FORM 10-Q
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

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

For the quarterly period ended June 29, 1996

OR

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

Commission file number 0-19621

APPLIANCE RECYCLING CENTERS OF AMERICA, INC.

MINNESOTA

(State or other jurisdiction of
incorporation or organization)
7400 Excelsior Blvd.
Minneapolis, Minnesota 55426-4517
(Address of principal executive
offices)

41-1454591
(I.R.S. Employer
Identification No.)

(612) 930-9000
(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, and (2) has been subject to such filing requirements for the past 90 days.

YES __X__ NO _____

As of August 5, 1996, the number of shares outstanding of the registrant's no par value common stock was 4,547,077 shares.

APPLIANCE RECYCLING CENTERS OF AMERICA, INC.

INDEX

PART I. FINANCIAL INFORMATION

Item 1: Financial Statements:

Consolidated Balance Sheets as of
June 29, 1996 and December 30, 1995

Consolidated Statements of Operations for the Three and Six
Months Ended June 29, 1996 and July 1, 1995

Consolidated Statements of Cash Flows for the
Six Months Ended June 29, 1996 and July 1, 1995

Notes to Consolidated Financial Statements

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

PART II. OTHER INFORMATION

<TABLE>
<CAPTION>

Appliance Recycling Centers of America, Inc. and Subsidiaries

CONSOLIDATED BALANCE SHEETS
(Unaudited)

| | June 29, 1996 | December 30, 1995 |
|---|---|---|
| <S> | <C> | <C> |
| ASSETS | | |
| Current Assets | | |
| Cash and cash equivalents | $ 254,000 | $ 4,605,000 |
| Accounts receivable | 1,386,000 | 1,382,000 |
| Inventories | 986,000 | 426,000 |
| Other current assets | 323,000 | 325,000 |
| Income taxes receivable | 70,000 | 106,000 |
| Deferred tax assets | 277,000 | 277,000 |
| Total current assets | $ 3,296,000 | $ 7,121,000 |
| Property and Equipment, at cost | | |
| Land | $ 2,103,000 | $ 2,101,000 |
| Buildings and improvements | 4,510,000 | 3,677,000 |
| Equipment | 6,295,000 | 6,483,000 |
| | $ 12,908,000 | $ 12,261,000 |
| Less accumulated depreciation | 4,221,000 | 3,973,000 |
| Net property and equipment | $ 8,687,000 | $ 8,288,000 |
| Other Assets | 576,000 | 108,000 |
| Deferred Tax Assets | 373,000 | 373,000 |
| Total assets | $ 12,932,000 | $ 15,890,000 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current Liabilities | | |
| Note payable to bank | $ 250,000 | $ -- |
| Current maturities of long-term obligations | 496,000 | 1,041,000 |
| Accounts payable | 1,675,000 | 1,536,000 |
| Accrued expenses | 836,000 | 1,041,000 |
| Total current liabilities | $ 3,257,000 | $ 3,618,000 |
| Long-Term Obligations, less current maturities | 1,813,000 | 2,084,000 |
| Total liabilities | $ 5,070,000 | $ 5,702,000 |
| Shareholders' Equity | | |
| Common Stock, no par value; authorized 20,000,000 shares; issued and outstanding 4,547,000 as of June 29, 1996 and 4,227,000 as of December 30, 1995 | $ 10,350,000 | $ 9,177,000 |
| Retained earnings (deficit) | (2,466,000) | 1,032,000 |
| Foreign currency translation adjustment | (22,000) | (21,000) |
| Total shareholders' equity | $ 7,862,000 | $ 10,188,000 |
| Total liabilities and shareholders' equity | $ 12,932,000 | $ 15,890,000 |

See Notes to Consolidated Financial Statements

</TABLE>

<TABLE>
<CAPTION>

Appliance Recycling Centers of America, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

| | Three Months Ended June 29, 1996 | Three Months Ended July 1, 1995 | Six Months Ended June 29, 1996 | Six Months Ended July 1, 1995 |
|---|---|---|---|---|
| <S> | <C> | <C> | <C> | <C> |
| Revenues | | | | |
| Recycling revenues | $ 1,399,000 | $ 3,073,000 | $ 3,166,000 | $ 5,797,000 |
| Appliance sales | 1,351,000 | 435,000 | 2,185,000 | 778,000 |
| Byproduct revenues | 523,000 | 504,000 | 982,000 | 1,105,000 |
| Net revenues | $ 3,273,000 | $ 4,012,000 | $ 6,333,000 | $ 7,680,000 |
| Cost of Revenues | 2,692,000 | 2,476,000 | 5,542,000 | 4,885,000 |

| | | | | |
|---|---|---|---|---|
| Gross profit | $ 581,000 | $ 1,536,000 | $ 791,000 | $ 2,795,000 |
| Selling, General and Administrative Expenses | 2,209,000 | 1,417,000 | 4,256,000 | 2,754,000 |
| Operating income (loss) | $(1,628,000) | $ 119,000 | $(3,465,000) | $ 40,000 |
| Other Income (Expense): | | | | |
| Other income | 84,000 | 6,000 | 70,000 | 37,000 |
| Interest income | 4,000 | 56,000 | 32,000 | 108,000 |
| Interest expense | (66,000) | (67,000) | (135,000) | (139,000) |
| Income (loss) before provision for income taxes | $(1,606,000) | $ 114,000 | $(3,498,000) | $ 47,000 |
| Provision for (Benefit of) Income Taxes | -- | 53,000 | -- | 25,000 |
| Net income (loss) | $(1,606,000) | $ 61,000 | $(3,498,000) | $ 22,000 |
| Net Earnings (Loss) per Common and Common Equivalent Share | $ (0.36) | $ 0.01 | $ (0.80) | $ 0.01 |
| Weighted Average Number of Common and Common Equivalent Shares | 4,404,000 | 4,247,000 | 4,365,000 | 4,245,000 |

</TABLE>

See Notes to Consolidated Financial Statements

<TABLE>
<CAPTION>

Appliance Recycling Centers of America, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

| | Six Months Ended June 29, 1996 | July 1, 1995 |
|---|---|---|
| <S> | <C> | <C> |
| Cash Flows from Operating Activities | | |
| Net income (loss) | $(3,498,000) | $ 22,000 |
| Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities: | | |
| Depreciation and amortization | 764,000 | 742,000 |
| Common Stock issued for services | 30,000 | -- |
| (Gain) loss on sale of equipment | (48,000) | (31,000) |
| Deferred income taxes | -- | (28,000) |
| Change in assets and liabilities, net of effects from acquisition of Universal Appliance Company, Inc. and Universal Appliance Recycling, Inc.: | | |
| (Increase) decrease in: | | |
| Receivables | 251,000 | 2,224,000 |
| Inventories | (505,000) | (10,000) |
| Other current assets | 11,000 | 60,000 |
| Income taxes receivable | 40,000 | (48,000) |
| (Increase) decrease in: | | |
| Accounts payable | (37,000) | (212,000) |
| Accrued expenses | (237,000) | (282,000) |
| Income taxes payable | (23,000) | (427,000) |
| Net cash provided by (used in) operating activities | $(3,252,000) | $ 2,010,000 |
| Cash Flows from Investing Activities | | |
| Purchase of equipment | $(1,147,000) | $ (249,000) |
| Cash acquired for acquisition of Universal Appliance Company, Inc. and Universal Appliance Recycling, Inc. | 26,000 | -- |
| Payments for noncompete agreements | (110,000) | -- |
| Proceeds from disposal of equipment | 153,000 | 76,000 |
| Net cash provided by (used in) investing activities | $(1,078,000) | $ (173,000) |
| Cash Flows from Financing Activities | | |
| Increase (decrease) in note payable to bank | $ 250,000 | -- |
| Payments on long-term obligations | (1,024,000) | (393,000) |
| Proceeds from placement of Common Stock | 700,000 | -- |
| Proceeds and tax benefit from stock options | 54,000 | 88,000 |
| Net cash provided by (used in) financing activities | $ (20,000) | $ (305,000) |

| | | |
|---|---|---|
| Effect of foreign currency exchange rate changes on cash and cash equivalents | $ (1,000) | $ 12,000 |
| Increase (decrease) in cash and cash equivalents | $(4,351,000) | $ 1,544,000 |
| Cash and Cash Equivalents | | |
| Beginning | 4,605,000 | 2,860,000 |
| Ending | $ 254,000 | $ 4,404,000 |

</TABLE>

<TABLE>
<CAPTION>

Appliance Recycling Centers of America, Inc. and Subsidiaries
CONSOLIDATED STATEMENTS OF CASH FLOWS - continued
(Unaudited)

| | Six Months Ended June 29, 1996 | July 1, 1995 |
|---|---|---|
| <S> | <C> | <C> |
| Supplemental Disclosures of Cash Flow Information | | |
| Cash payments (receipts) for: | | |
| Interest | $ 136,000 | $ 138,000 |
| Income taxes net of refunds | $ (9,000) | $ 422,000 |
| Supplemental Schedule of Noncash Investing and Financing Activities | | |
| Acquisition of Universal Appliance Company, Inc. and Universal Appliance Recycling, Inc. | | |
| Working capital acquired, including cash and cash equivalents of $26,000 | 118,000 | -- |
| Fair value of other assets acquired, principally property and equipment and a noncompete agreement | 176,000 | -- |
| Value assigned to Goodwill | 302,000 | -- |
| Long-term debt assumed | (207,000) | -- |
| Total consideration, 84,000 shares of Common Stock | $ 389,000 | -- |

</TABLE>

See Notes to Consolidated Financial Statements

Appliance Recycling Centers of America, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Financial Statements - In the opinion of management of the Company, the accompanying unaudited consolidated financial statements contain all adjustments (consisting of only normal, recurring accruals) necessary to present fairly the financial position of the Company and its subsidiaries as of June 29, 1996, and the results of operations for the three-month and six-month periods and its cash flows for the six-month periods ended June 29, 1996 and July 1, 1995. The results of operations for any interim period are not necessarily indicative of the results for the year. These interim consolidated financial statements should be read in conjunction with the Company's annual financial statements and related notes in the Company's Annual Report on Form 10-K for the year ended December 30, 1995.

2. Accrued Expenses

Accrued expenses were as follows:

| | June 29, 1996 | December 30, 1995 |
|---|---|---|
| Vacation | $ 183,000 | $ 171,000 |
| Payroll | 312,000 | 307,000 |
| Customer Deposit | 90,000 | 140,000 |
| Other | 251,000 | 423,000 |

| | |
|---|---|
| $ 836,000 | $1,041,000 |
| ========== | ========== |

PART I: ITEM 2 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis provides information that management believes is relevant to an assessment and understanding of the Company's level of operation and financial condition. This discussion should be read with the consolidated financial statements appearing in Item 1.

RESULTS OF OPERATIONS

Net revenues for the three and six months ended June 29, 1996 were $3,273,000 and $6,333,000, respectively, compared to $4,012,000 and $7,680,000 for the same periods in the prior year. Recycling revenues for the three and six months ended June 29, 1996 decreased by $1,674,000 and $2,631,000, respectively, from the same periods in the prior year. The decreases were primarily due to decreased revenues from contracts with electric utility programs. The Company expects recycling revenues for the last six months of 1996 to decrease when compared to the same period in the prior year but to increase when compared to the first six months of 1996.

Appliance sales for the three and six months ended June 29, 1996 increased by $916,000 and $1,407,000, respectively, over the same periods in the prior year. The increases were primarily due to the Company's expansion of its retail business through a new chain of stores under the name "Encore Recycled Appliances." As of June 29, 1996 the Company had 30 retail locations compared to three as of July 1, 1995 and ten as of January 1, 1996. The Company expects a significant increase in revenues generated from appliance sales compared to the prior year as sales volumes continue to increase at the retail locations. The Company expects to open an additional two to three retail stores during the remaining six months of 1996.

Byproduct revenues for the three months ended June 29, 1996 increased by $19,000 over the same period in the prior year, but decreased by $123,000 for the six months ended June 29, 1996 from the same period in the prior year. The decrease was primarily due to reduced sales of reclaimed chlorofluorocarbons ("CFCs") partially offset by higher sales of scrap metals. The Company expects a small increase in byproduct revenues in the remaining six months of 1996 compared to the first six months of 1996.

Gross profit as a percentage of net revenues decreased to 17.7% for the three months and 12.5% for the six months ended June 29, 1996 from 38.3% for the three months and 36.4% for the six months ended July 1, 1995. The decrease between the three and six months ended June 29, 1996 compared to the same periods in the prior year was primarily due to inefficiencies in the conversion to add appliance reconditioning capabilities to 6 of the Company's 11 recycling centers. Gross profit as a percentage of net revenues increased from 7.3% for the first quarter of 1996 to 17.7% for the second quarter of 1996. The Company expects gross profit as a percentage of revenues to increase in the third and fourth quarters of 1996 when compared to the first and second quarters of 1996 due to improved efficiencies in appliance reconditioning. Due to the expiration of utility contracts and the implementation of cost-cutting programs, four recycling centers were closed in the second quarter of 1996 leaving seven centers open as of June 29, 1996. The Company believes the gross margin rate will continue to improve throughout the remainder of the year. Gross profit margin for any single period, however, will be affected favorably or unfavorably by numerous factors, including volume of appliances recycled, training of personnel, speed at which appliance sales increase, costs incurred in opening new retail stores and the price and volume of byproduct revenues.

Selling, general and administrative expenses for the three and six months ended June 29, 1996 increased to $2,209,000 and $4,256,000, respectively, from $1,417,000 and $2,754,000 in the same periods of 1995. The increases in the three and six months ended June 29, 1996 were primarily due to costs associated with 30 retail stores compared to three retail stores in the same period in the prior year and by a small increase in general and administrative expenses. The Company expects total selling, general and administrative expenses for the last six months of 1996 to be slightly less than the total for the first six months of 1996. The Company expects an increase in selling expenses to be offset by reductions in general and administrative expenses.

Interest income decreased to $4,000 from $56,000 for the three months and to $32,000 from $108,000 for the six months ended June 29, 1996 compared to the same periods in 1995. The decrease in interest income for the three and six months ended June 29, 1996 resulted from lower cash balances when compared to the same periods in the prior year.

Interest expense was $66,000 for the three months and $135,000 for the six months ended June 29, 1996 compared to $67,000 and $139,000 for the same periods in 1995.

During the first six months of 1996, the Company recorded a valuation allowance of approximately $1,390,000, and accordingly, no tax benefit was recorded for the first six months of 1996. $400,000 of the deferred tax assets as of June 29, 1996 will be realized by carrybacks to prior taxable years and the realization of the remaining deferred tax assets is dependent upon future taxable income.

The Company recorded a net loss of $1,606,000 for the three months and $3,498,000 for the six months ended June 29, 1996 compared to a net income of $61,000 and $22,000 in the same periods of 1995. The increase in loss was primarily due to the increased operational expenses and increased selling, general and administrative expenses associated with the development of the Company's retail business. The Company expects losses for the remaining six months of 1996 to continue but to be reduced substantially as utility revenue, appliance sales and byproduct revenue are expected to increase during the last six months of 1996 compared to the first six months of 1996.

LIQUIDITY AND CAPITAL RESOURCES

At June 29, 1996, the Company's working capital was $39,000 compared to $3,503,000 at December 30, 1995. Cash and cash equivalents decreased to $254,000 at June 29, 1996 from $4,605,000 at December 30, 1995. Net cash used in operating activities was $3,252,000 for the six months ended June 29, 1996 compared to net cash provided by operating activities of $2,010,000 in the same period of 1995. The decrease in cash provided by operating activities was primarily due to the net loss from operations and an increase in inventory offset by depreciation and a decrease in accounts receivable. The Company anticipates its net cash used in operating activities will decrease significantly for the remaining six months of 1996 compared to the first six months of 1996 due to anticipated increases in sales and corresponding margins.

The Company's capital expenditures were approximately $1,147,000 and $249,000 for the six months ended June 29, 1996 and July 1, 1995, respectively. The 1996 capital expenditures were primarily related to leasehold improvements to the Company's recycling centers and additional retail stores. The Company had no material purchase commitments for assets as of June 29, 1996.

On January 2, 1996, the Company acquired Universal Appliance Company, Inc. and Universal Appliance Recycling, Inc., Washington, D.C.-based companies, by exchanging a total of 84,000 shares of its Common Stock for 100% ownership of the respective companies. The acquisitions were accounted for as an asset purchase. In addition, selling shareholders can earn up to a total of 100,000 shares of Company stock in contingent consideration over the next four years. Also, the selling shareholders received a total of $110,000 under noncompete agreements.

The Company had a bank line of credit of $2,500,000 which expired in April 1996. The Company had no borrowings under the line. The Company has negotiated a revised bank line of credit in the amount of $400,000 which expires October 1, 1996. Advances under the line are secured by all receivables, are subject to borrowing base requirements, require the Company to meet certain financial covenants, are due on demand and bear interest at three percentage points above the bank's base rate. As of June 29, 1996 the Company was not in compliance with the required financial covenants. The bank's base rate as of June 29, 1996 was 8.25%. As of June 29, 1996 the Company has borrowed $250,000 from the line of credit.

In May 1996, $700,000 was raised in a private placement of Common Stock to an institutional investor that currently holds approximately 15% of the outstanding shares. These proceeds were used to pay off an equipment loan of $480,000 and for additional working capital. The proceeds were raised from selling 200,000 shares at $3.50 each.

The Company anticipates that its current cash balance, existing and anticipated financing, and bank line of credit will be sufficient to finance its operations and capital expenditures during the remainder of 1996. The Company's total capital requirements will depend on the number, size and timing of recycling centers and retail stores added during the year. If the Company does not achieve its planned revenue levels or expenses are higher than anticipated, the Company may require additional capital to finance operations. Sources of additional financing, if needed in the future, may include further debt financing or the sale of equity or other securities.

Statements regarding the Company's operations, performance and results for 1996, including the increase in revenues from utility revenue, appliance sales and byproduct revenue and the improvement of the gross margin rate, discussed herein are forward-looking and therefore are subject to certain risks and uncertainties. Certain events that could significantly affect the 1996 results include the speed at which Encore stores reach profitability, whether new stores are able to attain planned revenue levels, higher than expected costs and expenses (including costs of new store openings and increased equipment costs associated with opening retail stores), recycling programs reaching planned revenue levels, and the availability of sufficient capital to cover start-up and other costs until revenues from operations are available.

## PART II. OTHER INFORMATION

ITEM 1 - LEGAL PROCEEDINGS - None

ITEM 2 - CHANGES IN SECURITIES - None

ITEM 3 - DEFAULTS UPON SENIOR SECURITIES - None

ITEM 4 - SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

On May 2, 1996 the Annual Meeting of the Shareholders of Appliance Recycling Centers of America, Inc. was held to obtain the approval of shareholders of record as of March 15, 1996 in connection with the two matters indicated below. Following is a brief description of each matter voted on at the meeting and the number of votes cast for, against or withheld, as well as the number of abstentions and broker nonvotes, as to each matter:

| Matter | Vote: For | Vote: Withhold Authority |
|---|---|---|
| 1. Election of Directors: | | |
| Edward R. Cameron | 3,721,024 | 19,330 |
| George B. Bonniwell | 3,721,424 | 18,930 |
| Duane S. Carlson | 3,720,524 | 19,830 |
| Harry W. Spell | 3,720,444 | 19,910 |

2. Ratification of McGladrey & Pullen, LLP as independent public accountants for 1996.

| Vote: For | Against | Abstain | Not Voted |
|---|---|---|---|
| 3,710,969 | 11,060 | 18,325 | 0 |

ITEM 5 - OTHER INFORMATION - None

ITEM 6 - EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibit No. 27 - Financial Data Schedule

(b) The Company did not file any reports on Form 8-K during the three months ended June 29, 1996.

## SIGNATURES

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

Appliance Recycling Centers of America, Inc.
Registrant

Date: August 9, 1996 /s/Edward R. Cameron

Edward R. Cameron
President

Date: August 9, 1996 /s/Kent S. McCoy

Kent S. McCoy
Vice President of Finance, Treasurer

```
<TABLE> <S> <C>



<ARTICLE> 5

<S>                             <C>
<PERIOD-TYPE>                   6-MOS
<FISCAL-YEAR-END>                          DEC-28-1996
<PERIOD-END>                               JUN-29-1996
<CASH>                                         254,000
<SECURITIES>                                         0
<RECEIVABLES>                                1,456,000
<ALLOWANCES>                                         0
<INVENTORY>                                    986,000
<CURRENT-ASSETS>                             3,296,000
<PP&E>                                      12,908,000
<DEPRECIATION>                               4,221,000
<TOTAL-ASSETS>                              12,932,000
<CURRENT-LIABILITIES>                        3,257,000
<BONDS>                                              0
<PREFERRED-MANDATORY>                                0
<PREFERRED>                                          0
<COMMON>                                    10,350,000
<OTHER-SE>                                           0
<TOTAL-LIABILITY-AND-EQUITY>                12,932,000
<SALES>                                      6,333,000
<TOTAL-REVENUES>                             6,333,000
<CGS>                                        5,542,000
<TOTAL-COSTS>                                5,542,000
<OTHER-EXPENSES>                              (70,000)
<LOSS-PROVISION>                                     0
<INTEREST-EXPENSE>                             135,000
<INCOME-PRETAX>                            (3,498,000)
<INCOME-TAX>                                         0
<INCOME-CONTINUING>                                 00
<DISCONTINUED>                                       0
<EXTRAORDINARY>                                      0
<CHANGES>                                            0
<NET-INCOME>                               (3,498,000)
<EPS-PRIMARY>                                    (.80)
<EPS-DILUTED>                                    (.80)


</TABLE>
```