufacturing business and oil and gas business through the disposition of all of its grating and oil and gas related assets. Upon adoption of the plans, Chatwins Group classified and began accounting for such businesses as discontinued operations.

At September 30, 2001 and December 31, 2000, the assets and liabilities of discontinued operations are comprised primarily of the assets and liabilities of the discontinued wine grape agricultural business. The liabilities of discontinued operations at December 31, 2000 also included a \$680,000 note payable due May 1, 2001 related to an industrial development revenue bond issue by Orem City, Utah, retained by the Company upon the sale of its domestic grating operations. This note payable was repaid in May 2001. The assets and liabilities have been separately classified on the balance sheet as net assets of discontinued operations.

For 2001, there are no results from discontinued operations. For 2000, results of discontinued operations relate to the Company's discontinued wine grape agricultural operations. Summarized results of discontinued operations for the three and nine month periods ended September 30, 2000 follow (in thousands):

	3-Mos.	9-Mos.
	-----	-----
Net sales	\$ 462	\$ 1,609
Loss before taxes	(157)	(513)

The above results of discontinued operations include actual and allocated interest expense totaling \$352,000 and \$760,000 for the three and nine month periods ended September 30, 2000, respectively.

- 20 -

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

### PART I. FINANCIAL INFORMATION

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

##### GENERAL

The Company owns and operates a diverse group of industrial manufacturing operations that design and manufacture highly engineered, high-quality products for specific customer requirements, such as large-diameter seamless pressure vessels, hydraulic and pneumatic cylinders, precision plastic components, heavy-duty cranes, bridge structures and materials handling systems. The Company's customers include original equipment manufacturers and end-users in a variety of industries, such as transportation, power generation, chemicals, metals, home electronics, office equipment and consumer goods. The Company's business units are organized into two operating groups:

The Metals Group designs, manufactures and markets a broad range of fabricated and machined industrial metal parts and products, including bridge structures and cranes, materials handling systems, seamless pressure vessels, cylinders and leaf springs. The Metals Group serves over 5,000 customers, including original equipment manufacturers and end-users.

The Plastics Group manufactures precision molded plastic parts and provides engineered plastics services to more than 500 original equipment manufacturers.

Prior to the third quarter of 2001, the Company considered these groups to be its reportable segments for financial reporting purposes. Due to the downturns in the markets for several of the Company's Metals Group product lines and the resulting significant variation in product line gross margins, management reevaluated the definition of its segments and has concluded that, except for the Plastics Group, which will continue to be reported as a single segment, former Metals Group product lines are now considered to be segments for financial reporting purposes.

##### RECENT DEVELOPMENTS AND OTHER MATTERS

###### Restructuring and Other Actions

As the result of downturns in several of the markets served by the Company and the resulting decrease in the Company's ability to absorb costs, management of the Company has determined to develop a plan to restructure its continuing businesses and dispose of or shut-down certain non-strategic businesses. These actions will be designed to improve productivity and operating performance.

[Development of the plan and its approval by the Company's board of directors is anticipated to be completed by the end of 2001. Once approved, management of the Company expects to record a charge for restructuring costs including employee separation costs, facility shut-down and rationalization costs and asset writedowns.] At this time, a reasonably dependable estimate of the total amount of the restructuring charge does not exist. [However, management anticipates that the charge will have a significant impact on the Company's results of operations for the year and quarter ended December 31, 2001.]

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

For the quarter ended March 31, 2001 and for each fiscal quarter thereafter in 2001, the Bank of America (BOA) financing and security agreement required the Company to maintain a minimum fixed charge coverage ratio of 1.25:1 and maximum funded debt to EBITDA ratios of 3.75:1, 3.50:1, 3.25:1 and 3.00:1.

In April 2001, the Company entered into a letter agreement with Bank of America whereby, as long as the Company maintained both a fixed charge coverage ratio of at least 1.00:1 and had a funded debt to EBITDA ratio of no more than 4.50:1 as of the September 30, 2001 and December 31, 2001 calculation dates, and as long as the Company was in compliance on all other covenants, the Bank of America would not accelerate any of its loans.

Due to the rate and level of the downturns in several of the markets served by the Company and the resulting decrease in the Company's ability to absorb costs, cost cutting and capital expenditure restriction measures taken by management during the third quarter of 2001 were not enough to achieve ratio compliance. For the quarter ended September 30, 2001, the Company's fixed charge coverage ratio was 0.79:1 and the funded debt to EBITDA ratio was 5.61:1. As a result, the Company is in default under its BOA Financing and Security Agreement.

The Company and Bank of America entered into various amendments to the BOA financing and security agreement during 2000. The December 12, 2000 amendment required the Company to maintain a minimum availability under the revolving credit facility of \$1.5 million. Through the second quarter of 2001, the Company had complied with this requirement. However, due to the downturn in several of the markets served by the Company during the third quarter of 2001 and the resulting decrease in the quality of the Company's borrowing base, ineligible receivables and inventory increased. Based on the borrowing base formulas as set forth in the BOA financing and security agreement, this increase in ineligibles resulted in a decrease in borrowing availability under the revolving credit facility and the Company's inability to maintain a minimum availability of \$1.5 million. As a result, the Company is in default under its BOA financing and security agreement.

[The Company is seeking to renegotiate or obtain waivers of its financial and minimum availability covenants. Although management believes it is unlikely, in the event that the Company is not able to successfully renegotiate its covenants or obtain the necessary waivers, the lenders have various remedies available to them including, but not limited to, acceleration of all amounts outstanding under the term and revolving credit facilities and a liquidation of their collateral.]

Semi-Annual Interest on 13% Senior Notes due November 1, 2001

The Company was unable to fund its \$1.616 million semi-annual interest payment on its 13% senior notes as it had insufficient funds available under its revolving credit facility. Failure to make the November 1 interest payment is a default under the indenture which supports the 13% senior notes. Under the terms of the indenture, the Company has thirty days to cure the default.

Management of the Company has been in contact with certain of the Note Holders and holders representing approximately ninety percent of the principal amount of senior notes outstanding have expressed their support of the Company. [Management of the Company is continuing to work with its secured lenders as well as other alternative financing sources in an effort to pay the \$1.616 million interest by November 30. Management of the Company currently

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

believes that it will be able to obtain the necessary funds. However, there can be no assurance that management will be successful in its efforts.]

### Acquisition of NPS Acquisition Corp. and Note Payable Assumption

On January 17, 2001, the Company acquired NPS Acquisition Corp. (f/k/a Naptech Pressure Systems) from Charles E. Bradley, Sr. (Mr. Bradley), the Company's chairman of the board and chief executive officer. NPSAC is based in Clearfield, Utah and manufactures seamless steel pressure vessels, an existing Metals Group segment.

The purchase price was \$10,000 plus the non-cash assumption of \$10.3 million of NPSAC's liabilities, including a 15% per annum \$6.9 million note payable to Shaw Group, the former owner of Naptech Pressure Systems and \$0.6 million of notes payable to Stanwich Financial Services Corp., a related party. Simultaneously with the acquisition, Reunion paid Shaw Group \$2.0 million of the note payable in cash from funds available under its revolving credit facility with Bank of America (BOA). The remainder of the note payable of \$4.9 million was then restructured to include quarterly principal payments of \$0.6 million for eight quarters which began on February 28, 2001. Reunion made the first two payments from funds available under its revolving credit facility. The Company was unable to fund the third payment due August 31, 2001 as it had insufficient funds available under its revolving credit facility. The note is unsecured and subordinate to the BOA term loan and revolving credit facilities.

The estimated fair value of assets acquired included approximately \$1.4 million of cash, receivables, inventories and other current assets, approximately \$0.3 million of fixed assets and \$1.3 million of deferred tax assets which are fully reserved by a valuation allowance. The purchase price in excess of net assets acquired of \$8.6 million was recorded as goodwill and is being amortized over 15 years. NPSAC's deferred tax assets are comprised primarily of net operating losses.

### Repayment of \$120,000 of 13% Senior Notes

Chatwins Group was required to make sinking fund payments to redeem \$12.5 million principal amount of the senior notes on May 1 in each of 2000 through 2003 at face value plus accrued interest and to offer to purchase \$25 million of the senior notes on June 1, 2000 at face value plus accrued interest. In February 2000, Chatwins Group solicited the holders of the \$49,975,000 of 13% senior notes outstanding asking them to waive their right to participate in the June 1, 2000 \$25.0 million purchase offer, of which \$47,450,000 agreed to waive such right resulting in a maximum purchase offer obligation on June 1, 2000 of \$2,525,000.

As such, on June 1, 2000 Reunion made the required offer to purchase \$2,525,000 of senior notes, of which holders of only \$120,000 of senior notes tendered. However, the \$25.0 million of 13% senior notes repaid from the merger proceeds was applied against Reunion's obligations for sinking fund payments and the purchase offer as follows (in thousands):

	May 1, 2000	June 1, 2000	May 1, 2001	Total
	-----	-----	-----	-----
Sinking fund payment or purchase offer obligation	\$ 12,500	\$ 120	\$ 12,500	\$ 25,120
\$25.0 million applied to obligations	(12,500)	(120)	(12,380)	(25,000)
	-----	-----	-----	-----
Maximum required payment	\$ -	\$ -	\$ 120	\$ 120
	=====	=====	=====	=====

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

- 23 -

Therefore, \$120,000 principal amount of 13% senior notes was repaid by the Company on May 1, 2001 from funds available under its revolving credit facility.

Of the remaining \$24.855 million of senior notes, \$12.5 million is scheduled to be repaid in May 2002 and \$12.355 million is scheduled to be repaid in May 2003. [Management does not expect to have the internally generated liquidity necessary to fund the May 1, 2002 sinking fund payment and is in the process of investigating various refinancing and repayment scenarios. Such scenarios involve not only mezzanine or additional term debt, which could potentially include warrants, but also involve other considerations such as a sale of assets. If the Company is unable to make its May 2002 sinking fund payment, the Company will be in default under the indenture for the senior notes which could result in the acceleration of all amounts due under the senior notes, including all principal and accrued but unpaid interest.]

### Solicitation of Consent of Senior Noteholders

The Company is required to make sinking fund payments on its \$24.855 million of senior notes of \$12.5 million on May 1, 2002 and \$12.355 million on May 1, 2003. On September 4, 2001, the Company solicited the consent of its senior noteholders to extend the sinking fund payment dates by two years. The solicitation expired on November 2, 2001. As part of the solicitation, the Company reserved the right to terminate it if holders of less than \$22.0 million principal amount of senior notes consented. The Company has exercised its right to terminate the solicitation.

### Additional Shares of Reunion Common Stock

In the merger, Reunion issued 9,500,000 shares of common stock to holders of Chatwins Group's common stock. The merger agreement also provided that up to an additional 500,000 shares of Reunion common stock would be issued to former Chatwins Group common stockholders if the former Chatwins Group businesses and the acquired Kingway business achieve specified performance levels in 2000. A determination of the number of shares to be issued was made by the board of directors at its meeting held on May 15, 2001. Such additional shares totaled 348,995 and were issued on May 29, 2001. The closing price of Reunion's common stock on that date was \$1.30 per share. The issuance of the additional shares was recorded as a merger purchase price adjustment to goodwill.

### Payment of \$680,000 Industrial Revenue Development Bonds

Upon the sale of its domestic grating operations in September 1999, the Company retained an obligation for a \$680,000 note payable due May 1, 2001 related to an industrial development revenue bond issue by Orem City, Utah. This note payable was repaid in May 2001 from funds available under the Company's revolving credit facility.

- 24 -

## RESULTS OF OPERATIONS

Three Months Ended September 30, 2001 Compared to  
Three Months Ended September 30, 2000

Metals Group

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

Metals Group net sales and gross margins for the third quarters of 2001 and 2000 are as follows. Third quarter 2000 seamless pressure vessels sales and margins are pro forma as though the acquisition of NPSAC occurred at the beginning of 2000.

	Net Sales		Gross Margin	
	2001	2000	2001	2000
Bridges and cranes	\$ 3,247	\$ 5,802	(51.8%)	(6.2%)
Materials handling systems	13,827	14,128	19.9%	24.4%
Seamless pressure vessels	8,042	8,648	25.1%	28.1%
Cylinders	4,246	6,938	6.1%	22.9%
Leaf springs	657	793	8.2%	17.7%
Metals Group totals	\$ 30,019	\$ 36,309	11.3%	20.0%
	=====	=====	=====	=====

Order levels in the bridges and cranes segment have dropped off significantly as the steel industry continues to respond to foreign steel imports by reducing large capital project spending. The resulting decrease in sales, coupled with losses on existing bridge contracts due to back-charges stemming from product quality issues and late deliveries, have had a significant negative impact on gross margin. Materials handling systems sales are only slightly below last year's third quarter. However, a shift in product mix towards lower margin structural racking resulted in a decrease in gross margin. Seamless pressure vessel sales are down 7% from the year-ago third quarter due to the softness in the microchip and computer industry. Gross margin has been affected by the decrease in volume and a change in product mix. Sales of cylinders continues to be affected by a downturn in this market, [a trend which the Company believes will continue into 2002.] Gross margin has been affected accordingly as the decreased volume has significantly impact this segment's ability to absorb costs. Sales of leaf springs in the third quarter 2001 continued to be impacted by the economic downturn as consumers decreased spending on recreational items, particularly in the marine market, [a trend management anticipates will continue into 2002].

Management evaluates the Company's segments based on EBITDA, a measure of cash generation. EBITDA and EBITDA as a percentage of sales decreased significantly during the 2001 third quarter compared to the pro forma 2000 third quarter primarily due to the same factors affecting gross profit margin discussed above.

### Plastics Group

Plastics Group sales for the third quarter of 2001 totaled \$8.7 million, compared to \$13.3 million in the third quarter of 2000, a decrease of \$4.6 million. Third quarter 2000 Plastics Group sales included \$1.8 million from its former Irish plastics subsidiary which the Company sold in the 2000 third quarter. On a proforma basis, Plastic Group 2000 sales excluding sales of the Irish business would be \$11.5 million, indicating a \$2.8 million decrease quarter-to-quarter. This decrease in revenues is the continuation into 2001 of a trend which began in 1999 and resulted from several factors, including certain customers relocating manufacturing operations to Mexico and Asia, reduced customer orders for continuing programs, end of product cycles and

- 25 -

delays in new program starts, which affected all Plastics Group facilities. [This trend in Plastics Group revenue could continue into 2002.]

Plastics Group gross profit for the third quarter of 2001 was \$847,000,

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

or 9.7%, compared to \$1.9 million, or 13.9%, for the third quarter of 2000. Third quarter 2000 Plastics Group gross profit included \$205,000 from its former Irish plastics subsidiary which the Company sold in the 2000 third quarter. On a proforma basis, Plastic Group third quarter 2000 gross profit excluding the gross profit of the Irish business would be \$1.6 million, indicating a \$0.8 million decrease quarter-to-quarter. This decrease in gross profit is directly related to the decreasing trend in sales, resulting in inefficiencies and the inability to absorb fixed overheads. [Depending on future sales volumes, the declining trend in gross margin could continue.]

Management evaluates the Company's segments based on EBITDA, a measure of cash generation. EBITDA and EBITDA as a percentage of sales decreased during the 2001 third quarter compared to the pro forma 2000 third quarter primarily due to the same factors affecting gross profit margin discussed above.

### Selling, General and Administrative

Selling, general and administrative (SGA) expenses for the third quarter of 2001 were \$5.4 million, compared to \$6.2 million for the third quarter of 2000, a decrease of \$0.8 million. Third quarter 2000 proforma SGA as if the Irish plastics business was sold and NPSAC was acquired at the beginning of 2000 would be \$6.1 million, a \$0.7 million decrease quarter-to-quarter. This decrease in SGA is directly related to the decreasing trend in sales, resulting in lower commissions expense, and cost cutting measures taken during June 2001, which included personnel reductions in sales and administration. The cost of these reductions was inconsequential as the Company paid no severance packages and retained no post-severance obligations related to these reductions. [Management estimates the savings from these reductions to be approximately \$1.0 million annually.] However, the benefits of these cost cutting measures are being offset by the continuation of the negative trend in sales and the resulting effect on the Company's ability to absorb costs. SGA expenses as a percentage of sales increased to 14.0% for the 2001 third quarter compared to 12.4% on a proforma basis in the 2000 third quarter. SGA as a percentage of sales was higher in the 2001 third quarter compared to 2000 due to the faster rate at which volume has decreased compared to decreases in fixed administrative costs.

### Other Expense

Other expense for the third quarter of 2001 was \$0.6 million, compared to other income of \$4.9 million for the third quarter of 2000. The third quarter 2000 includes a gain of \$4.9 million from the sale of the Irish plastics business. Excluding this gain, other expenses increased \$0.6 million. The increase in other expense in the third quarter of 2001 compared to 2000 is the result of an increase in goodwill amortization as the result of the \$8.6 million of goodwill created in the NPSAC acquisition in January 2001 compared to no such amortization in the 2000 third quarter and a higher level of other income in the 2000 third quarter, primarily from scrap sales. There were no other individually significant or offsetting items in either of the third quarters of 2001 or 2000.

### Interest Expense

Interest expense, net, for the third quarter of 2001 was \$2.3 million, compared to \$2.9 million for the third quarter of 2000, a decrease of \$0.6 million. The decrease in interest expense reflects the lower level of debt of the Company as the result of the \$29.5 million of cash proceeds generated through asset sales during the second half of 2000 partially offset by the

debt assumed in the NPSAC acquisition. The decrease in interest expense is

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

also the result of the lower interest rates on the Company's Bank of America facilities due to the many rate reductions by the Federal Reserve after June 2000. [The Company anticipates that interest expense for 2001 will continue to decrease compared to 2000 due to the lower debt level as the result of the \$29.5 million of cash proceeds generated through asset sales during the second half of 2000 and the decrease in prime lending rates during 2001.] However, during the third quarter the rate paid by the Company under its revolving credit facility with BOA increased 200 basis points due to the Company's default status under the BOA financing and security agreement.

### Income Taxes

There was a tax benefit from continuing operations of \$1.3 million for the third quarter of 2001 compared to a nominal tax provision for the third quarter of 2000. The effective tax rate of just over 32% in the 2001 third quarter is lower than the statutory rate due to permanent differences between book and tax operating results, primarily non-deductible goodwill. The effective tax rate in the 2000 third quarter is significantly lower than the statutory rate as the valuation allowance against deferred tax assets related to the Company's net operating loss carryforwards was reduced for the tax effect of the \$4.9 million gain on sale of the Irish plastics business.

### Discontinued Operations

There was a loss from discontinued operations during the third quarter of 2000 of \$337,000 related to the discontinued wine grape agricultural operations.

### Extraordinary Items

The loss from extraordinary items in the 2000 third quarter of \$80,000, net of \$-0- taxes, represents the write-offs of deferred financing costs related to the early repayment of the Company's term loan B with BOA in August 2000 with the proceeds from the sale of the Company's Irish plastics business.

Nine Months Ended September 30, 2001 Compared to  
Nine Months Ended September 30, 2000

### Metals Group

Metals Group net sales and gross margins for the third quarters of 2001 and 2000 are as follows. Year 2000 materials handling systems sales and margins are pro forma as though the acquisition of Kingway occurred at the beginning of 2000. Year 2000 seamless pressure vessels sales and margins are pro forma as though the acquisition of NPSAC occurred at the beginning of 2000.

	Net Sales		Gross Margin	
	2001	2000	2001	2000
Bridges and cranes	\$ 12,625	\$ 18,657	(11.5%)	0.5%
Materials handling systems	38,999	42,268	22.8%	23.9%
Seamless pressure vessels	30,695	25,033	28.7%	29.8%
Cylinders	15,776	23,838	12.9%	22.9%
Leaf springs	2,279	2,864	10.0%	20.8%
Metals Group totals	\$ 100,374	\$ 112,660	18.5%	20.0%

Order levels in the bridges and cranes segment have dropped off significantly as the steel industry continues to respond to foreign steel

imports by reducing large capital project spending. The resulting decrease in sales, coupled with losses on existing bridge contracts due to back-charges stemming from product quality issues and late deliveries, have had a significant negative impact on gross margin. Materials handling systems sales are below last year's first three quarters as large retailers have held back on large warehouse and distribution center projects due to a softening in retail spending by consumers. Also, competitive pressures in the material handling systems segment have resulted in a decrease in cents per pound sales prices. A shift in product mix towards lower margin structural racking resulted in a decrease in gross margin. The increase in pressure vessel sales in the first nine months of 2001 compared to 2000 was due to a strong order levels in that product line towards the end of 2000, the backlog for which at the end of 2000 was \$8.6 million higher than at the end of 1999, and the recognition of \$2.8 million of revenues on a large NASA contract relating to pressure vessels produced in the fourth quarter of 2000 but not received by NASA until the first quarter of 2001. Gross margin has been affected by a change in product mix. Sales of cylinders continues to be affected by a downturn in this market, [a trend which the Company believes will continue into 2002.] Gross margin has been affected accordingly as the decreased volume has significantly impact this segment's ability to absorb costs. Sales of leaf springs in the first nine months of 2001 continued to be impacted by the economic downturn as consumers decreased spending on recreational items, particularly in the marine market, [a trend management anticipates will continue into 2002].

Management evaluates the Company's segments based on EBITDA, a measure of cash generation. EBITDA and EBITDA as a percentage of sales decreased significantly during the first nine months of 2001 compared to the pro forma 2000 primarily due to the same factors affecting gross profit margin discussed above.

#### Plastics Group

Plastics Group sales for the first nine months of 2001 totaled \$31.7 million, compared to \$32.0 million in the first nine months of 2000. Year-to-date 2000 Plastics Group sales included \$5.0 million from its former Irish plastics subsidiary which the Company sold in the 2000 third quarter but excluded \$11.3 million of sales from the pre-March 16, 2000 merger period. On a proforma basis assuming these events occurred at the beginning of 2000, Plastic Group 2000 sales would be \$38.3 million, indicating a \$6.6 million decrease year-to-year. This decrease in revenues is the continuation into 2001 of a trend which began in 1999 and resulted from several factors, including certain customers relocating manufacturing operations to Mexico and Asia, reduced customer orders for continuing programs, end of product cycles and delays in new program starts, which affected all Plastics Group facilities. [This trend in Plastics Group revenue could continue into 2002.]

Plastics Group gross profit for the first nine months of 2001 was \$4.3 million, or 13.5%, compared to \$4.9 million, or 15.2%, for the first nine months of 2000. On a proforma basis for the events described above Plastics Group gross profit and margin would be \$5.9 million, or 15.5%. The decrease in gross profit is directly related to the decreasing trend in sales, resulting in inefficiencies and the inability to absorb fixed overheads. [Depending on future sales volumes, the declining trend in gross margin could continue.]

Management evaluates the Company's segments based on EBITDA, a measure of cash generation. EBITDA and EBITDA as a percentage of sales decreased significantly during the first nine months of 2001 compared to the pro forma 2000 primarily due to the same factors affecting gross profit margin discussed

above.

- 28 -

#### Selling, General and Administrative

Selling, general and administrative (SGA) expenses for the first nine months of 2001 were \$17.6 million, compared to \$16.7 million for the first nine months of 2000. Had the merger, the acquisitions of Kingway and NPSAC and the sale of the Company's Irish plastics business occurred at the beginning of 2000, SGA for the first nine months of 2000 would have been \$18.0 million, indicating a pro forma decrease of \$0.4 million. This decrease in SGA is directly related to the decreasing trend in sales, resulting in lower commissions expense, and cost cutting measures taken during June 2001, which included personnel reductions in sales and administration. The cost of these reductions was inconsequential as the Company paid no severance packages and retained no post-severance obligations related to these reductions.

[Management estimates the savings from these reductions to be approximately \$1.0 million annually.] However, the benefits of these cost cutting measures are being offset by the continuation of the negative trend in sales and the resulting effect on the Company's ability to absorb costs. SGA expenses as a percentage of sales increased to 13.3% for the first nine months of 2001 compared to 11.9% on a proforma basis in the 2000 period. SGA as a percentage of sales was higher in the 2001 period compared to 2000 due to the faster rate at which volume has decreased compared to decreases in fixed administrative costs.

#### Other Expense

Other expense for the first nine months of 2001 was \$1.8 million, compared to other income of \$4.3 million for the first nine months of 2000. Excluding the \$4.9 million gain on sale of the Irish plastics business, other expenses would be 0.6 million, a net increase of \$1.2 million. The increase in other expense in the first nine months of 2001 compared to 2000 is the result of an increase in goodwill amortization. The first nine months of 2001 includes a full three quarters of goodwill amortization related to the merger, Kingway acquisition and NPSAC acquisition compared to the approximate six-and-one-half month post-merger and Kingway acquisition period in the 2000 first nine months and no goodwill amortization related to the NPSAC goodwill. Except for goodwill amortization, there were no individually significant or offsetting items in either of the first nine months of 2001 or 2000.

#### Interest Expense

Interest expense, net, for the first nine months of 2001 was \$7.0 million, compared to \$7.9 million for the first nine months of 2000, a decrease of \$0.9 million. The decrease in interest expense reflects the lower level of debt of the Company as the result of the \$29.5 million of cash proceeds generated through asset sales during the second half of 2000 partially offset by the debt assumed in the NPSAC acquisition. The decrease in interest expense is also the result of the lower interest rates on the Company's Bank of America facilities due to the many rate reductions by the Federal Reserve after June 2000. [The Company anticipates that interest expense for 2001 will continue to decrease compared to 2000 due to the lower debt level as the result of the \$29.5 million of cash proceeds generated through asset sales during the second half of 2000 and the decrease in prime lending rates during 2001]. However, during the third quarter the rate paid by the Company under its revolving credit facility with BOA increased 200 basis points due to the Company's default status under the BOA financing and security agreement.

#### Equity Results

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

Equity in loss of continuing operations of affiliate in the first nine months of 2000 represents Chatwins Group's pre-merger share of Reunion's loss from continuing operations in that period.

- 29 -

### Income Taxes

There was a tax benefit from continuing operations of \$1.1 million for the first nine months of 2001 compared to a tax benefit of \$0.3 million for the first nine months of 2000. The effective tax rate of almost 32% in the 2001 first nine months is lower than the statutory rate due to permanent differences between book and tax operating results, primarily non-deductible goodwill. The effective tax rate in the 2000 third quarter is significantly lower than the statutory rate as the valuation allowance against deferred tax assets related to the Company's net operating loss carryforwards was reduced for the tax effects of the \$4.9 million gain on sale of the Irish plastics business and the extraordinary items discussed below.

### Discontinued Operations

There was a loss from discontinued operations during the first nine months of 2000 of \$0.8 million related to the discontinued wine grape agricultural operations.

### Extraordinary Items

The losses from extraordinary items in the first nine months of 2000 of \$1.9 million, net of \$-0- taxes, represents the pre-merger write-offs of deferred financing costs at both Chatwins Group and pre-merger Reunion and fees related to the early repayment of the Company's term loan B with BOA in August 2000 with the proceeds from the sale of the Company's Irish plastics business.

## LIQUIDITY AND CAPITAL RESOURCES

### GENERAL

The Company manages its liquidity as a consolidated enterprise. The operating groups of the Company carry minimal cash balances. Cash generated from group operating activities generally is used to repay borrowings under revolving credit arrangements, as well as other uses (e.g. corporate headquarters expenses, debt service, capital expenditures, etc.). Conversely, cash required for group operating activities generally is provided from funds available under the same revolving credit arrangement. Although the Company operates in relatively mature markets, [it intends to continue to invest in and grow its businesses through selected capital expenditures as cash generation permits.]

### RECENT DEVELOPMENTS AND OTHER MATTERS

#### Restructuring and Other Actions

As the result of downturns in several of the markets served by the Company and the resulting decrease in the Company's ability to absorb costs, management of the Company has determined to develop a plan to restructure its continuing businesses and dispose of or shut-down certain non-strategic businesses. These actions will be designed to improve productivity and operating performance.

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

[Development of the plan and its approval by the Company's board of directors is anticipated to be completed by the end of 2001. Once approved, management of the Company expects to record a charge for restructuring costs including employee separation costs, facility shut-down and rationalization costs and asset writedowns.] At this time, a reasonably dependable estimate of the total amount of the restructuring charge does not exist. [However,

- 30 -

management anticipates that the charge will have a significant impact on the Company's results of operations for the year and quarter ended December 31, 2001.]

### 2001 Covenant Compliance

For the quarter ended March 31, 2001 and for each fiscal quarter thereafter in 2001, the BOA financing and security agreement required the Company to maintain a minimum fixed charge coverage ratio of 1.25:1 and maximum funded debt to EBITDA ratios of 3.75:1, 3.50:1, 3.25:1 and 3.00:1.

In April 2001, the Company entered into a letter agreement with Bank of America whereby, as long as the Company maintained both a fixed charge coverage ratio of at least 1.00:1 and had a funded debt to EBITDA ratio of no more than 4.50:1 as of the September 30, 2001 and December 31, 2001 calculation dates, and as long as the Company was in compliance on all other covenants, the Bank of America would not accelerate any of its loans.

Due to the rate and level of the downturns in several of the markets served by the Company and the resulting decrease in the Company's ability to absorb costs, cost cutting and capital expenditure restriction measures taken by management during the third quarter of 2001 were not enough to achieve ratio compliance. For the quarter ended September 30, 2001, the Company's fixed charge coverage ratio was 0.79:1 and the funded debt to EBITDA ratio was 5.61:1. As a result, the Company is in default under its BOA Financing and Security Agreement.

The Company and Bank of America entered into various amendments to the BOA financing and security agreement during 2000. The December 12, 2000 amendment required the Company to maintain a minimum availability under the revolving credit facility of \$1.5 million. Through the second quarter of 2001, the Company had complied with this requirement. However, due to the downturn in several of the markets served by the Company during the third quarter of 2001 and the resulting decrease in the quality of the Company's borrowing base, ineligible receivables and inventory increased. Based on the borrowing base formulas as set forth in the BOA financing and security agreement, this increase in ineligibles resulted in a decrease in borrowing availability under the revolving credit facility and the Company's inability to maintain a minimum availability of \$1.5 million. As a result, the Company is in default under its BOA financing and security agreement.

[The Company is seeking to renegotiate or obtain waivers of its financial and minimum availability covenants. Although management believes it is unlikely, in the event that the Company is not able to successfully renegotiate its covenants or obtain the necessary waivers, the lenders have various remedies available to them including, but not limited to, acceleration of all amounts outstanding under the term and revolving credit facilities and a liquidation of its collateral.]

### Semi-Annual Interest on 13% Senior Notes due November 1, 2001

The Company was unable to fund its \$1.623 million semi-annual interest payment on its 13% senior notes as it had insufficient funds available under

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

its revolving credit facility. Failure to make the November 1 interest payment is a default under the indenture which supports the 13% senior notes. Under the terms of the indenture, the Company has thirty days to cure the default.

- 31 -

Management of the Company has been in contact with certain of the Note Holders and holders representing approximately ninety percent of the principal amount of senior notes outstanding have expressed their support of the Company. [Management of the Company is continuing to work with its secured lenders as well as other alternative financing sources in an effort to pay the \$1.616 million interest by November 30. Management of the Company currently believes that it will be able to obtain the necessary funds. However, there can be no assurance that management will be successful in its efforts.]

### Acquisition of NPS Acquisition Corp. and Note Payable Assumption

On January 17, 2001, the Company acquired NPS Acquisition Corp. (f/k/a Naptech Pressure Systems) from Charles E. Bradley, Sr. (Mr. Bradley), the Company's chairman of the board and chief executive officer. NPSAC is based in Clearfield, Utah and manufactures seamless steel pressure vessels, an existing Metals Group segment.

The purchase price was \$10,000 plus the non-cash assumption of \$10.3 million of NPSAC's liabilities, including a 15% per annum \$6.9 million note payable to Shaw Group, the former owner of Naptech Pressure Systems and \$0.6 million of notes payable to Stanwich Financial Services Corp., a related party. Simultaneously with the acquisition, Reunion paid Shaw Group \$2.0 million of the note payable in cash from funds available under its revolving credit facility with Bank of America (BOA). The remainder of the note payable of \$4.9 million was then restructured to include quarterly principal payments of \$0.6 million for eight quarters which began on February 28, 2001. Reunion made the first two payments from funds available under its revolving credit facility. The Company was unable to fund the third payment due August 31, 2001 as it had insufficient funds available under its revolving credit facility. The note is unsecured and subordinate to the BOA term loan and revolving credit facilities.

The estimated fair value of assets acquired included approximately \$1.4 million of cash, receivables, inventories and other current assets, approximately \$0.3 million of fixed assets and \$1.3 million of deferred tax assets which are fully reserved by a valuation allowance. The purchase price in excess of net assets acquired of \$8.6 million was recorded as goodwill and is being amortized over 15 years. NPSAC's deferred tax assets are comprised primarily of net operating losses.

### Repayment of \$120,000 of 13% Senior Notes

Chatwins Group was required to make sinking fund payments to redeem \$12.5 million principal amount of the senior notes on May 1 in each of 2000 through 2003 at face value plus accrued interest and to offer to purchase \$25 million of the senior notes on June 1, 2000 at face value plus accrued interest. In February 2000, Chatwins Group solicited the holders of the \$49,975,000 of 13% senior notes outstanding asking them to waive their right to participate in the June 1, 2000 \$25.0 million purchase offer, of which \$47,450,000 agreed to waive such right resulting in a maximum purchase offer obligation on June 1, 2000 of \$2,525,000.

As such, on June 1, 2000 Reunion made the required offer to purchase \$2,525,000 of senior notes, of which holders of only \$120,000 of senior notes tendered. However, the \$25.0 million of 13% senior notes repaid from the

Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

- 32 -

merger proceeds was applied against Reunion's obligations for sinking fund payments and the purchase offer as follows (in thousands):

	May 1, 2000	June 1, 2000	May 1, 2001	Total
	-----	-----	-----	-----
Sinking fund payment or purchase offer obligation	\$ 12,500	\$ 120	\$ 12,500	\$ 25,120
\$25.0 million applied to obligations	(12,500)	(120)	(12,380)	(25,000)
	-----	-----	-----	-----
Maximum required payment	\$ -	\$ -	\$ 120	\$ 120
	=====	=====	=====	=====

Therefore, \$120,000 principal amount of 13% senior notes was repaid by the Company on May 1, 2001 from funds available under its revolving credit facility.

Of the remaining \$24.855 million of senior notes, \$12.5 million is scheduled to be repaid in May 2002 and \$12.355 million is scheduled to be repaid in May 2003. [Management does not expect to have the internally generated liquidity necessary to fund the May 1, 2002 sinking fund payment and is in the process of investigating various refinancing and repayment scenarios. Such scenarios involve not only mezzanine or additional term debt, which could potentially include warrants, but also involves other considerations such as a sale of assets. If the Company is unable to make its May 2002 sinking fund payment obligation, the Company will be in default under the indenture for the senior notes which could result in the acceleration of all amounts due under the senior notes, including all principal and accrued but unpaid interest.]

#### Solicitation of Consent of Senior Noteholders

The Company is required to make sinking fund payments on its \$24.855 million of senior notes of \$12.5 million on May 1, 2002 and \$12.355 million on May 1, 2003. On September 4, 2001, the Company solicited the consent of its senior noteholders to extend the sinking fund payment dates by two years. The solicitation expired on November 2, 2001. As part of the solicitation, the Company reserved the right to terminate it if holders of less than \$22.0 million principal amount of senior notes consented. The Company has exercised its right to terminate the solicitation.

#### Additional Shares of Reunion Common Stock

In the merger, Reunion issued 9,500,000 shares of common stock to holders of Chatwins Group's common stock. The merger agreement also provided that up to an additional 500,000 shares of Reunion common stock would be issued to former Chatwins Group common stockholders if the former Chatwins Group businesses and the acquired Kingway business achieve specified performance levels in 2000. A determination of the number of shares to be issued was made by the board of directors at its meeting held on May 15, 2001. Such additional shares totaled 348,995 and were issued on May 29, 2001. The closing price of Reunion's common stock on that date was \$1.30 per share. The issuance of the additional shares was recorded as a merger purchase price adjustment to goodwill.

#### Payment of \$680,000 Industrial Revenue Development Bonds

Upon the sale of its domestic grating operations in September 1999, the

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

Company retained an obligation for a \$680,000 note payable due May 1, 2001 related to an industrial development revenue bond issue by Orem City, Utah. This note payable was repaid in May 2001 from funds available under the

- 33 -

Company's revolving credit facility.

### SUMMARY OF 2001 ACTIVITIES

Cash and cash equivalents totaled \$1.3 million at September 30, 2001. During the first nine months of 2001, cash and cash equivalents decreased \$1.2 million, with \$2.9 million used in operations, \$2.5 million used in investing activities and \$4.2 million provided by financing activities.

#### Operating Activities

Cash used of \$2.9 million for operating activities in the first nine months of 2001 was the result of an increase in net working capital, primarily reductions in trade payables and other current liabilities, and the funding of operating losses.

#### Investing Activities

Capital expenditures were \$2.5 million, including \$1.6 million in the Metals Group and \$0.9 million in the Plastics Group.

#### Financing Activities

To fund capital expenditures, operating losses, the decreases in trade payables and other current liabilities, the \$2.0 million payment to Shaw Group at the date of the NPSAC acquisition and principal payments on debt, the Company made a net increase in borrowings under its revolving credit facility of \$8.0 million and \$0.5 million under its capital expenditure facility. Principal payments on debt totaled \$4.3 million including \$2.8 million of term loan A, \$1.2 million of the Shaw Group note payable and \$0.3 million of other debt, primarily \$120,000 of senior notes, \$123,000 of capital expenditure facility repayments, a \$48,000 final payment on a note payable related to the Metals Group and various capital lease and small business loan obligations.

### FACTORS AFFECTING CURRENT AND FUTURE LIQUIDITY

During the third quarter of 2001, the Company experienced downturns in several of the markets it serves resulting in a decrease in the Company's ability to absorb costs and a decrease in the quality of its borrowing base due to an increase in ineligible receivables and inventory. Based on the borrowing base formulas as set forth in the BOA financing and security agreement, this increase in ineligibles resulted in a decrease in borrowing availability under the revolving credit facility. These events have had a significant adverse effect on the Company's ability to meet its obligations.

Although management of the Company is currently in the process of developing a restructuring plan, including the disposition of non-strategic businesses, which will be designed to improve productivity and operating performance, [the benefits of its implementation may not materialize for several quarters]. At the same time, the Company has immediate and near-term obligations.

[Management of the Company is currently pursuing several scenarios in order to alleviate the current and future strain on liquidity, including a sale of assets and/or new financing. However, no assurances can be given that such pursuits will be successful and that, if unsuccessful, the Company may

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

not be able to meet its immediate and near-term obligations.]

### Item 3. Quantitative and Qualitative Disclosures About Market Risk

There have been no significant changes in the market risk factors which affect the Company since the end of the preceding fiscal year.

- 34 -

## PART II. OTHER INFORMATION

### Item 1. Legal Proceedings

The Company and its subsidiaries are defendants in a number of lawsuits and administrative proceedings, which have arisen in the ordinary course of business of the Company and its subsidiaries. The Company believes that any material liability which can result from any of such lawsuits or proceedings has been properly reserved for in the Company's consolidated financial statements or is covered by indemnification in favor of the Company or its subsidiaries, and therefore the outcome of these lawsuits or proceedings will not have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

In June 1993, the U.S. Customs Service (Customs) made a demand on Chatwins Group's former industrial rubber distribution division for \$612,948 in marking duties pursuant to 19 U.S.C. Sec. 1592. The duties are claimed on importations of "unmarked" hose products from 1982 to 1986. Following Chatwins Group's initial response raising various arguments in defense, including expired statute of limitations, Customs responded in January 1997 by reducing its demand to \$370,968 and reiterating that demand in October 1997. Chatwins Group restated its position and continues to decline payment of the claim. Should the claim not be resolved, Customs threatens suit in the International Courts of Claims. The Company continues to believe, based on consultation with counsel, that there are facts which raise a number of procedural and substantive defenses to this claim, which will be vigorously defended. There is no applicable insurance coverage.

In December 1999, a stockholder of Reunion filed a purported class-action lawsuit in Delaware Chancery Court alleging, among other things, that Reunion's public stockholders would be unfairly diluted in the merger with Chatwins Group. The lawsuit sought to prevent completion of the merger and, the merger having been completed, seeks rescission of the merger or awarding of damages. The lawsuit is in the initial stages of discovery. Reunion intends to vigorously contest the suit.

The Company has been named as a defendant in fifteen consolidated lawsuits filed in December 2000 or early 2001 in the Superior Court for Los Angeles County, California, three of which are purported class actions asserted on behalf of approximately 200 payees. The plaintiffs in these suits except one are structured settlement payees to whom Stanwich Financial Services Corp. (SFSC) is indebted. The Company and SFSC are related parties.

In addition to the Company, there are numerous defendants in these suits, including SFSC, Mr. Bradley, the sole shareholder of SFSC's parent, several major financial institutions and certain others. All of these suits arise out of the inability of SFSC to make structured settlement payments when due. Pursuant to the court's order, plaintiffs in the purported class actions and plaintiffs in the individual cases actions filed a model complaint. Except for the class allegations, the two model complaints are identical. The plaintiffs seek compensatory and punitive damages, restoration of certain alleged trust assets, restitution and attorneys' fees and costs.

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

The plaintiffs in one of the suits are former owners of a predecessor of SFSC and current operators of a competing structured settlement business. These plaintiffs claim that their business and reputations have been damaged by SFSC's structured settlement defaults, seek damages for unfair competition and purport to sue on behalf of the payees.

The plaintiffs allege that the Company borrowed funds from SFSC and has not repaid these loans. The plaintiffs' theories of liability against the Company are that it is the alter ego of SFSC and Mr. Bradley and that the

- 35 -

Company received fraudulent transfers of SFSC's assets. The plaintiffs also assert direct claims against the Company for inducing breach of contract and aiding and abetting an alleged breach of fiduciary duty by SFSC.

On May 25, 2001, SFSC filed a chapter 11 bankruptcy petition in the U.S. Bankruptcy Court for the District of Connecticut. SFSC filed an adversary proceeding in the bankruptcy case against the plaintiffs seeking a declaration that the structured settlement trust assets are the property of the bankruptcy estate. On July 16, 2001, the bankruptcy court granted a temporary restraining order enjoining the plaintiffs from prosecuting their claims against the Company, SFSC, Mr. Bradley and others. As a result of this restraining order of the bankruptcy court, the Company entered a standstill agreement with the plaintiffs on August 22, 2001. Pursuant to the standstill agreement, and the stipulation of the parties to the SFSC bankruptcy case, the plaintiffs agreed to take no further action to prosecute any claim in the litigation against the Company, Mr. Bradley and others to recover any structured settlement trust assets or any derivative claims or claims based on allegations of alter ego, fraudulent transfer or conversion. The plaintiffs did not agree to waive or release their direct personal claims against the Company for damages, but the plaintiffs agreed to cease and desist the prosecution of those claims until no earlier than sixty days following service of written notice to the Company stating that they have elected to unilaterally terminate the standstill agreement.

Plaintiffs filed second amended model complaints in the class actions and individual cases on August 24, 2001. Both model complaints allege causes of action against the Company for interference with contract and aiding and abetting breach of fiduciary duty. However, pursuant to the standstill agreement, the plaintiffs are taking no action to prosecute these claims against the Company at this time.

Certain of the financial institution defendants have asserted cross-complaints against the Company for implied and express indemnity and contribution and negligence. The Company denies the allegations of the plaintiffs and the cross-complainant financial institutions and intends to vigorously defend against these actions and cross-actions.

The Company has been named in approximately 195 separate asbestos suits filed since January 1, 2001 by two plaintiffs' law firms in Wayne County, Michigan. The claims allege that cranes from the Company's crane manufacturing location in Alliance, OH were present in various parts of McLouth Steel Mill in Wayne County, Michigan and that those cranes contained asbestos to which plaintiffs were exposed over a 40 year span. As of the date of this report, counsel for the Company has filed an answer to each complaint denying liability by the Company and asserting all alternative defenses permitted under the Court's Case Management Order. Counsel for the Company has negotiated dismissal of 95 cases without any cost to the Company.

The Company denies that it manufactured any products containing asbestos or otherwise knew or should have known that any component part manufacturers

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

provided products containing asbestos. The Company intends to vigorously defend against these lawsuits.

On July 10, 2001, a lawsuit that alleges personal injury from asbestos exposure was filed in the Superior Court for San Francisco County in California against greater than fifty defendants, including Oneida Rostone Corporation (ORC), pre-merger Reunion's Plastics subsidiary and the Company's Plastics Group. In October 2001, Allen-Bradley Company, a former owner of the Rostone business of ORC, agreed to defend and indemnify Reunion in this lawsuit pursuant to a contractual obligation to do so.

- 36 -

### Item 3. Defaults Upon Senior Securities

Debt in default consists of the following (in thousands):

	At September 30, 2001 ----- (unaudited)
13% senior notes (net of unamortized discount of \$5)	\$ 24,850
BOA revolving credit facility	27,358
BOA term loan A due March 16, 2007	16,993
BOA capital expenditure facility	1,051
	-----
Total debt in default	\$ 70,252 =====

### 13% Senior Notes

The Company was unable to make its November 1, 2001 semi-annual interest payment of \$1.616 million on its 13% Senior Notes due 2003 due to lack of available funds under its revolving credit facility.

Failure to make the November 1 interest payment is a default under the indenture which supports the 13% Senior Notes. Under the terms of the indenture, the Company has thirty days to cure the default.

### BOA Financing and Security Agreement

In April 2001, the Company entered into a letter agreement with Bank of America whereby the Company was required to maintain both a fixed charge coverage ratio of at least 1.00:1 and a funded debt to EBITDA ratio of no more than 4.50:1 as of the September 30, 2001 and December 31, 2001 calculation dates. For the quarter ended September 30, 2001, the Company's fixed charge coverage ratio was 0.79:1 and the funded debt to EBITDA ratio was 5.61:1. As a result, the Company is in default under its BOA financing and security agreement.

The Company and Bank of America entered into various amendments to the BOA financing and security agreement during 2000. The December 12, 2000 amendment required the Company to maintain a minimum availability under the revolving credit facility of \$1.5 million. Due to the downturn in several of the markets served by the Company during the third quarter of 2001 and the resulting decrease in the quality of the Company's borrowing base, the Company was unable to maintain a minimum availability of \$1.5 million. As a result, the Company is in default under its BOA financing and security agreement.

- 37 -

## Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

### Item 5. Other Information

On June 14, 2000, the Company's Board of Directors approved the exchange of its Series A and Series B preferred stocks for 3,245,515 shares of the Company's common stock at an exchange price of \$5.00 per share. The Series A and Series B preferred stocks were issued in connection with the March 16, 2000 merger with Chatwins Group and acquisition of Kingway, and had an aggregate liquidation value of \$16.2 million. The closing market price of Reunion's common stock was \$1.00 on that date.

The Series A preferred stock was issued to holders of Chatwins Group's Class D, Series A, B and C preferred stock in exchange for their shares. Since its incorporation on May 12, 1988, Chatwins Group has had several classes of preferred stock outstanding. Since that time, Chatwins Group made liquidation value and dividend accretions totaling \$15.0 million recorded as charges to retained earnings. Of the \$15.0 million of such charges, \$12.5 million related to its Class D, Series A, B and C preferred stock. Since May 12, 1988, Chatwins Group made payments for redemptions and dividends totaling \$3.5 million related to such preferred stock. Accordingly, \$9.0 million of such charges on its Class D, Series A, B and C preferred stock remained unpaid.

Because Chatwins Group was considered the acquirer in the merger, Reunion Industries' accumulated deficit at September 30, 2001 is primarily comprised of the historical activity of Chatwins Group which includes its historical results of operations, dividends declared and paid and the \$9.0 million of unpaid liquidation value and dividend accretions. As such, the merged Reunion's accumulated deficit is largely a legacy of the former Chatwins Group's preferred stock accretions. The following supplemental disclosure of the components of the \$5.7 million accumulated deficit at September 30, 2001 separates operating results from preferred stock accretions and dividends paid (in 000's):

	Components of Reunion's Accumulated Deficit -----
Accumulated deficit on May 12, 1988 (date of incorporation of Chatwins Group)	\$ (13)
Cumulative net income	9,809
Preferred stock liquidation accretions, all classes	(7,728)
Preferred stock dividend accretions, all classes	(7,293)
Dividends paid	(435) -----
Accumulated deficit at September 30, 2001	\$ (5,660) =====

- 38 -

### Item 6. Exhibits and Reports on Form 8-K

#### (b) Reports on Form 8-K

Third Quarter 2001:  
-----

None.

Fourth Quarter 2001:  
-----

Edgar Filing: REUNION INDUSTRIES INC - Form 10-Q

On November 8, 2001, the Company filed a Current Report on Form 8-K dated November 1, 2001 to report under Items 5 and 7 that the Company delayed payment of its semi-annual interest payment on its senior notes of \$1.616 million due November 1, 2001 and to file the related press release as an exhibit.

SIGNATURES

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

Date: November 14, 2001  
-----

REUNION INDUSTRIES, INC.  
(Registrant)

By: /s/ Kimball J. Bradley  
-----  
Kimball J. Bradley  
President and Chief  
Operating Officer

By: /s/ John M. Froehlich  
-----  
John M. Froehlich  
Executive Vice President, Finance  
and Chief Financial Officer  
(chief financial and accounting officer)